



PRELIMINARY DECISION

CitiPower distribution determination 2016–20

Attachment 8 – Corporate income tax

October 2015

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Note

This attachment forms part of the AER's preliminary decision on CitiPower's revenue proposal 2016–20. It should be read with all other parts of the preliminary decision.

The preliminary decision includes the following documents:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Value of imputation credits

Attachment 5 – Regulatory depreciation

Attachment 6 – Capital expenditure

Attachment 7 – Operating expenditure

Attachment 8 – Corporate income tax

Attachment 9 – Efficiency benefit sharing scheme

Attachment 10 – Capital expenditure sharing scheme

Attachment 11 – Service target performance incentive scheme

Attachment 12 – Demand management incentive scheme

Attachment 13 – Classification of services

Attachment 14 – Control mechanism

Attachment 15 – Pass through events

Attachment 16 – Alternative control services

Attachment 17 – Negotiated services framework and criteria

Attachment 18 – f-factor scheme

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Shortened forms

Shortened form	Extended form
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AMI	Advanced metering infrastructure
augex	augmentation expenditure
capex	capital expenditure
CCP	Consumer Challenge Panel
CESS	capital expenditure sharing scheme
CPI	consumer price index
DRP	debt risk premium
DMIA	demand management innovation allowance
DMIS	demand management incentive scheme
distributor	distribution network service provider
DUoS	distribution use of system
EBSS	efficiency benefit sharing scheme
ERP	equity risk premium
Expenditure Assessment Guideline	expenditure forecast assessment Guideline for electricity distribution
F&A	framework and approach
MRP	market risk premium
NEL	national electricity law
NEM	national electricity market
NEO	national electricity objective
NER	national electricity rules
NSP	network service provider
opex	operating expenditure
PPI	partial performance indicators
PTRM	post-tax revenue model
RAB	regulatory asset base
RBA	Reserve Bank of Australia
repex	replacement expenditure

Shortened form	Extended form
RFM	roll forward model
RIN	regulatory information notice
RPP	Revenue and pricing principles
SAIDI	system average interruption duration index
SAIFI	system average interruption frequency index
SLCAPM	Sharpe-Lintner capital asset pricing model
STPIS	service target performance incentive scheme
WACC	weighted average cost of capital

8 Corporate income tax

We are required to make a decision on the estimated cost of corporate income tax for CitiPower's 2016–20 regulatory control period.¹ Under the post-tax framework, a corporate income tax allowance is calculated as part of the building block assessment using our post-tax revenue model (PTRM). This amount enables CitiPower to recover the costs associated with the estimated corporate income tax payable during the 2016–20 regulatory control period.

This attachment presents our assessment of CitiPower's proposed corporate income tax allowance for the 2016–20 regulatory control period. It also presents our assessment of its proposed opening tax asset base (TAB), and the standard and remaining tax asset lives used to estimate tax depreciation for the purpose of calculating tax expenses.

8.1 Preliminary decision

We do not accept CitiPower's proposed cost of corporate income tax allowance of \$130.6 million (\$ nominal). Our preliminary decision on the estimated cost of corporate income tax is \$72.8 million over the 2016–20 regulatory control period. This represents a reduction of \$57.8 million (or 44.2 per cent) compared to its proposal.

The reduction reflects our amendments to some of CitiPower's proposed inputs for forecasting the cost of corporate income tax such as the standard tax asset lives (section 8.4.3) and remaining tax asset lives (section 0). It also reflects changes to the proposed tax treatment of revenue adjustments associated with the EBSS, S factor and share asset schemes (section 8.4.5), and our preliminary decision on the value of imputation credits—gamma—(attachment 4). Changes to building block costs also affect revenues, which in turn impacts the tax calculation. The changes affecting revenues are discussed in attachment 1.

Table 8.1 sets out our preliminary decision on the estimated cost of corporate income tax allowance for CitiPower.

¹ NER, cl. 6.4.3(a)(4).

