2019/20 TAX REPORT

Transmission & Distribution RP6 Price Control

01 July 2022

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1. LICENCE REQUIREMENT

Paragraph 12.35 of Annex 2 of Northern Ireland Electricity Ltd's Electricity Distribution and Participate in Transmission Licences requires NIE Networks to furnish the Utility Regulator with an annual tax report which sets out the following:

a) audited tax reports that enables a full reconciliation between:
   i. information submitted to HMRC on the Licensee's tax affairs; and
   ii. Information used for the calculation of the tax element of the Licensee's Maximum Regulated Distribution / Transmission Revenue, as calculated at paragraph 9 of Annex 2 of the Licences;
b) information submitted to HMRC on the Licensee's tax affairs;
c) information used for the calculation of the tax element of the Licensee's Maximum Regulated Distribution / Transmission Revenue, as calculated at paragraph 9 of Annex 2 of the Licences; and
d) any retrospective adjustments in respect of previous years together with any restatement of 12.35 (a), 12.35 (b) and 12.35 (c).

This audited report has been designed to fulfil this licence requirement. Sections 2 to 6 address the requirements of Paragraphs 12.35 (a), 12.35 (b) and 12.35 (c) and Section 7 addresses the requirement of Paragraph 12.35 (d).

The Licence requirements above are effective for the RP6 price control period. The RP6 price control spans six and a half years from October 2017 – March 2024.

Note that all figures in this report are in nominal prices.

2. TRANSMISSION TAX ENTITLEMENT

2019/20 Tax calculation

The following paragraphs set out the calculation of the tax amount included within Transmission Entitlement for the regulatory reporting year 2019/20.

Tax Amount – TAX_t

The maximum regulated transmission revenue for NIE Networks is set out in Paragraph 3.5 of Annex 2 of the Transmission Licence. This formula is as follows:

$$RP6R_t = DEP_t + RET_t + BD_t + O_t + P_t + TAX_t + K_t$$

TAX_t is one of the components of allowed revenue and is calculated in accordance with the following formula set out in Paragraph 9.1 of Annex 2:

$$TAX_t = TR_t / (1 - TR_t) * (RET_t + DEP_t - INT_t - CA_t)$$

Tax Rate – TR_t

TR_t represents the corporation tax rate applicable in Northern Ireland as specified by HMRC which in 2019/20 is 19%. The tax factor $TR_t / (1 - TR_t)$ is therefore 23.5%.

Return Amount – RET_t

RET_t represents the return on the Regulatory Asset Base (RAB). It is calculated by taking the average value of the opening ($ORAB\_X_t$) and closing ($CRAB\_X_t$) values of the individual RABs and multiplying them by the adjusted vanilla weighted average cost of capital ($AVWACC_t$). The formula for calculating RET_t is set out in Paragraph 5.1 of Annex 2:

$$RET_t = \left(\sum_{\text{All RAB\_X}} (ORAB\_X_t + CRAB\_X_t) / 2 \right) * AVWACC_t$$

In 2019/20 the average value of all Transmission RABs is £352m and the adjusted vanilla WACC is 3.092%. The RET_t value for 2019/20 is therefore **£10.886m**.

Depreciation amount – DEP_t

DEP_t represents the depreciation amount and is calculated in accordance with the formula set out in Paragraph 4.43 of Annex 2:

$$DEP_t = \sum_{\text{All RAB\_X}} (DEPADD\_X_t + FDEP\_X_t)$$

$DEPADD\_X_t$ represents the depreciation amount for capex incurred on network assets from 1 October 2017 onwards.

$FDEP\_X_t$ represents the depreciation amount of capex incurred on network assets prior to 30 September 2017.

The DEP_t value for 2019/20 is **£17.001m**.

Interest amount – INT_t

INT_t means an amount equal to the interest on the value of the average of all Transmission RABs calculated in accordance with the following formula set out in Paragraph 9.1 of Annex 2:

$$INT_t = \left(\sum_{All\ RAB\_X} (ORAB\_X_t + CRAB\_X_t) / 2 \right) * G * NCOD$$

Where: G represents notional gearing and has a value of 45%

NCOD represents a notional nominal cost of debt with a value of 4.89%.

