Final decision

AusNet Gas Services
Gas distribution access arrangement
1 July 2023 to 30 June 2028

Attachment 7 – Corporate income tax

June 2023

AUSTRALIAN
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Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601
Tel: 1300 585 165

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7 Corporate income tax

Our determination of the total revenue for AusNet includes the estimated cost of corporate income tax for the 2023–28 access arrangement period (2023–28 period).[1] Under the post-tax framework, a corporate income tax amount is calculated as part of the building blocks assessment using our post-tax revenue model (PTRM). This amount allows AusNet to recover the estimated cost of corporate income tax for the 2023–28 period.

This attachment presents our assessment of AusNet's proposed corporate income tax amount for the 2023–28 period. It also presents our assessment of the proposed opening tax asset base (TAB), and the standard and remaining tax asset lives as at 1 July 2023 used to estimate tax depreciation for the purpose of calculating tax expenses.

7.1 Final decision

Our final decision on AusNet's estimated cost of corporate income tax is $42.0 million ($ nominal) over the 2023–28 period. This decision represents a decrease of $8.7 million (17.2%) from AusNet's revised proposed cost of corporate income tax of $50.7 million. The reason for the decrease is due to our final decision on a lower regulatory depreciation amount (section 4.1 of attachment 4). As regulatory depreciation is a component of revenue for tax purposes, the lower amount driven by a reduction in accelerated depreciation decreases AusNet's taxable income and, in turn, the cost of corporate income tax.

This decrease is partially offset by our final decision:

- on a higher return on equity (attachment 3)[2]
- on a lower tax depreciation[3]
- on a lower imputation credit (gamma) consistent with the new 2022 *Rate of Return Instrument* (attachment 3).[4]

For this final decision, we accept AusNet's revised proposal for establishing the opening TAB as at 1 July 2023. However, we have updated AusNet's opening TAB value to $1047.3 million, reflecting AusNet's revised capex estimate for 2022.

Table 7-1 sets out our final decision on the estimated cost of corporate income tax for AusNet over the 2023–28 period.

1 NGR, r. 76(c).

2 The higher return on equity amount is driven by a higher rate of return on equity and reduction to accelerated depreciation, which in turn increases the capital base, in our final decision compared to AusNet's revised proposal. All else being equal, a higher return on equity amount increases the cost of corporate income tax as it is a component of revenue for tax purposes.

3 The lower tax depreciation is driven by a lower expected inflation rate and lower opening TAB in our final decision compared to AusNet's revised proposal. All else being equal, a lower tax depreciation increases the cost of corporate income tax as it is a component of tax expense.

4 All else being equal, a lower gamma increases the cost of corporate income tax as it is an offset to the tax payable.

Table 7-1 AER's final decision on AusNet's cost of corporate income tax for the 2023–28 access arrangement period ($ million, nominal)

	2023–24	2024–25	2025–26	2026–27	2027–28	Total
Tax payable	20.7	18.6	17.7	19.5	21.1	97.6
Less: value of imputation credits	11.8	10.6	10.1	11.1	12.0	55.6
Net corporate income tax	**8.9**	**8.0**	**7.6**	**8.4**	**9.1**	**42.0**

Source: AER analysis.

In our draft decision, we accepted:[5]

- AusNet's proposed method to establish the opening TAB as at 1 July 2023, but amended the proposed value of 2021–23 capex to include Software as a Service (SaaS) related costs, reflecting our approach to mid-period changes in accounting standards.
- AusNet's proposed standard tax asset lives for all of its existing asset classes and the continuation of using the weighted average method to calculate remaining tax asset lives for estimating the forecast tax depreciation.
- AusNet's implementation of the findings of our 2018 tax review, including the introduction of immediate expensing of capital expenditure, diminishing value method of tax depreciation and applying a 20 year cap on the tax asset lives for certain classes of new gas assets.[6]
- AusNet's proposed new asset classes for 'Capitalised leases 1 July 2023' and 'Cathodic protection - post 1998'.
- AusNet's reallocation of $6.3 million ($2022–23) from the 'Cathodic protection' asset class to the 'Cathodic protection – post 1998' asset class, with the same standard tax asset life of 20 years and remaining tax asset life of 20.7 years.[7]

However, our draft decision updated:

- AusNet's proposed final year asset adjustment for including capitalised leases in the TAB to be consistent with the adjustment for the capital base.
- The tax calculations to include the carrying forward for the forecast tax loss of $8.6 million ($2022–23) as at 1 July 2023, consistent with the final decision PTRM for the half-year extension period.
- AusNet's proposed remaining tax asset lives to reflect our adjustments to the opening TAB value.