Table 8.1 AER's preliminary decision on CitiPower's cost of corporate income tax allowance for the 2016–20 regulatory control period (\$ million, nominal)

	2016	2017	2018	2019	2020	Total
Tax payable	26.4	23.8	22.5	23.8	24.9	121.3
Less: value of imputation credits	10.5	9.5	9.0	9.5	9.9	48.5
Net corporate income tax allowance	15.8	14.3	13.5	14.3	14.9	72.8

Source: AER analysis.

8.2 CitiPower's proposal

CitiPower proposed a forecast cost of corporate income tax of 130.6 million (\$ nominal) using the AER's PTRM and the following inputs:²

- an opening TAB as at 1 January 2016 of \$1245.7 million (\$ nominal)
- an expected statutory income tax rate of 30 per cent per year
- a value for gamma of 0.25
- remaining tax asset lives of assets in existence as at 31 December 2015 calculated based on the standard tax asset life for an asset class multiplied by the ratio of the RAB remaining asset life to the RAB standard asset life³
- standard tax asset lives calculated using a weighted average of relevant tax categories from the July 2014 ATO tax ruling (TR 2014/4).⁴

Table 8.2 sets out CitiPower's proposed corporate income tax allowance for the 2016–20 regulatory control period.

Table 8.2 CitiPower's proposed cost of corporate income tax allowance for the 2016–20 regulatory control period (\$ million, nominal)

	2016	2017	2018	2019	2020	Total
Tax payable	34.6	34.0	33.9	34.1	37.5	174.1
Less: value of imputation credits	8.6	8.5	8.5	8.5	9.4	43.5
Net corporate income tax allowance	25.9	25.5	25.4	25.6	28.2	130.6

Source: CitiPower, *Regulatory proposal*, April 2015, Attachment CP 2016-20 PTRM.

² CitiPower, *Regulatory proposal*, April 2015, pp. 2501–251; and Attachment CP 2016-20 PTRM.

³ CitiPower, *Regulatory proposal*, April 2015, p. 251.

⁴ CitiPower, *Regulatory proposal*, April 2015, Attachment CP 2011-15 RFM.

8.3 AER's assessment approach

Under clause 6.5.3 of the National Electricity Rules (NER), we must make an estimate of taxable income for each regulatory year. Our estimate must be for the taxable income a benchmark efficient entity would earn for providing standard control services if it operated CitiPower's business. The estimate is required to be determined in accordance with the PTRM. Our approach for calculating a service provider's cost of corporate income tax allowance is set out in our PTRM and involves the following steps:

1. We estimate the annual taxable income that would be earned by a benchmark efficient entity operating the service provider's business. A service provider's taxable income is calculated by subtracting from the approved forecast revenues the benchmark estimates of tax expenses. Using the PTRM, we model the service provider's benchmark tax expenses, including interest tax expense and tax depreciation, over the regulatory control period. The interest tax expense is estimated using the benchmark 60 per cent gearing used for the rate of return calculation. Tax depreciation is calculated using a separate value for the TAB, and standard and remaining tax asset lives for taxation purposes. All tax expenses (including other expenses such as opex) are offset against the service provider's forecast revenue to estimate the taxable income.
2. The statutory income tax rate is then applied to the estimated annual taxable income (after adjustment for any tax loss carried forward) to arrive at a notional amount of tax payable.
3. We apply a discount to that notional amount of tax payable to account for the utilisation of imputation credits (gamma) by investors.
4. The tax payable net of assumed utilised imputation credits represents the corporate income tax allowance and is included as a separate building block in determining the service provider's annual revenue requirement.