In 2019/20 the average value of all Transmission RABs is £352m which equates to an INT_t figure of **£7.751m**.

Regulatory capital allowances – CA_t

CA_t represents the value of capital allowances calculated in accordance with guidelines published by HMRC. There are three main groupings or 'pools' used in the calculation of capital allowances; a) a long-life asset pool, b) a general pool and c) a deferred revenue pool. There are three pools because different types of assets attract different capital allowance percentages.

Each pool is classed as follows:

Capital Allowance Pool	Useful economic life	Capital allowance rate for 2019/20	Comments
Long-life asset pool	25 years or greater	6% reducing balance	This includes transmission and renewables 40-year capex and tree cutting capex.
General pool	Less than 25 years	18% reducing balance	This includes non-network IT capex.
Deferred revenue pool	N/A	2.5% straight line	This represents the proportion of capital expenditure which is classified as non-load related expenditure where we are replacing worn assets on a like-for-like basis or the nearest modern equivalent basis

The classification of capital expenditure for tax purposes across various tax pools is determined by tax legislation and HMRC working agreements.

CA_t is calculated by taking the opening written down value of the various capital allowance pools for the relevant year. Capital additions are then added to the opening value to give a total value on which capital allowances can be claimed for that year. The capital allowance figure is then deducted to give the closing written down value (WDV) which becomes the opening value for the next year.

The opening WDVs for 2019/20 are set out in Table 4 of the Apr 18 – Mar 19 Tax Report and shown in Table 1.

Table 1: 2019/20 Opening Written Down Values

Pool	£m
Long-life asset pool	138.573
General pool	1.508
Deferred revenue pool	38.784
Cumulative additions for Deferred Revenue Pool	48.366

Regulatory additions

The statutory capex additions for Transmission in 2019/20 are £17.578m. Regulatory additions are £16.225m which includes a capex incentive adjustment of £0.386m. The reconciliation of statutory capex additions to regulatory additions is shown in Table 2 below.

Table 2: Reconciliation of Statutory Capex to Regulatory Additions

Ref	Description	£m
A	Gross Statutory Capex per “Rec 2 – Capex” of Financial Data RIGs	17.578
	Items included in Regulatory Additions but not in Statutory Capex Additions	
B	Customer Contributions - Approved Generation Cluster Infrastructure	(1.685)
C	D5 Mechanism Costs (opex costs included within qualifying capex)	(0.001)
	Items in Statutory Capex additions but not included in Regulatory Additions	
D	Legacy RP5 Dt Items	(0.053)
E	**Total Regulatory Additions**	**15.839**
F	Capex Incentive Adjustment	0.386
G	**Total Regulatory Additions (Including Capex Incentive)**	**16.225**

This Regulatory additions figure is then adjusted for non qualifying capex items to give capital additions eligible for capital allowances of £15.940m. This is then split across the three tax pools, as shown in Table 3 in line with HMRC guidance.

Table 3: Allocation of Additions by Capital Allowance Pool

Ref	Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
		£m	£m	£m	£m
A	Regulatory Additions	12.660	0.266	2.913	**15.839**
B	Capex Incentive Adjustment	0.241	0.145	-	**0.386**
C	Adjustment for Non-Qualifying Capex	(0.285)	-	-	**(0.285)**
D	**Total Additions for TAX_t Capital Allowances**	**12.616**	**0.412**	**2.913**	**15.940**

The capex additions are then added to the opening WDV and capital allowances are calculated. Table 4 sets out the capital allowances used in the calculation of regulated revenue entitlement for 2019/20.

