

FINAL DECISION

Directlink transmission determination

2015−16 to 2019−20

Attachment 8 − Corporate income tax

April 2015

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1. Note
2. This attachment forms part of the AER's final decision on Directlink's revenue proposal 2015–20. It should be read with other parts of the final decision.
3. The final decision includes the following documents:
4. Overview
5. Attachment 1 – maximum allowed revenue
6. Attachment 2 – regulatory asset base
7. Attachment 3 – rate of return
8. Attachment 4 – value of imputation credits
9. Attachment 5 – regulatory depreciation
10. Attachment 6 – capital expenditure
11. Attachment 7 – operating expenditure
12. Attachment 8 – corporate income tax
13. Attachment 9 – efficiency benefit sharing scheme
14. Attachment 10 – capital expenditure sharing scheme
15. Attachment 11 – service target performance incentive scheme
16. Attachment 12 – pricing methodology and negotiated services
17. Attachment 13 – pass through events
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1. Shortened forms

| 1. Shortened form
 | 1. Extended form
 |
| --- | --- |
| 1. AARR
 | 1. aggregate annual revenue requirement
 |
| 1. AEMC
 | 1. Australian Energy Market Commission
 |
| 1. AEMO
 | 1. Australian Energy Market Operator
 |
| 1. AER
 | 1. Australian Energy Regulator
 |
| 1. ASRR
 | 1. annual service revenue requirement
 |
| 1. augex
 | 1. augmentation expenditure
 |
| 1. capex
 | 1. capital expenditure
 |
| 1. CCP
 | 1. Consumer Challenge Panel
 |
| 1. CESS
 | 1. capital expenditure sharing scheme
 |
| 1. CPI
 | 1. consumer price index
 |
| 1. DRP
 | 1. debt risk premium
 |
| 1. EBSS
 | 1. efficiency benefit sharing scheme
 |
| 1. ERP
 | 1. equity risk premium
 |
| 1. MAR
 | 1. maximum allowed revenue
 |
| 1. MRP
 | 1. market risk premium
 |
| 1. NEL
 | 1. national electricity law
 |
| 1. NEM
 | 1. national electricity market
 |
| 1. NEO
 | 1. national electricity objective
 |
| 1. NER
 | 1. national electricity rules
 |
| 1. NSP
 | 1. network service provider
 |
| 1. NTSC
 | 1. negotiated transmission service criteria
 |
| 1. opex
 | 1. operating expenditure
 |
| 1. PPI
 | 1. partial performance indicators
 |
| 1. PTRM
 | 1. post-tax revenue model
 |
| 1. RAB
 | 1. regulatory asset base
 |
| 1. RBA
 | 1. Reserve Bank of Australia
 |
| 1. repex
 | 1. replacement expenditure
 |
| 1. RFM
 | 1. roll forward model
 |
| 1. RIN
 | 1. regulatory information notice
 |
| 1. RPP
 | 1. revenue and pricing principles
 |
| 1. SLCAPM
 | 1. Sharpe-Lintner capital asset pricing model
 |
| 1. STPIS
 | 1. service target performance incentive scheme
 |
| 1. TNSP
 | 1. transmission network service provider
 |
| 1. TUoS
 | 1. transmission use of system
 |
| 1. WACC
 | 1. weighted average cost of capital
 |

# Corporate income tax

1. The AER is required to make a decision on the estimated cost of corporate income tax for Directlink's 2015–20 regulatory control period.[[1]](#footnote-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).
2. This attachment sets out our final decision on Directlink's revised proposed corporate income tax allowance. It also presents our final decision on the revised proposed opening tax asset base (TAB), and the standard and remaining tax asset lives used to estimate tax depreciation for the purpose of calculating tax expenses.

## Final decision

1. We accept Directlink's proposed approach to estimating its cost of corporate income tax. We determine Directlink's corporate income tax allowance to be $2.1 million ($ nominal) for the 2015–20 regulatory control period. This represents a reduction of $1.1 million (or 35.6 per cent) from Directlink's revised proposal.
2. Our final decision differs from Directlink's revised proposal due to our determination on Directlink's proposed value of imputation credits (gamma) as discussed in attachment 4. Our determinations on other building block components including forecast capex (attachment 6) and forecast opex (attachment 7) affect revenues, which also impact the tax calculation.
3. Table 8‑1 sets out our final decision on the estimated cost of corporate income tax allowance for Directlink.

Table 8‑1 AER's final decision on Directlink's cost of corporate income tax allowance for the 2015–20 regulatory control period ($ million, nominal)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 2015–16 | 2016–17 | 2017–18 | 2018–19 | 2019–20 | Total |
| Tax payable | 0.6 | 0.6 | 0.7 | 0.7 | 0.8 | 3.4 |
| Less: value of imputation credits | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 | 1.4 |
| **Net corporate income tax allowance** | **0.3** | **0.4** | **0.4** | **0.4** | **0.5** | **2.1** |

Source: AER analysis.

## Directlink’s revised proposal

Directlink's methodology for determining its corporate income tax is unchanged from its initial proposal. We accepted the approach in our draft decision. Directlink has revised its corporate income tax allowance using the AER's PTRM and includes the following inputs:[[2]](#footnote-2)

* A revised opening TAB at 1 July 2015, reflecting updates for 2013–14 actual capex and 2014–15 estimate of capex.
* Revised forecast capex.
* Revised forecast opex.