The cost of corporate income tax allowance is an output of our PTRM. We therefore assess the service provider's proposed cost of corporate tax allowance by analysing the proposed inputs to the PTRM for calculating that allowance. These inputs include:

- **The opening TAB as at the commencement of the 2016–20 regulatory control period:** We consider that the roll forward of the opening TAB should be based on the approved opening TAB as at commencement of the 2011–15 regulatory control period and the service provider's actual capex incurred during the 2011–15 regulatory control period.⁵
- **The remaining tax asset life for each asset class at the commencement of the 2016–20 regulatory control period:** For the 2016–20 regulatory control period, CitiPower proposed to transition to the straight-line tax depreciation approach from

⁵ The tax depreciation is therefore recalculated based on actual capex. The same tax depreciation approach of using actual capex applies to the roll forward of the TAB at the next reset.

the diminishing value approach.⁶ This requires the establishment of remaining tax asset lives at 1 January 2016. We have recently approved a method in our determination for Ausgrid to establish remaining tax asset lives for existing assets.⁷ CitiPower's proposal is based on this method to calculate the remaining tax asset life for an asset class. This involves using the standard tax asset life for the asset class multiplied by the ratio of the RAB remaining asset life to the RAB standard asset life. We will assess CitiPower's proposed approach against that approved method.

- **The standard tax asset life for each asset class:** We assess the service provider's proposed standard tax asset lives, where necessary, against those prescribed by the Commissioner for taxation in tax ruling 2015/2 and the approved standard tax asset lives in the service provider's distribution determination for the 2011–15 regulatory control period.
- **The income tax rate:** The statutory income tax rate is 30 per cent per year.
- **The value of gamma:** The gamma input for CitiPower is 0.40. Refer to attachment 4 for detailed discussion on this matter.

We are required to estimate the cost of corporate income tax based on a benchmark efficient entity.⁸ This estimate must be determined in accordance with the manner set out in the PTRM.⁹

8.3.1 Interrelationships

The cost of corporate income tax building block feeds directly into the annual revenue requirement (ARR). This allowance is determined by four factors:

- pre-tax revenues
- tax expenses (including tax depreciation)
- the corporate tax rate
- gamma—the expected proportion of company tax that is returned to investors through the utilisation of imputation credits—which is offset against the corporate income tax allowance. This is discussed further at attachment 4.

Of these four factors, the corporate tax rate is set externally by the Government. The higher the tax rate the higher the required tax allowance.

The pre-tax revenues depend on all the building block components. Any factor that affects revenue will therefore affect pre-tax revenues. Higher pre-tax revenues can

⁶ Our 2011–15 determination for CitiPower did not contain remaining tax asset lives for depreciating its opening TAB at 1 January 2011 as they are not required under the diminishing value approach.

⁷ AER, *Draft decision, Ausgrid distribution determination 2015–16 to 2018–19, Attachment 8: Corporate income tax*, November 2014, pp. 8–17 to 8–19.

⁸ NER, cl. 6.5.3.

⁹ NER, cls. 6.5.3 and 6.4.2(b)(4).

increase the tax allowance.¹⁰ Depending on the source of the revenue increase, the tax increase may be equal to or less than proportional to the company tax rate.¹¹

The tax expenses (or deductions) depend on various building block components and their size. Some components give rise to tax expenses, such as opex, interest payments and tax depreciation of assets. However, others do not, such as increases in return on equity. Higher tax expenses offset revenues as deductions in the tax calculation and therefore reduce the cost of corporate income tax allowance (all things being equal). Tax expenses include:

- Interest on debt – Interest is a tax offset. The size of this offset depends on the ratio of debt to equity and therefore the proportion of the RAB funded through debt. It also depends on the allowed return on debt and the size of the RAB.
- General expenses – In the main these expenses will match the opex allowance.
- Tax depreciation – A separate TAB is maintained for the businesses reflecting tax rules. This TAB is affected by many of the same factors as the RAB, such as capex, although unlike the RAB value it is maintained at its historical cost with no indexation. The TAB is also affected by the depreciation rate and asset lives assigned for tax depreciation purposes.

For CitiPower, a 10 per cent increase in the corporate income tax allowance causes revenues to increase by about 1 per cent. The proposed gamma of 0.25, compared to the value in our preliminary decision of 0.40, would increase the corporate income tax allowance by 32 per cent and total revenues by about 2.5 per cent.