Table 4: 2019/20 Capital Allowance Calculation

Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
	£m	**£m**	**£m**	**£m**
Opening WDV @ 01/04/2019	138.573	1.508	38.784	**178.866**
Additions (Table 3)	12.616	0.412	2.913	**15.940**
Adjusted WDV	151.189	1.920	41.697	**194.806**
Capital Allowances	(9.071)	(0.346)	(1.281)	**(10.698)**
Closing WDV @ 31/03/2020	**142.118**	**1.574**	**40.416**	**184.108**
Capital Allowance Rate	6% Reducing Balance	18% Reducing Balance	2.5% Straight Line	
Deferred Revenue Pool				
Cumulative Additions to 01/04/2019			48.336	
Additions			2.913	
Cumulative Additions to 31/03/2020			51.249	
Capital Allowances			**1.281**	

The CA_t amount for 2019/20 is **£10.698m**.

Calculation of TAX_t

When the various components of TAX_t are inserted into the licence formula, the value of TAX_t for 2019/20 is **£2.214m** as detailed in Table 5 below.

$$TAX_t = TR_t / (1 – TR_t) * (RET_t + DEP_t – INT_t – CA_t)$$

Table 5: Calculation of TAX_t

Formula	£m
Return on RAB – RET_t	10.886
RAB Depreciation – DEP_t	17.001
Less Interest – INT_t	(7.751)
Less Capital Allowances – CA_t	(10.698)
	9.438
Tax Factor – TR_t / (1 - TR_t)	23.5%
Tax Entitlement – TAX_t	**2.214**

3. DISTRIBUTION TAX ENTITLEMENT

2019/20 Tax calculation

The following paragraphs set out the calculation of the tax amount included within Distribution Entitlement for the regulatory reporting year 2019/20.

Tax Amount – TAX_t

The maximum regulated distribution revenue for NIE Networks is set out in Paragraph 3.5 of Annex 2 of the Distribution Licence. This formula is as follows:

$$RP6R_t = DEP_t + RET_t + BD_t + RI_t + O_t + P_t + TAX_t - RPSI_t + K_t$$

TAX_t is one of the components of allowed revenue and is calculated in accordance with the following formula set out in Paragraph 9.1 of Annex 2:

$$TAX_t = TR_t / (1 - TR_t) * (RET_t + DEP_t - INT_t - CA_t)$$

Tax Rate – TR_t

TR_t represents the corporation tax rate applicable in Northern Ireland as specified by HMRC which in 2019/20 is 19%. The tax factor $TR_t / (1 - TR_t)$ is therefore 23.5%.

Return Amount – RET_t

RET_t represents the return on the Regulatory Asset Base (RAB). It is calculated by taking the average value of the opening ($ORAB\_X_t$) and closing ($CRAB\_X_t$) values of the individual RABs and multiplying them by the adjusted vanilla weighted average cost of capital ($AVWACC_t$). The formula for calculating RET_t is set out in Paragraph 5.1 of Annex 2:

$$RET_t = \left(\sum_{\text{All RAB\_X}} (ORAB\_X_t + CRAB\_X_t) / 2 \right) * AVWACC_t$$

In 2019/20 the average value of all Distribution RABs is £1,244m and the adjusted vanilla WACC is 3.092%. The RET_t value for 2019/20 is therefore **£38.472m**.

Depreciation amount – DEP_t

DEP_t represents the depreciation amount and is calculated in accordance with the formula set out in Paragraph 4.60 of Annex 2:

$$DEP_t = \sum_{\text{All RAB\_X}} (DEPADD\_X_t + FDEP\_X_t)$$

$DEPADD\_X_t$ represents the depreciation amount for capex incurred on network assets from 1 October 2017 onwards.

$FDEP\_X_t$ represents the depreciation amount of capex incurred on network assets prior to 30 September 2017.

The DEP_t value for 2019/20 is **£78.259m**.

Interest amount – INT_t

INT_t means an amount equal to the interest on the value of the average of all Distribution RABs calculated in accordance with the following formula set out in Paragraph 9.1 of Annex 2:

$$INT_t = \left(\sum_{\text{All RAB\_X}} (ORAB\_X_t + CRAB\_X_t) / 2 \right) * G * NCOD$$

Where: G represents notional gearing and has a value of 45%

NCOD represents a notional nominal cost of debt with a value of 4.89%.

