

23 November 2018

Mr Warwick Anderson
General Manager, Network Finance and Reporting
Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Dear Mr Anderson

AER discussion paper on review of regulatory tax approach

Evoenergy welcomes the opportunity to provide a submission in response to the Australian Energy Regulator's (AER's) discussion paper of 2 November 2018 (the discussion paper) on the AER's current review of regulatory tax approach (the tax review).

Evoenergy voluntarily provided information requested by the AER on its taxation arrangements, which formed the basis for the paper, as well as responding as required to the AER regulatory information notice (RIN).

Evoenergy is a member of Energy Networks Australia (ENA) and fully supports the ENA's submission on this matter, specifically:

- The efficient benchmark approach should be maintained within the incentive-based regulatory framework. Under this approach, it is the actions of the benchmark efficient operator that are relevant to estimating efficient tax expenses.
- The statutory tax rate should be retained given that few entities face a different tax rate and there is no obvious alternative.
- Diminishing value depreciation may be appropriate if it reflects the approach that would be adopted by the benchmark efficient firm in the relevant circumstances. However, it should not be assumed that diminishing value tax depreciation should be applied to all assets. Any change should be prospective, applying to new assets only.
- Internal consistency requires that the same approach be used for gearing and the return on debt when determining the allowed rate of return and the corporate tax allowance.
- No change should be made to the treatment of refurbishments without proper consultation and analysis of this issue given the complexities and materiality involved.

Evoenergy is currently finalising its revised regulatory proposal, due for submission by 29 November 2018, in anticipation of the AER's ACT distribution network determination for the regulatory control period beginning 1 July 2019 (the AER's final determination is due 30 April 2019). The AER has indicated a preference for ensuring that any amendments to the regulatory tax approach would, where practicable, apply to Evoenergy and other distribution businesses at the same point in the regulatory cycle. Evoenergy would expect to be adequately consulted in this context on any proposed changes to tax arrangements if they are to form part of its regulatory determination for the 2019-24 regulatory control period.

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Given that some issues raised in the AER's discussion paper require further consideration, including analysis of the RIN data and consideration of interest expenses (the discussion paper does not make any decisions on this very material issue), Evoenergy seeks assurance that the AER's proposed process will provide a reasonable opportunity for the necessary consultation.

In relation to the estimation of tax expenses in Evoenergy's 2019-24 regulatory determination, Evoenergy is particularly concerned about the potential treatment of a large mandated Commonwealth Government project to be undertaken during the upcoming regulatory period. While the project would be fully funded, the tax implications are significant given the mismatch between the timing of when revenues and costs are recognised for tax purposes.

At this time, planning for the project is in preliminary stages and Evoenergy would not expect to be able to satisfy requirements for an efficiency and prudence test. However, the delivery and timing of the project are mandated by government and are outside of Evoenergy's control. If the AER were to exclude this project from the 2019-24 regulatory determination, then Evoenergy has no ability to recover the relevant tax expenses. Rather, tax expenses in future regulatory periods would be reduced as the tax asset base will be rolled-forward in the subsequent regulatory period using actual capex. Evoenergy seeks the AER's views on how it will address such issues.

Finally, Evoenergy notes the AER's email of 19 November 2019 to Evoenergy seeking views on the process for implementing model changes in time for Evoenergy's final determination in April 2019. The email seeks comment on implementation matters including information available that would allow identification of capex that may be subject to immediate expensing, and asset classes currently using a diminishing value depreciation approach for tax purposes. As stated above, there appear to be a number of issues raised in the AER's discussion paper that require further consideration and analysis, including how the AER intends to take the individual circumstances of DNSPs into account while adopting the benchmark efficient entity approach. Evoenergy anticipates that the AER will clarify its proposed approach in its final report. While Evoenergy will actively engage in any process for determining model changes, it is difficult to provide information that may assist the AER, or comment on the process, without a clear understanding of the AER's proposal.

If you wish to discuss any aspect of our response, please do not hesitate to contact Chris Bell, Manager Regulatory Pricing Review on [REDACTED] or chris.bell@actewagl.com.au

Yours sincerely,

[REDACTED]
Dean Ward
Acting Chief Finance Officer