Attachment 9 – Ausgrid's pass through application

Networks NSW Memorandum: Common Company Policy – Transfer Pricing

August 2015

Company Policy

FINANCIAL MANAGEMENT	Document No	:	FM000-Y0023
	Amendment No	:	0
	Approved By	:	CEO
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	Review Date	:	05 August 2017

FM000-Y0023 TRANSFER PRICING

1.0 POLICY STATEMENT

The company will charge for goods and/or services provided to another Distribution Network Service Provider (DNSP) at a rate which reflects the cost of providing the goods and/or services via transfer pricing.

Services being provided to a DNSP which are subject to an existing set of arrangements as at 5 August 2014 are excluded from the scope of this policy, however any renewal of these arrangements is subject to this policy.

2.0 PURPOSE

The purpose of this policy is to set out a consistent transfer pricing policy which provides an equitable framework for charging incurred costs for instances where goods and/or services are provided to another DNSP.

3.0 REFERENCES

Internal
Company Policy (Procurement & Logistics) – Obsolete and Excess Stock
Annexure A – Policy Application Guidance

External
Energy Services Corporations Amendment (Distributor Efficiency) Act 2013
Income Tax Assessment Act 1997
A New tax System (Goods and Services Tax) Act 1999
Public Authorities (Financial Arrangements) Act 1987 (‘PAFA’)
Public Authorities (Financial Arrangements) Regulation 2005
Australian Accounting Standards

4.0 DEFINITIONS

DNSP
Distribution Network Service Provider ie Ausgrid, Endeavour Energy and Essential Energy.

Document control
Employees who work with printed copies of documents must check the Business Management Systems regularly to monitor version control. Documents are considered “UNCONTROLLED IF PRINTED”, as indicated in the footer.

Executive Leadership Group
Chief Executive Officer, Chief Operating Officers, Group Chief Financial Officer, Group Executive Network Strategy, Group Executive People & Services and Board Secretary.

Executive Leadership Team Chief Operating Officer, General Manager Health, Safety & Environment, General Manager People & Services, Chief Engineer, General Manager Network Development, General Manager Network Operations, General Manager Finance & Compliance and General Manager Information, Communications & Technology.

Review date
The review date displayed in the header of the document is the future date for review of a document. The default period is three years from the date of approval. However a review may be mandated at any time where a need is identified due to changes in legislation, organisational changes, restructures, occurrence of an incident or changes in technology or work practice.

5.0 KEY REQUIREMENTS

All transactions entered into with another DNSP are required to have a business purpose and be carried out in a commercial manner; requiring a charge to be made for the goods and/or services provided.

5.1 One off events

Assistance may be provider to another DNSP in times of need as a result of one off events (eg such as natural disasters). In providing goods and/or services the company should recover any cost incurred.

5.2 On-going services

On-going services may be provided to another DNSP. In providing such services the company must charge for the on-going services at a rate which reflects the cost of providing the services.

5.3 Determining the change

In determining a suitable charge, the charge should equate to a recovery of costs without profit margin. Cost for the purpose of these cost recoveries is determined using the company's current costing methodology (ie direct operating expenditure plus overheads). In the case of inventory and property, plant and equipment, cost means the carrying amount of the inventory/asset after taking into account write offs, obsolescence or depreciation, subject to section 5.3.1 below.

The charge out process should leverage off established cost recovery processes to minimise any administration burden and support compliance with Goods and Services Tax (GST) requirements.

5.3.1 Surplus or obsolete inventory/assets

In the case of surplus or obsolete inventory/assets, cost is to be:

a) if there is an active market for the item(s), the lesser of:
- the market value, or
- the written down value of the item(s), after taking into account write offs, obsolescence or depreciation.

b) if there is no active market for the item(s), the lesser of:
- the scrap value plus 10% transaction cost, or
- the written down value of the item(s), after taking into account write offs, obsolescence or depreciation.

The overriding principle for transfer pricing of surplus or obsolete inventory/assets is to make the purchase/utilisation of these excess items more attractive to another DNSP than having the DNSP procure new items.

Refer to Annexure A for guidance as to how to apply this policy.

5.3.2 GST

The provision of goods and/or services to another DNSP involves taxable supplies that are subject to GST.