In 2019/20 the average value of all Distribution RABs is £1,244m which equates to an INT_t figure of **£27.394m**.

Regulatory capital allowances – CA_t

CA_t represents the value of capital allowances calculated in accordance with guidelines published by HMRC. There are three main groupings or 'pools' used in the calculation of capital allowances; a) a long-life asset pool, b) a general pool and c) a deferred revenue pool. There are three pools because different types of assets attract different capital allowance percentages.

Each pool is classed as follows:

Capital Allowance Pool	Useful economic life	Capital allowance rate for 2019/20	Comments
Long-life asset pool	25 years or greater	6% reducing balance	This includes distribution 40-year capex, tree cutting capex and domestic contributions.
General pool	Less than 25 years	18% reducing balance	This includes metering, market opening and IT capex.
Deferred revenue pool	N/A	2.5% straight line	This represents the proportion of capital expenditure which is classified as non-load related expenditure where we are replacing worn assets on a like-for-like basis or the nearest modern equivalent basis

The classification of capital expenditure for tax purposes across various tax pools is determined by tax legislation and HMRC working agreements.

CA_t is calculated by taking the opening written down value of the various capital allowance pools for the relevant year. Capital additions are then added to the opening value to give a total value on which capital allowances can be claimed for that year. The capital allowance figure is then deducted to give the closing written down value (WDV) which becomes the opening value for the next year.

The opening WDVs for 2019/20 are set out in Table 4 of the Apr 18 – Mar 19 Tax Report and shown in Table 6.

Table 6: 2019/20 Opening Written Down Values

Pool	£m
Long life asset pool	398.688
General pool	65.021
Deferred revenue pool	229.576
Cumulative additions for Deferred Revenue Pool	278.968

Regulatory additions

The statutory capex additions for Distribution in 2019/20 are £119.361m. Regulatory additions are £95.220m which includes a capex incentive adjustment of (£0.498m). The reconciliation of statutory capex additions to regulatory additions is shown in Table 7 below.

Table 7: Reconciliation of Statutory Capex to Regulatory Additions

Ref	Description	£m
A	Gross Statutory Capex per "Rec 2 – Capex" of Financial Data RIGs	119.361
	Items included in Regulatory Additions but not in Statutory Capex Additions	
B	Customer Contributions - Housing sites with 12 or more Domestic Premises	(4.610)
C	IT Contestability opex costs recovered through Regulatory additions	0.003
	Items in Statutory Capex additions but not included in Regulatory Additions	
D	Connection expenditure: Various other Connections categories	(19.036)
E	**Total Regulatory Additions**	**95.718**
F	Capex Incentive Adjustment	(0.498)
G	**Total Regulatory Additions (Including Capex Incentive)**	**95.220**

This Regulatory additions figure is then adjusted for items such as asset disposals and non qualifying capex to give additions that are eligible for capital allowances of £92.602m. This is then split across the three tax pools, as shown in Table 8, in line with HMRC guidance.

Table 8: Allocation of Additions by Capital Allowance Pool

Ref	Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
		£m	£m	£m	£m
A	Regulatory Additions	61.198	13.158	21.362	**95.718**
B	Capex Incentive Adjustment	(1.349)	0.851	-	**(0.498)**
C	Asset Disposals	(0.055)	-	-	**(0.055)**
D	Non-Qualifying Capex	(2.563)	-	-	**(2.563)**
E	**Total Additions for TAX_t Capital Allowances**	**57.231**	**14.009**	**21.362**	**92.602**

The capex additions are then added to the opening WDV and capital allowances are calculated.

Table 9 sets out the capital allowances used in the calculation of regulated revenue entitlement for 2019/20.