8.4 Reasons for preliminary decision

We do not accept CitiPower's proposed cost of corporate income tax allowance of \$130.6 million (\$ nominal). We have instead determined a cost of corporate income tax allowance of \$72.8 million. This represents a reduction of \$57.8 million (or 44.2 per cent) from CitiPower's proposal.

This is because we adjusted the following proposed inputs to the PTRM for tax purposes:

- the standard and remaining tax asset lives (sections 8.4.3 and 8.4.4 respectively)
- the value of gamma (attachment 4)

¹⁰ In fact, there is an iterative relationship between tax and revenues. That is, revenues lead to tax, being applied, which increases revenues and leads to slightly more tax and so on. The PTRM is therefore set up to run an iterative process until the revenue and tax allowances become stable.

¹¹ For example, although increased opex adds to revenue requirement, these expenses are also offset against the revenues as deductions in determining tax, so there is no net impact in this case. A higher return on equity, in contrast, gives rise to no offsetting tax expenses and therefore increases the tax allowance in proportion to the company tax rate.

- other building block components including forecast opex (attachment 7) and forecast capex (attachment 6) that affect revenues, and therefore also impact the forecast corporate income tax allowance.

We also made changes to CitiPower's proposed tax treatment of revenue adjustments associated with the EBSS and S factor schemes (section 8.4.5).

8.4.1 Transition to straight-line tax depreciation

We accept CitiPower's proposal to use the straight-line depreciation approach to calculate the corporate income tax allowance for the 2016–20 regulatory control period. This is consistent with the approach set out in the PTRM.

CitiPower's corporate income tax allowance for the 2011–15 regulatory control period was calculated based on the diminishing value method. This method was established by the previous regulator, the Essential Services Commission of Victoria (ESCV), and adopted by the AER for the 2011–15 regulatory control period in accordance with clause 11.17.2 (Transitional provisions of specific application to Victoria) of the NER.¹² This transitional rule does not apply for the 2016–20 regulatory control period. Therefore, we accept CitiPower's proposal to transition to our preferred straight-line tax depreciation approach for the 2016–20 regulatory control period.¹³

8.4.2 Opening tax asset base

We accept CitiPower's proposed method to establish the opening TAB as at 1 January 2016 as it is based on the approach approved at the 2010 determination. We also accept CitiPower's proposed opening TAB value as at 1 January 2016 of \$1245.7 million (\$ nominal).¹⁴ We have reviewed the inputs to the TAB roll forward and found that they were correct and reconcile with relevant data sources such as annual reporting RIN and the 2011–15 decision models.¹⁵

We consider that the opening TAB value for land as at 1 January 2016 should be allocated to its own non-depreciating asset class. CitiPower's proposal allocated the closing TAB value of land assets as at 31 December 2015 to its 'Subtransmission' and 'Distribution system assets' asset classes.¹⁶ Allocating this value to these asset classes results in the TAB value of land depreciating over their remaining tax asset lives. We do not consider this appropriate as land is generally considered a non-

¹² AER, *Final decision, Victorian electricity distribution network service providers Distribution determination 2011–2015*, October 2010, pp. 520–521.

¹³ CitiPower, *Regulatory proposal*, April 2015, Attachment CP 2011-15 RFM.

¹⁴ At the time of this preliminary decision, the roll forward of CitiPower's TAB includes estimated capex values for 2015. We will update the 2015 estimated capex values for the substitute (final) decision.

¹⁵ We made one amendment to the proposed value of equity raising cost included in 2011 capex. This amendment resulted in some changes to the tax depreciation profile within the TAB roll forward during the 2011–15 regulatory control. However, the changes did not impact on the proposed closing TAB value at 31 December 2015.

¹⁶ CitiPower, *Regulatory proposal*, April 2015, Attachment CP 2011-15 RFM.

depreciating asset for tax purposes.¹⁷ This is also consistent with the treatment of the 'Land' asset class under the ESCV's approach to tax depreciation. Therefore, we have created a new non-depreciating 'Land' asset class to allocate the TAB value of land as at 1 January 2016.

