FINAL DECISION

Directlink
Transmission Determination
2020 to 2025

Attachment 7
Corporate income tax

June 2020

AUSTRALIAN ENERGY REGULATOR

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Note

This attachment forms part of the AER's final decision on Directlink's 2020–25 transmission determination. It should be read with all other parts of the final decision.

The final decision includes the following attachments:

Overview

Directlink transmission determination 2020–2025

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment A – Pricing methodology

Contents

7 Corporate income tax

Our revenue determination includes the estimated cost of corporate income tax for Directlink's 2020–25 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 attachment sets out our final decision on Directlink's revised proposed corporate income tax allowance for the 2020–25 regulatory control period. It presents our assessment of the inputs required in the PTRM for the calculation of the cost of corporate income tax.

7.1 Final decision

Our final decision on Directlink's estimated cost of corporate income tax is $0.8 million over the 2020–25 regulatory control period. This represents no material difference to Directlink's revised proposed cost of corporate income tax.

Any small difference reflects our minor adjustment to the return on capital building block (section 2.2 of the overview), which affects the calculation of the estimated taxable income, and in turn impacts the corporate income tax allowance.

We accept the revised proposed opening tax asset base (TAB) value as at 1 July 2020 of $111.2 million. We also accept Directlink's revised proposed standard tax asset lives, including the 5 years assigned to the proposed new 'Transmission determination costs' asset class.

Table 7.1 sets out our final decision on the estimated cost of corporate income tax for Directlink over the 2020–25 regulatory control period.

Table 7.1 AER's final decision on Directlink's cost of corporate income tax for the 2020–25 regulatory control period ($million, nominal)

	2020–21	2021–22	2022–23	2023–24	2024–25	Total
Tax payable	0.4	0.4	0.4	0.4	0.4	1.9
Less: value of imputation credits	0.2	0.2	0.2	0.2	0.2	1.1
Net corporate income tax allowance	0.2	0.2	0.1	0.1	0.2	0.8

Source: AER analysis.

[1] NER, cl. 6A.5.4(a)(4).

Opening tax asset base as at 1 July 2020

For this final decision, we accept Directlink's revised proposed opening TAB value as at 1 July 2020 of $111.2 million ($nominal). This is $2.0 million (or 1.8 per cent) higher than the value of $109.2 million determined in our draft decision.

In our draft decision, we accepted Directlink's proposed method to establish the opening TAB as at 1 July 2020. However, we updated Directlink's 2018–19 estimated capital expenditure (capex) with actuals. We noted that these figures would be reviewed for the final decision when the audited regulatory accounts for 2018–19 would be available.[2] We have checked the 2018–19 actual capex in the revised proposal and are satisfied it aligns with Directlink's regulatory accounts for that year.

Directlink's revised proposal updated its 2019–20 estimate of capex with the latest figures.[3] For the reasons discussed in attachment 2, we accept the updated 2019–20 capex estimate in the revised proposal. This capex estimate is higher than what we approved in our draft decision, reflecting more recent data. The estimated capex will be updated for actuals in the roll forward for the 2020–25 period at the next revenue reset.

Table 7.2 sets out our final decision on the roll forward of Directlink's TAB values over the 2015–20 regulatory control period.

Table 7.2 AER's final decision on Directlink's TAB roll forward for the 2015–20 regulatory control period

	2015–16	2016–17	2017–18	2018–19	2019–20[a]
Opening TAB	99.0	99.2	98.6	104.6	106.4
Capital expenditure[b]	3.9	3.3	10.0	6.2	9.5
Less: tax depreciation	3.7	3.9	4.0	4.4	4.6
Closing TAB	**99.2**	**98.6**	**104.6**	**106.4**	**111.2**

Source: AER analysis.

(a) As commissioned, net of disposals

(b) Based on estimated capex.

Standard and remaining tax asset lives as at 1 July 2020

For this final decision, we accept Directlink's revised proposed approach for its existing asset classes to assign the remaining tax asset life and standard tax asset life of its forecast capex for the 2020–25 regulatory control period to align with the remaining

2 AER, *Directlink 2020–25 Transmission Determination - Draft Decision - Attachment 7 - Corporate income tax*, October 2019, pp. 7–16.