Table 9: 2019/20 Capital Allowance Calculation

Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
	£m	£m	£m	£m
Opening WDV @ 01/04/2019	398.688	65.021	229.576	**693.285**
Additions (Table 8)	57.231	14.009	21.362	**92.602**
Adjusted WDV	455.919	79.030	250.938	**785.887**
Capital Allowances	(27.355)	(14.225)	(7.508)	**(49.089)**
Closing WDV @ 31/03/2020	**428.564**	**64.805**	**243.429**	**736.798**
Capital Allowance Rate	6% Reducing Balance	18% Reducing Balance	2.5% Straight Line	
Deferred Revenue Pool				
Cumulative Additions to 01/04/2019			278.968	
Additions			21.362	
Cumulative Additions to 31/03/2020			300.330	
Capital Allowances			**7.508**	

The CA_t amount for 2019/20 is **£49.089m**.

Calculation of TAX_t

When the various components of TAX_t are inserted into the licence formula, the value of TAX_t for 2019/20 is **£9.441m** as detailed in Table 10 below.

$$TAX_t = TR_t / (1 – TR_t) * (RET_t + DEP_t – INT_t – CA_t)$$

Table 10: Calculation of TAX_t

Formula	£m
Return on RAB – RET_t	38.472
RAB Depreciation – DEP_t	78.259
Less Interest – INT_t	(27.394)
Less Capital Allowances – CA_t	(49.089)
	40.248
Tax Factor – TR_t / (1 - TR_t)	23.5%
Tax Entitlement – TAX_t	**9.441**

4. COMPARISON OF TAX ENTITLEMENT TO STATUTORY TAX

NIE Networks submits statutory tax returns to HMRC in line with its statutory year end which is on a calendar year basis. For the regulatory period 2019/20, consideration needs to be given to the tax returns filed by NIE Networks for both calendar years 2019 and 2020.

Table 11 below shows the comparison of Tax Entitlement calculated above and statutory tax paid. As the information contained within the tax returns does not specify between Transmission and Distribution the entitlement amount is collated into a combined Transmission and Distribution view.

Table 11: Comparison of Tax Entitlement and Tax Paid for RP6

Period	Oct 17 – Mar 18	Apr 18 – Mar 19	Apr 19 – Mar 20	Total
	£m	**£m**	**£m**	**£m**
Tax Entitlement – TAX_t - Transmission (Table 5)[1]	0.693	1.428	2.214	4.334
Tax Entitlement – TAX_t - Distribution (Table 10)[1]	3.774	7.104	9.441	20.318
Total Tax Entitlement	4.466	8.531	11.655	24.652
Tax amount per Tax computation	7.914	9.275	14.798	31.986
Variance	**(3.448)**	**(0.744)**	**(3.143)**	**(7.334)**

The total variance for the period Oct 2017 to Mar 2020 above is explained in Table 12 below.

Table 12: Reconciliation of Tax Entitlement to Statutory Tax for RP6

Period	Oct 17 – Mar 20	Comment
	£m	£m
Capital Allowances	0.537	At 1 April 2017 the opening pool figure for capital allowances was similar in the Regulatory Entitlement model and the statutory tax pool. However, in the regulatory model, the general pool was lower which has resulted in lower capital allowances which means a higher tax entitlement allowance than the statutory tax paid. This has been offset by the long-life pool being higher in the regulatory model. The differences have arisen due to the differences in the treatment of capital additions as detailed in Sections 5 and 6 of this and previous reports.
Pension Deficit	0.885	Difference due to the ERDC disallowance of Pension deficit contributions.
Income / Opex Differences	(8.192)	This mainly relates to timing differences between actual income received and regulatory entitlement.
Interest Amount	1.152	Differences between notional interest in the tax entitlement calculation and actual interest paid.
Reliability Incentive	(1.140)	Entitlement for the Reliability incentive is not included within the tax entitlement calculation.
Other	(0.576)	Relates to other minor adjustments within the tax return.
Variance	**(7.334)**	

[1] Relates to Tables 5 and 10 from the specific year's Tax Report.

There is a seasonality to the Distribution element of NIE Networks income. This impacts the analysis above as the regulatory year 2017/18 crosses two price control periods. ***Table 13*** and

Table 14 show the comparison of Tax Entitlement calculated above and statutory tax paid including the full regulatory year Apr 17 – Mar 2018.