Table 8.3 sets out our preliminary decision on the roll forward of CitiPower's TAB values over the 2011–15 regulatory control period.

Table 8.3 AER's preliminary decision on CitiPower's TAB roll forward (\$ million, nominal)

	2011	2012	2013	2014	2015 ^a
Opening TAB	775.2	874.1	946.3	1030.8	1128.6
Capital expenditure	155.8	130.2	156.1	171.2	201.8
Less: Tax depreciation	56.8	58.1	71.5	73.5	84.7
Closing TAB	874.1	946.3	1030.8	1128.6	1245.7

Source: AER analysis.

(a) Based on estimated capex.

8.4.3 Standard tax asset lives

We accept CitiPower's proposed standard tax asset lives because they are broadly consistent with the values prescribed by the Commissioner for taxation in tax ruling 2015/2.¹⁸

We are satisfied that the proposed standard tax asset lives are appropriate for applying over the 2016–20 regulatory control period.

We also consider that a standard tax asset life of 'n/a' should be assigned to the new 'Land' asset class for tax modelling purposes in the PTRM reflecting the non-depreciating nature of land capex.¹⁹

Table 8.4 sets out our preliminary decision on the standard tax asset lives for CitiPower.

¹⁷ The Income Tax Assessment Act (ITAA) 1997 excludes land from the definition of a 'depreciating asset' (ITAA 1997, s. 40-30).

¹⁸ ATO, *Taxation Ruling Income tax: effective life of depreciating assets (applicable from 1 July 2015)*, July 2015, <http://law.ato.gov.au/atolaw/view.htm?docid=%22TXR%2FTR20152%2FNAT%2FATO%2F00001%22>, accessed on 29 July 2015.

¹⁹ We note that CitiPower did propose any land capex over the 2016–20 regulatory control period, therefore this change has no impact over that period.

8.4.4 Remaining tax asset lives

Our 2010 determination for CitiPower did not contain remaining tax asset lives for depreciating its opening TAB as at 1 January 2011. Instead, the transitional rules at the time required us to adopt for the 2011–15 regulatory control period the same tax depreciation methodology as used by the ESCV for the 2006–10 regulatory control period.²⁰ As discussed in section 8.4.1, we accept CitiPower's proposal to use the straight-line depreciation approach to calculate the corporate income tax allowance for the 2016–20 regulatory control period. This requires us to determine remaining tax asset lives for depreciating the opening TAB as at 1 January 2016.

We accept CitiPower's proposed approach for calculating the remaining tax asset lives at 1 January 2016. This approach calculates the remaining tax asset life using the standard tax asset life for the asset class multiplied by the ratio of the RAB remaining asset life to the RAB standard asset life. We consider CitiPower's proposed approach provides reasonable estimates of remaining tax asset lives for the majority of CitiPower's asset classes. We also consider that CitiPower's proposed approach aligns the cash flows associated with the estimate of tax depreciation with the expected life of the network. This is because for the majority of asset classes the standard asset lives for CitiPower's RAB are comparable to the standard tax asset lives. We are therefore satisfied that the proposed approach results in an estimate of tax depreciation consistent with the tax expenses used to estimate the annual taxable income of a benchmark efficient entity over the 2016–20 regulatory control period. The proposed approach is consistent with the method approved in our recent determination for Ausgrid.²¹

However, in accepting CitiPower's approach for calculating the remaining tax asset lives as at 1 January 2016, we have updated the inputs to reflect the adoption of the new regulatory depreciation approach, year-by-year tracking, as discussed in attachment 5. CitiPower's approach for calculating the remaining tax asset lives as at 1 January 2016 requires the remaining RAB asset life as at the same date. The change to the year-by-year tracking approach means that the RAB remaining lives are no longer recorded in the PTRM.²² However, we are able to calculate RAB remaining lives as at 1 January 2016 consistent with the year-by-year tracking approach and these are used to calculate the remaining tax asset lives. Having established the remaining tax asset lives as at 1 January 2016 for this determination process, we consider that when rolling forward these remaining tax asset lives to 1 January 2020 at the next reset our preferred weighted average method should be used.