5.3.3 Waiving of charge

The DNSP may decide, as part of community service and being a good corporate citizen, to assist another DNSP in times of need without charging for this service; in such cases written approval must be obtained from the Chief Executive Officer, with endorsement from the Chief Operating Officer.

5.4 Recording of cost and revenue

The costs and revenues are to be recorded in the following sections of the company's monthly Finance Performance Report to the Board:

Item	Current classification	Proposed
Revenue (as supporting entity)	Other income	Operating expenditure
Costs (as supporting entity)	Operating expenditure	Operating expenditure
Costs (as assisted entity)	Operating expenditure	Operating expenditure
Impact on Assisting Entity		
Impact on operating expenditure Key performance Indicators (KPI)	Yes	No
Earnings Before Interest and Tax (EBIT)	No	No

Normalisation for scorecard purposes may be required for cost of assistance provided depending on materiality.

6.0 ACTIONS TO ACHIEVE IMPLEMENTATION OF THIS POLICY

- development or revision of procedures to support operational compliance to this policy; and
- communication of policy to all impacted areas.

7.0 AUTHORITIES AND RESPONSIBILITIES

Chief Executive Officer has the authority and responsibility for approving this policy.

General Manager Finance and Compliance has the authority and responsibility for:

- providing appropriate resources to support the management of this policy; and
- establishing and maintaining procedures to support the adherence of this policy.

Manager Commercial & Decision Support has authority and responsibility for calculating and affecting the charges required under this policy.

Executive Leadership Team has the authority and responsibility for implementing this policy within their Division.

Managers have the authority and responsibility for ensuring all employees within their area comply with this policy.

Employees have the authority and responsibility for complying with this policy.

8.0 DOCUMENT CONTROL

Content Coordinator	**:**	Manager Commercial & Decision Support
Distribution Coordinator	**:**	GRC Process Coordinator

Annexure A: Policy Application Guidance

Below are four scenarios illustrating the application of this policy.

Scenario 1 – Decommissioned Equipment

Facts
The DNSP plans to remove 66kV Circuit Breakers from a zone substation (switch room is being decommissioned). The company have sufficient critical spares for this kind of equipment and have no further need for it. If the circuit breakers remain company property they will be deemed obsolete and will be scrapped. Another DNSP has a requirement for the 66 kV circuit breakers.

Question for consideration
What is the appropriate charge to the receiving DNSP in addition to the transport costs which they have already committed to pay?

Answer
The overriding principle in the policy is that transfer prices for obsolete inventory/assets are based on the cost of the items less any obsolescence, depreciation and write off. As there is no active market to determine a resale value, then the appropriate charge is the lesser of:

- scrap values plus 10% transaction cost; or
- the written down value of the item(s).

Scenario 2 – New Project Materials

Facts
The DNSP purchased a new 132/11kv, 45 MVA transformer from a supplier (where it is being stored) in September 2009 to be used on a major capital project. The project has now been postponed indefinitely. Another DNSP will have a requirement for the same type of transformer in June 2015. The cost of the transformer new (in 2009) was $908,333.

Questions for consideration
Is this a surplus asset?
Is there an active market for this asset?
What is the charge to the DNSP?

Answer
Given there is no expectation of the company using this asset in the foreseeable future, this would be considered a surplus asset as per 5.3.1.

Scenario 3 – Inventory which is obsolete due to a change in standards

Facts
The DNSP has made concrete poles redundant in its network, moving to a more effective mix of timber and steel. Other DNSPs would like to use up any concrete poles which the first DNSP has which are excess that are still current on their networks and costly to procure.

Question for consideration
What is the process to transfer and what will the price be?

Answer
As the company has made the poles redundant in its network, this would be considered obsolete inventory as per 5.3.1.

Scenario 4- Excess inventory materials

Facts
A change in standard has led to material **'A'** not being fully utilised and over 500 units remain in inventory. The other DNSPs no longer use material A so the options for disposal are to scrap, to sell back to the manufacturer, or to sell to a third party.

Question for consideration
If the best business outcome is to sell to a third party, what is the mechanism for sale and what should the process be?

Answer
As the transaction is not between the company and another DNSP, the above case is outside the scope of this policy.

Sales to external parties will follow normal terms of trade.