Table 13: Comparison of Tax Entitlement and Tax Paid (including full year 2017/18)

Period	Apr 17 – Mar 18	Apr 18 – Mar 19	Apr 19 – Mar 20	Total
	£m	**£m**	**£m**	**£m**
Tax Entitlement – TAX_t - Transmission (Table 11)[2]	1.244	1.428	2.214	**4.886**
Tax Entitlement – TAX_t - Distribution (Table 11)[2]	7.021	7.104	9.441	**23.565**
Total Tax Entitlement	8.265	8.531	11.655	**28.451**
Tax amount per Tax computation	6.946	9.275	14.798	**31.019**
Variance	**1.319**	**(0.744)**	**(3.143)**	**(2.568)**

Table 14: Reconciliation of Tax Entitlement to Statutory Tax (including full year 2017/18)

Period	Apr 17 – Mar 20
	£m
Capital Allowances	0.445
Pension Deficit	1.068
Income / Opex Differences	(2.948)
Interest Amount	(0.757)
Reliability Incentive	(1.140)
Other	(0.750)
Variance	**(2.568)**

[2] Refer to Table 13 of Oct 17 – Mar 18 report for Apr 17 – Mar 18 figures

5. ANALYSIS OF CAPITAL ADDITIONS IN TAX RETURNS

The capital additions eligible for capital allowances and the analysis across the various pools in the submitted tax returns are shown in Table 15 and Table 16 below.

Table 15: Analysis of Capital Additions in 2019 Tax Return

Ref Period	A Jan – Mar 19	B Apr – Dec 19	C Jan – Dec 19
Gross Additions	**£m**	**£m**	**£m**
Total Capex Additions per Tax Returns	33.464	102.136	135.600
Less: Total Customer Capital Contributions	(4.736)	(17.550)	(22.286)
Total Net Capex Additions	28.728	84.586	113.314
Add: Domestic Capital Contributions	1.288	4.107	5.395
Total Net Additions eligible for Capital Allowances	**30.017**	**88.691**	**118.709**
Analysis for tax purposes			
Long Life Asset Pool	19.476	57.361	76.837
General Pool	3.693	10.789	14.482
Deferred Revenue Pool	6.113	18.338	24.450
Non-Qualifying Capex	0.735	2.205	2.940
Total	**30.017**	**88.692**	**118.709**

Table 16: Analysis of Capital Additions in 2020 Tax Return

Ref Period	D Jan – Mar 20	E Apr – Dec 20	F Jan – Dec 20
Gross Additions	**£m**	**£m**	**£m**
Total Capex Additions per Tax Returns	34.803	88.184	122.987
Less: Total Customer Capital Contributions	(6.657)	(19.047)	(25.704)
Total Net Capex Additions	28.145	69.137	97.283
Add: Domestic Capital Contributions	1.275	6.086	7.361
Total Net Additions eligible for Capital Allowances	**29.421**	**75.223**	**104.644**
Analysis for tax purposes			
Long Life Asset Pool	19.592	44.015	63.607
General Pool	3.249	11.468	14.717
Deferred Revenue Pool	5.938	17.813	23.750
Non-Qualifying Capex	0.643	1.928	2.570
Total	**29.421**	**75.223**	**104.644**

The information in Table 15 for the 9 month period Apr – Dec 2019 and Table 16 for the 3 month period Jan – Mar 2020 is combined to show the analysis of the Regulatory period 2019/20 in Table 17.