At the time of this preliminary decision, the RAB remaining asset lives used in this calculation include estimated capex values for 2015. We expect to update the 2015

²⁰ AER, *Victorian distribution draft decision 2011–15*, June 2010, p. 552.

²¹ AER, *Draft decision, Ausgrid distribution determination 2015–16 to 2018–19, Attachment 8: Corporate income tax*, November 2014, pp. 8–17 to 8–19.

²² Instead, as set out section 5.4.2, the regulatory depreciation amounts are calculated in a separate model and directly entered into the PTRM.

estimated capex values for the final decision. Therefore, for the final decision, we will update CitiPower's remaining tax asset lives at 1 January 2016 using the method approved in this preliminary decision for any revisions to the RAB remaining asset lives.

As discussed in section 8.4.2, we consider that a remaining tax asset life of 'n/a' should be assigned to the new 'Land' asset class for tax modelling purposes in the PTRM reflecting the non-depreciating nature of land capex.

Table 8.4 sets out our preliminary decision on the remaining tax asset lives at 1 January 2016 for CitiPower. We are satisfied the remaining tax asset lives provide an appropriate estimate of the tax depreciation amount for a benchmark efficient service provider as required by the NER.²³

Table 8.4 AER's preliminary decision on CitiPower's standard and remaining tax asset lives (years)

Asset class	Standard tax asset life	Remaining tax asset lives as at 1 January 2016
Subtransmission	43.0	32.2
Distribution system assets	49.0	26.3
Standard metering	n/a	n/a
Public lighting	n/a	n/a
SCADA/Network control	10.0	6.3
Non-network general assets - IT	4.0	3.4
Non-network general assets - other	12.0	8.6
VBRC	45.0	n/a
Supervisory cables	n/a	n/a
Old SWER ACRs	n/a	n/a
Land	n/a	n/a
Equity raising costs	5.0	n/a

Source: AER analysis.

n/a: not applicable.

8.4.5 Tax treatment of other revenue adjustments

We do not accept CitiPower's proposed tax treatment of the revenue adjustments arising from the operation of the EBSS over the 2011–15 regulatory control period and the close out of the ESCV's previous S factor scheme. The approach is inconsistent

²³ NER, cl. 6.5.3.

with incentives developed for the schemes and the approach used to calculate the revenue adjustments at the 2010 regulatory determination.

CitiPower submitted that the revenues associated with these schemes are not a tax expense for the purposes of tax accounting.²⁴ In CitiPower's proposed PTRM it set the switch for tax expense to 'no' in relation to these revenue adjustments, while recognising the revenues as income for the tax calculation. This approach adds an additional tax penalty or reward to the revenues associated with the schemes. In contrast, if the revenue adjustments are recognised in the PTRM as both income and expenses for tax purposes, no additional tax penalty or reward is calculated.²⁵ An equivalent outcome occurs in the PTRM if the revenue adjustments are completely excluded from the tax calculation, counted as neither tax income nor tax expense.²⁶ In both cases, the sizes of the revenue adjustments reflect the parameters of the scheme only.

We consider that the EBSS and S factor revenue adjustments should be given identical income and expense tax status in the PTRM.²⁷ We consider that such an approach:

- is consistent with the implementation of the EBSS and S factor in the 2010 regulatory determination for CitiPower²⁸
- is consistent with our recently published guidelines on incentive schemes, which were subject to stakeholder consultation²⁹
- is consistent with our application of incentive schemes for all other network service providers to date³⁰
- means that the service provider faces a constant incentive to pursue efficiency gains across the regulatory control period. That is, the service provider obtains the same reward (or penalty) from a given expenditure decrease (increase), regardless

²⁴ CitiPower, *Regulatory proposal 2016–2020*, April 2015, p. 251.

²⁵ This can be done in the PTRM by setting both the tax income and tax expense switches to 'yes'.

²⁶ This can be done in the PTRM by setting both the tax income and tax expense switches to 'no'.

