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Recovery of tax on capital contributions

As of 1 May 2014, there will be a change to the way Western Power recovers taxation costs arising from capital contributions.

A capital contribution includes any work we perform for a customer and receive cash for the works undertaken. It also includes any work completed by a third party, which is then is given or gifted to us to operate and maintain.

For local governments, this includes relocations, street lighting, new revenue projects, built strata, network extensions and pole-to-pillar.

Western Power incurs a tax liability because capital contributions are treated as income under the National Tax Equivalents Regime (NTER).

Up until now we have not been recovering the tax liability, creating a shortfall in operating cash flow revenue. As part of our Third Access Arrangement, we proposed these tax costs should be recovered through the AA3 target revenue.

In its final decision, the ERA determined costs should be recovered directly from the customer that makes the contribution. The ERA considers this 'user pays' approach more economically efficient.

Since receiving this decision we have been working closely with members of your industry on the implementation of this charge.

The cost to contributors will be 13.9 per cent of the value of the cash contribution or gifted asset. This figure has been independently endorsed by Ernst and Young.

The change will affect *any new applications received after 1 May 2014.*

For more information a FAQ can be found online at www.westernpower.com.au/aboutus/Recovering_tax_on_capital_contributions_.html or you can call us on 13 10 87.

westernpower

13 13 51 (24 hours)

INFOPAGE

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To:	Chief Executive Officer	**From:**	Paul Schollum
Organisation:	All Councils	**Date:**	4 April 2014
Reference:	05-042-02-0001		
Subject:	Western Power Capital Contributions policy	**Priority:**	Medium

IN BRIEF

Operational Area:	**Infrastructure**
Key Issues:	• Western Power incurs a tax liability when it receives capital contributions, e.g., cash contributions and gifted assets. • From May 1 2014, Western Power will commence recovering this tax liability at the rate of 13.9% on the value of capital contributions.
Action Required:	**None**

Developers construct assets that are required to extend the Western Power grid to their end customers and then vest these assets to Western Power. Local Governments also often gift assets to Western Power, for example, infrastructure associated with the State Underground Power Program.

Australian tax rules treat such capital contributions as revenue in the year in which they are received; therefore, Western Power incur a tax liability on these amounts. Previously, Western Power has absorbed this cost. Following consultation and review by the Economic Regulation Authority (ERA), Western Power concluded that it is more appropriate for these costs to be passed onto the customer requesting the work.

The ERA is the independent economic regulator for Western Australia and one of its key roles is to review and approve the access arrangement for Western Power's electricity network. The access arrangement covers terms, conditions and prices for the services sought by users of the network. The access arrangement also sets a cap on Western Power's revenue for the period of the arrangement. In setting the current access arrangement, the ERA ruled that no amounts in relation to tax on capital contributions may be included in Western Power's target revenue. The ERA made this ruling because:

> Western Power does have a tax liability associated with a contribution, but given the objective of economic efficiency and the associated principal of 'user pays', this should be recovered from the

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contributor – to do otherwise would lead to a subsidy from the existing customer base to the contributing entity[1].

Subsequently, Western Power has developed a new policy stating that it may recover an amount, equivalent to its forecast of the net tax liability it will incur on gifted assets, from those making such capital contributions. Western Power has proposed to recover this tax liability at the rate of 13.9% on the value of capital contributions (this figure incorporates a number of considerations, including the tax benefit Western Power gains from depreciation). Western Power has also indicated they will start recovering this amount from contributors from 1 May 2014 – note that the policy will not be applied retrospectively to capital contributions made before this date.

The recovery of the tax will also impact Local Governments involved in projects where assets are to be gifted to Western Power.

Financial planning for any such projects will now need to include additional costs due to the charges Western Power intends to use to recover its tax liability on these assets.

If you have any comments or questions on this policy please contact Paul Schollum, Policy Manager – Economics, using the details below. More information on the policy can also be found here:
http://www.westernpower.com.au/documents/aboutus/accessarrangement/2012/Contributions_policy.pdf

[1] Economic Regulation Authority 2012, *Further Final Decision on Proposed Revisions to the Access Arrangement for the Western Power Network*. Retrieved from http://www.erawa.com.au/cproot/10987/2/20121129%20-%20D96106%20-%20Further%20Final%20Decision%20on%20Proposed%20Revisions%20to%20the%20Access%20Arrangement%20for%20the%20Western%20Power%20Network.PDF