Table 17: Analysis of 2019/20 per tax returns

Ref Period	Table 15 – B Apr – Dec 19	Table 16 – D Jan – Mar 20	G Apr – Mar 20
Gross Additions	**£m**	**£m**	**£m**
Total Capex Additions per Tax Returns	102.136	34.803	136.938
Less: Total Customer Capital Contributions	(17.550)	(6.657)	(24.207)
Total Net Capex Additions	84.586	28.145	112.217
Add: Domestic Capital Contributions	4.107	1.275	5.382
Total Net Additions eligible for Capital Allowances	**88.692**	**29.421**	**118.113**
Analysis for tax purposes			
Long Life Asset Pool	57.361	19.592	76.953
General Pool	10.789	3.249	14.038
Deferred Revenue Pool	18.338	5.938	24.275
Non-Qualifying Capex	2.205	0.643	2.848
Total	**88.692**	**29.421**	**118.113**

6. RECONCILIATION OF REGULATORY CAPITAL ALLOWANCES TO STATUTORY TAX RETURNS

The information contained within the tax returns does not specify between Transmission and Distribution. Therefore, in order to reconcile the regulatory amounts to the tax returns the amounts need to be collated in a combined Transmission and Distribution view shown in Table 18 below.

Table 18: Total Regulatory additions split by Capital Allowance pool

Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
	£m	£m	£m	£m
Transmission (Table 3)	12.616	0.412	2.913	**15.940**
Distribution (Table 8)	57.231	14.009	21.362	**92.602**
Total Regulatory Additions	**69.847**	**14.421**	**24.275**	**108.542**

Table 19 provides a reconciliation of capital additions in each pool shown in the tax return (Table 17 – Column G) with the additions used in the calculation of regulatory entitlement for 2019/20 as set out in Table 18.

Table 19: Reconciliation of Additions in Tax return to Regulatory Capital Allowances Pools

Description	Long-Life Asset Pool	General Pool	Deferred Revenue Pool	Total
	£m	£m	£m	£m
Capex per Tax Return (Table 17 - G)	76.953	14.038	24.275	**115.266**
Transmission Capex Incentive Adjustment (Table 3 – B)	0.241	0.145	-	**0.386**
Distribution Capex Incentive Adjustment (Table 8 – B)	(1.349)	0.851	-	**(0.498)**
Less Legacy RP5 Dt Items (Table 2 – D)	(0.053)	-	-	**(0.053)**
Add IT Contestability opex costs recovered through Regulatory additions (Table 7 – C)	-	0.003	-	**0.003**
Add D5 Mechanism Costs (opex costs included within qualifying capex) (Table 2 – C)	(0.001)	-	-	**(0.001)**
Less Domestic Contributions (Table 17 - G)	(5.382)	-	-	**(5.382)**
Less Connection expenditure (Non-price control) (Table 7 – D)	(18.420)	(0.616)	-	**(19.036)**
Add Connection income (Non-price control) (Table 17 - G less Table 2 – B & Table 7 – B)	17.913	-	-	**17.913**
Less Asset Disposals (Table 8 – C)	(0.055)	-	-	**(0.055)**
Regulatory Additions	**69.847**	**14.421**	**24.275**	**108.542**

7. RETROSPECTIVE ADJUSTMENTS

With reference to Paragraph 12.35 (d) of Annex 2 of the Licences, there are no retrospective adjustments in respect of previous years and no restatement of 12.35 (a), 12.35 (b) and 12.35 (c) is required.

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Independent Auditors' Report to the directors of Northern Ireland Electricity Networks Limited (the Company) and Utility Regulator (the Regulator)

Audit of regulatory tax reports in accordance with Paragraph 12.35 of Annex 2 of Northern Ireland Electricity Distribution and Participate in Transmission Licences (the Licences) for RP6 covering the period 1 October 2017 to 31 March 2020.

Introduction

This report is produced in accordance with the terms of our engagement letter with the Company dated 15 January 2021.

Background

This report is made in order to meet the requirements of Paragraph 12.35 of Annex 2 of the Company's Regulatory Licences. Our audit work has been undertaken to (a) assist the Company to meet its obligation under the Regulatory Licences to procure such a report and to (b) facilitate the carrying out by the Regulator of its regulatory functions, and for no other purpose. We do not accept or assume responsibility to anyone other than the Company and the Regulator, for our audit work, for this report or for the opinions we have formed. We understand that the format and content of the tax report has been agreed with the Regulator.

For clarification, the statutory tax returns are filed on a calendar year basis and the Company's Maximum Regulated Revenue is calculated on the regulatory year April – March. The information within the tax returns is converted into regulatory periods which can cause timing differences.