²⁷ As noted above, whether the switches for income: expenses are set 'yes: yes' or 'no: no' for these revenue adjustments brings the same tax outcome.

²⁸ AER, *Final framework and approach paper for Victorian electricity distribution regulation*, CitiPower, Powercor, Jemena, SP AusNet and United Energy, *Regulatory control period commencing 1 January 2011*, May 2009, pp. 103–104, 112–113; AER, *Final decision, Victorian electricity distribution network service providers, Distribution determination 2011–2015*, October 2010, pp. 643–644, 654–658, 708–716; Australian Competition Tribunal, *Application by United Energy Distribution Pty Limited (No 2) [2012] ACompT 8 (5 April 2012)*, paragraphs 24–81.

²⁹ AER, *Better regulation, Efficiency benefit sharing scheme for electricity network service providers*, November 2013; AER, *Better regulation, Capital expenditure incentive guideline for electricity network service providers*, November 2013; and AER, *Better regulation, Shared asset guideline*, November 2013.

³⁰ See for example; AER, *Final decision, New South Wales Distribution determination 2009–10 to 2013–14*, 28 April 2009, p. 208; AER, *Final decision, Australian Capital Territory distribution determination*, 28 April 2009, p. 88; AER, *Final decision, Victorian electricity distribution network service providers distribution determination 2011–2015*, October 2010, p. 520; AER, *Final decision, Queensland distribution determination 2010–11 to 2014–15*, May 2010, p. 229; AER, *Final decision, South Australia distribution determination 2010–11 to 2014–15*, May 2010, p. 163; AER, *Final distribution determination, Aurora Energy Pty Ltd 2012–13 to 2016–17*, April 2012, p. 251.

of which year of the regulatory control period it occurs.³¹ A constant incentive means timing issues associated with the application of regulation do not distort expenditure decisions.

These reasons were discussed in detail in our final decision for Ausgrid.³² We do not repeat the detailed reasoning here. Ausgrid had also proposed to change the tax treatment of scheme revenue adjustments in the PTRM and raised the same issues as CitiPower. Accordingly, no new issues have been raised by CitiPower for us to consider regarding this matter. We have therefore amended the proposed PTRM to recognise the revenue adjustments with consistent tax status across revenues and expenses for the tax calculation in the PTRM.³³

There is a third type of revenue adjustment included in our preliminary decision, arising from revenue received for shared assets. CitiPower did not include this adjustment in its initial proposal because its forecast of shared assets revenue was just below the relevant threshold (1 per cent of the smoothed revenue requirement in any year).³⁴ As set out in attachment 1 of this preliminary decision shared assets revenue now reaches the relevant threshold. It is therefore necessary to specify the tax treatment of the shared asset revenue reduction. We have applied an approach that achieves the same tax outcome as for the EBSS and S factor by effectively excluding the amounts from the tax calculation. This tax treatment for shared assets revenue is consistent with the fixed proportion of shared assets revenue specified in our guideline.³⁵

Given the overall negative revenue adjustments determined for CitiPower for the 2016–20 regulatory control period, the changes in this preliminary decision add a small additional tax allowance (about \$0.4 million) that would not have been included under CitiPower’s proposed approach.³⁶

³¹ In contrast, CitiPower’s proposal would distort this incentive by providing a greater reward (penalty) to the business for expenditure decreases (increases) in later years of the regulatory control period.

³² AER, *Final decision, Ausgrid distribution determination 2015–16 to 2018–19, Attachment 8 – Corporate income tax*, April 2015, pp. 8–18.

³³ That is, the revenue adjustments are either both tax income and tax expense (EBSS, shared assets); or neither tax income nor tax expense (S factor).

³⁴ CitiPower, *Regulatory proposal 2016–2020*, April 2015, p. 250.

³⁵ AER, *Better regulation, Shared asset guideline*, November 2013, p. 20.

³⁶ CitiPower has a small positive S factor revenue adjustment, but this is offset by the larger negative EBSS and shared asset revenue adjustments.