Directlink also used standard and remaining tax asset lives consistent with those approved in the draft decision and a value for gamma of 0.25. Due to the revised inputs, Directlink's estimated corporate income tax allowance is $1.2 million (or 27.3 per cent) lower in its revised proposal than in its initial proposal. Table 8‑2 sets out Directlink's proposed corporate income tax allowance for the 2015–20 regulatory control period.

Table 8‑2 Directlink's revised proposed corporate income tax allowance for the 2015–20 regulatory control period ($ million, nominal)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 2015–16 | 2016–17 | 2017–18 | 2018–19 | 2019–20 | Total |
| Tax payable | 0.7 | 0.8 | 0.9 | 0.9 | 1.0 | 4.3 |
| Less: value of imputation credits | 0.2 | 0.2 | 0.2 | 0.2 | 0.3 | 1.1 |
| **Net corporate income tax allowance** | **0.5** | **0.6** | **0.6** | **0.7** | **0.7** | **3.2** |

Source: Directlink, Revised revenue proposal, p. 15.

## AER’s assessment approach

We did not change our assessment approach for the corporate income tax allowance from our draft decision. Section 8.3 of our draft decision details that approach.

## Reasons for final decision

1. We do not accept Directlink's revised proposed estimated cost of corporate income tax. We instead determine an estimated cost of corporate income tax of $2.1 million ($ nominal) for Directlink, which represents a reduction of $1.1 million (or 35.6 per cent) from its revised proposal.
2. We have accepted the following revised proposed inputs to the PTRM for tax purposes:
* The opening TAB value at the commencement of the 2015–2020 regulatory control period (section 8.4.1)
* The standard and remaining tax asset lives (section 8.4.2).
1. However, we have adjusted other proposed inputs to the PTRM which affect the calculation of the taxable income, and therefore the estimated corporate income tax allowance. These include the value for gamma (attachment 4), forecast opex (attachment 7) and forecast capex (attachment 6).

### Opening tax base at 1 July 2015

1. We accept Directlink's proposed opening TAB value as at 1 July 2015 of $99.1 million ($ nominal). Directlink has applied the approach set out in our roll forward model (RFM) to establish its revised proposed opening TAB value.

Also, as discussed in attachment 2, we accept Directlink's revised proposal where it updated its estimated capex for 2013–14, with actual capex in the RFM. We also accept Directlink's revised proposal estimate of capex for 2014–14 in the RFM.

Table 8‑3 sets out our final decision on the roll forward of Directlink's TAB values.

Table 8‑3 AER's final decision on Directlink's TAB roll forward for the 2015–20 regulatory control period ($ million, nominal)

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2005–06 | 2006–07 | 2007–08 | 2008–09 | 2009–10 | 2010–11 | 2011–12 | 2012–13 | 2013–14 | 2014–15b |
| Opening TAB |  116.7  |  115.7  |  113.4  |  110.3 |  107.2  |  104.2  |  103.1 |  101.4  |  99.2  |  98.6  |
| Capital expenditurea | 2.0 | 0.8 | – | – | – | 2.0 | 1.5 | 0.9 | 2.6 | 3.8 |
| Tax depreciation | –3.0 | –3.1 | -3.1 | –3.1 | –3.1 | -3.1 | –3.1 | –3.2 | –3.2 | –3.2 |
| Closing TAB | 115.7 | 113.4 | 110.3 | 107.2 | 104.2 | 103.1 | 101.4 | 99.2 | 98.6 | 99.1 |

Source: AER analysis.

(a) As commissioned, net of disposals.

(b) Based on estimated capex.

### Standard and remaining tax asset lives

Consistent with our draft decision, we accept Directlink's proposed standard and remaining tax asset lives for its 'Substation' and 'Transmission line' asset classes.

1. In the draft decision, we accepted Directlink's proposal to align the remaining tax asset life of the ‘Transmission line’ asset class with that of the ‘Substation’ asset class. This is because the transmission line will have no useful life when the substation ceases to operate. We also accepted Directlink's proposal to change its standard tax asset lives for tax depreciation purposes of new capex over the 2015–20 regulatory control period. We considered the proposed forecast capex are for stay in business and ancillary equipment purposes and should have the same remaining tax life as the substation assets. Therefore, we were satisfied that it was reasonable to change the standard tax asset life of the ‘Transmission line’ asset class and 'Substations' asset class to 26 years.[[3]](#footnote-3)
2. We are satisfied the proposed standard and remaining tax asset lives are likely to provide an appropriate estimate of the tax depreciation amount for a benchmark efficient TNSP as required by the NER.[[4]](#footnote-4)
3. Table 8‑4 sets out our final decision on Directlink's standard and remaining tax asset lives for the 2015–20 regulatory control period.

Table 8‑4 AER's final decision on Directlink's standard and remaining tax asset lives as at 1 July 2015 (years)

| 1. Asset class
 | Standard tax asset life  | Remaining tax asset life as at 1 July 2015  |
| --- | --- | --- |
| Substations | 26.2 | 26.2 |
| Transmission line | 26.2 | 26.2 |
| Easements | n/a | n/a |

Source: AER analysis.

n/a: Not applicable.

1. NER, cl. 6A.5.4(a)(4). [↑](#footnote-ref-1)
2. Directlink, Revenue proposal, pp.40–42; Directlink, Revised proposed PTRM, January 2015. [↑](#footnote-ref-2)
3. AER, Draft decision, Directlink transmission determination 2015-16 to 2019-20, Attachment 8: Corporate income tax, November 2014, p. 11. [↑](#footnote-ref-3)
4. NER, cl. 6A.6.4. [↑](#footnote-ref-4)