Scope of work

We draw your attention to the fact that the engagement is to review the reconciliation of the information submitted to HMRC on the Company's tax affairs with the information used for the calculation of the tax element of the Company's Maximum Regulated Revenue as calculated in accordance with Paragraph 9 of Annex 2 of the Licences.

Limitation of Scope

We would specifically note the following limitations on our procedures;

- We have not audited the Company's statutory tax returns submitted to HMRC nor have we reviewed the appropriateness of the capital spend allocation to the respective capital allowance pools in each of those statutory tax returns.
- We have not audited the Financial Data RIGs submitted to the Utility Regulator which set out actual costs for the Company in accordance with the various licence terms.
- We have not audited the components of the Company's Maximum Regulated Revenue as calculated in Paragraph 3 of Annex 2 of the Licences.
- In various schedules figures reflected in either the statutory tax returns or the statutory financial statements have been allocated to regulatory periods on different bases e.g. on a specific allocation basis or on a time apportioned basis. We have not audited in detail these allocations to the regulatory period, however where appropriate, we have

compared the total of the relevant figures across the entire period from 1 October 2017 – 31 March 2020.

- We would specifically note across the entire period from 1 October 2017 – 31 March 2020 there is a difference of £98k between the corporation tax liability in the statutory tax returns compared to the tax liability calculated on a regulatory year basis. The main reason for this difference is the rate of tax for the statutory period compared to the regulatory periods will vary in 2017 due to timing differences of changes in the rate of tax. From 1 April 2017 the rate of corporation tax was consistently 19% and a hybrid rate was used in the statutory period ended 31 December 2017.We note that the total taxable profits (i.e. before applying the tax rate) did agree across the entire period.
- We note there is a difference of £3.878m between additions eligible for capital allowances in the tax returns submitted to HMRC and the regulatory reports. The differences arise in the statutory periods ended 31 December 2018 and 31 December 2019 and relates to the treatment of customer contributions. The amount of eligible additions in the tax returns are understated as a consequence of the element of capital contributions which reduce the amount of capital allowances being claimed. The regulatory reports reflect the correct position.

Approach

In order to complete this engagement, we adopted the following approach:

- Meetings were held with the Regulatory Reporting team to discuss the content of the Tax Reports and the models used to calculate the tax entitlement amount.
- Verified the calculation of the Tax Amount per Paragraph 9 of Annex 2 of the RP6 Transmission and Distribution Licences.
- Verified the underlying numbers within the tax reports to the source documents as listed below;
  - Financial Data RIGS Reporting workbook
  - RP6 Financial model

  We understand the Regulator has reviewed the numbers within the above source documents. As noted above, we have not audited the source documents.
- Verified the opening balances of the regulatory capital allowance pools. The opening values for 2017/18 reflecting the values set out in Table 4 and Table 9 of the 2016/17 Tax report which was audited previously as part of RP5 Transmission and Distribution Licences.
- Verified the allocation of capital additions (including the incentive amounts) to the appropriate regulatory capital allowance pools to ensure these reflected the same allocations as those in the Statutory Tax submission, other than differences as noted under limitations in scope.
- Checked the analysis of the tax allowance set out in the Tax Reports to the tax returns submitted to HMRC.
- Verified the allocation of capital additions per the Statutory tax return (based on a Calendar Year) to the allocation of capital additions per the regulatory reporting period (April to March), other than noted above under limitations of scope.
- Agreed the reconciliation of Tax Entitlement to Statutory Tax, subject to the timing difference as highlighted under limitations in scope above.

- Verified the reconciliation of capital additions per the statutory tax return to regulatory additions for each capital allowance pool.

Opinion

Based on our examination as above, we report that based on our findings, in our opinion the Tax Reports are consistent with the records we inspected and has been prepared, in all respects, in accordance with the requirements of the Licence.

Brendan McSparran
Tax Partner
Ernst & Young LLP
Chartered Accountants and Statutory Auditors
Belfast
4 July 2022