3 Directlink, *Revised roll forward model*, December 2019.

technical life of Directlink, which is 21.2 years.[4] This is because unlike other transmission network service providers, Directlink provides prescribed transmission services as a single standalone entity. We therefore consider that Directlink's assets will have no useful life at the end of its technical life. This approach is consistent with our draft decision and also our decision on the standard and remaining tax asset lives for Directlink in the 2015–20 regulatory control period.[5]

We also accept Directlink's revised proposed new 'Transmission determination costs' asset class and the associated standard tax asset life of 5 years assigned for this asset class in the PTRM. This is because we consider that this life is consistent with the ATO's requirements for intangible assets.[6] We discuss the approved capex for this asset class in attachment 5.

In the draft decision, we made the following changes to Directlink's modelling of its cost of corporate income tax:[7]

- we used the latest version of the PTRM (version 4) released in April 2019, which implemented the findings in our final report on the review of the regulatory tax approach.[8] Specifically, we applied the diminishing value method for tax depreciation to all new depreciable assets except for forecast capex associated with buildings[9]
- we accepted Directlink's proposed approach for its remaining and standard tax asset lives. However, we separated out land and easements allocated to the 'Transmission assets' asset class into two new asset classes labelled 'Land' and 'Easements' respectively. These two asset classes do not depreciate for tax purposes. This is because land and easements are not considered depreciable assets under the tax rules[10]
- we removed Directlink's proposed new 'Restoration and rectification' asset class and its associated standard tax asset life of 21.2 years from the PTRM. This is because we did not approve the proposed forecast capex associated with this asset class.

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4 This is because the ATO allows an asset to be written-off for tax purposes if the business no longer holds or uses the asset. We note Directlink's assets would not have any useful life when Directlink ceases to operate in 2041–42. Therefore, we consider this proposed alignment of the standard and remaining tax asset lives is appropriate for tax depreciation purposes.

5 AER, *Final decision, Directlink transmission determination 2015–20, Attachment 8 - Corporate income tax*, April 2015, p. 9.

6 ATO, *Taxation Ruling 2019/5*, July 2019, ITAA, section 40.95(8).

7 AER, *Directlink 2020–25 Transmission Determination - Draft Decision - Attachment 7 - Corporate income tax*, October 2019, pp. 7–5.

8 AER, *Final report, Review of regulatory tax approach*, December 2018.

9 All assets acquired prior to 30 June 2020 will continue to be depreciated using the straight-line depreciation method for regulatory tax purposes, until these assets are fully depreciated.

10 ITAA, section. 40.30.

Directlink's revised proposal adopted the draft decision changes in full.[11]

Table 7.3 sets out our final decision on the standard and remaining tax asset lives as at 1 July 2020 for Directlink. We are satisfied that the standard and remaining tax asset lives are appropriate for application over the 2020–25 regulatory control period. We are also satisfied the standard and remaining tax asset lives provide an estimate of the tax depreciation amount that would be consistent with the tax expenses used to estimate the annual taxable income for a benchmark efficient service provider.[12]

Table 7.3 AER's final decision on Directlink's standard and remaining tax asset lives as at 1 July 2020 (years)

Asset class	Standard tax asset life	Remaining tax asset lives as at 1 July 2020[a]
Transmission assets	21.2[b]	21.2
Transmission determination costs	5.0[b]	n/a
Easements	n/a	n/a
Land	n/a	n/a
Buildings	21.2[a]	n/a
Equity raising costs	5.0[a]	n/a

Source: AER analysis.

(a) Used for straight-line method of tax depreciation.

(b) Used for diminishing value method of tax depreciation.

n/a not applicable. We have not assigned a standard tax asset life or a remaining tax asset life to the 'Land' and 'Easements' asset classes because the assets allocated to these asset classes are non-depreciating assets for tax purposes. We have not assigned a remaining tax asset life to the 'Transmission determination costs', 'Buildings' and 'Equity raising costs' asset classes because they do not have an opening TAB value as at 1 July 2020.

7.2 Assessment approach

We did not change our assessment approach for the cost of corporate income tax from our draft decision. Attachment 7 (section 7.3) of our draft decision details that approach.[13]

11 Directlink, *Revised PTRM*, December 2019.

12 NER, cl. 6A.6.4.

13 AER, *Directlink 2020–25 Transmission Determination - Draft Decision - Attachment 7 - Corporate income tax*, October 2019, pp. 7–14.

Shortened forms

Shortened form	Extended form
AER	Australian Energy Regulator
ATO	Australian Taxation Office
capex	capital expenditure
ITAA	Income Tax Assessment Act 1997
NER	national electricity rules
PTRM	post-tax revenue model
TAB	tax asset base