Our draft decision did not accept AusNet's proposed new asset classes of 'Transmission pipelines - post 1998', 'Distribution pipelines - post 1998' and 'Service pipes - post 1998' and

5 AER, *Draft decision, AusNet Gas Services Access Arrangement 2023–28, Attachment 7 – Corporate income tax*, December 2022, pp. 14–18.

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

7 This is consistent with the remaining life of the 'Cathodic protection' asset class prior to reallocation.

so did not reallocate existing assets or allocate capex to these asset classes for capital base or tax purposes.

AusNet's revised proposal broadly adopted all our draft decision amendments. However, it maintained its proposal for new asset classes for pipeline and services assets, which it renamed 'Transmission pipelines - post 2023', 'Distribution pipelines - post 2023' and 'Service pipes - post 2023'. For these asset classes AusNet proposed to allocate forecast capex but did not reallocate any existing assets. AusNet proposed a standard tax asset life of 20 years for the new asset classes consistent with the broader existing pipeline and services asset classes. For our final decision, we are not satisfied that these asset classes are required for the purposes of assigning shorter asset lives.[8]

Our final decision confirms our acceptance of AusNet's approach to forecasting its cost of corporate income tax for the 2023–28 period as set out in the PTRM.

Consistent with our draft decision, we accept AusNet's proposed $13.3 million ($2022–23) of forecast immediate expensing of capex for the 2023–28 period. We are satisfied that AusNet's approach to immediate expensing based on overheads for the 2023–28 period is reasonable, and we accept the proposed forecast capex that forms these overheads.[9] We will collect actual data relating to this expenditure in our annual reporting regulatory information notice (RIN) to further inform our decision on the forecast for the immediate expensing of capex in the next review for AusNet.

In our draft decision, we accepted $0.02 million ($2022–23) of forecast capex associated with equity raising costs are to be exempted from the diminishing value tax depreciation method. Our final decision updates this amount to $0.28 million, reflecting our final decision on AusNet's total revenue requirement.

In its response to our information request, AusNet confirmed that its revised proposed gross capex and capital contributions for the 2023–28 period do not contain any gifted assets.[10] We are satisfied that this approach is consistent with the Federal Court's ruling on the tax treatment of gifted assets.[11]

Opening tax asset base as at 1 July 2023

For our final decision, we determine an opening TAB value of $1047.3 million ($ nominal) after applying AusNet's update to the capex estimate for 2022. Our final decision opening TAB is $1.6 million lower than AusNet's revised proposal.

In our draft decision, we accepted AusNet's proposed method to establish the opening TAB as at 1 July 2023 but amended the proposed values of 2021–23 actual capex to reflect

8 Please see section 4.4.1 of attachment 4 of this final decision for details.

9 Our decision on forecast capex is discussed in attachment 5

10 AusNet, *Response to information request #025*, 21 February 2023, p. 5.

11 Federal Court of Australia, *Victoria Power Networks Pty Ltd v Commissioner of Taxation [2020] FCAFC 169*, 21 October 2020. The Court confirmed that cash contributions were ordinary income and should be treated as assessable income for tax purposes. Therefore, cash contributions are included in gross capex and customer contributions. The Court determined that while a gifted asset was a 'non-cash business benefit' there was effectively nil income for tax purposes. As a result, the cost of construction of gifted assets are excluded from gross capex and customer contributions.

inclusion of SaaS expenditures. We also updated AusNet's proposed final year asset adjustment for capitalised leases in the TAB to be consistent with our adjustment to the capital base.

We noted in our draft decision that the opening TAB may be updated to reflect any revisions for 2022 and the six-month extension period capex estimates as part of the final decision.[12]

AusNet's revised proposal adopted the amendments we made to the opening TAB value in the draft decision in full. It did not make any further updates to the opening TAB value. Subsequently, in its response to our information request, AusNet provided us with its revised gross capex estimate for 2022 which is lower than the amount approved in our draft decision for this period, while no updates were made to the six-month extension period.[13]

We accept AusNet's revised capex estimate for 2022 and the six-month extension period estimate based on our capex assessment. We will update the 2022 and the six-month extension period capex estimates for actuals at the next access arrangement review.

Table 7-2 sets out our final decision on the roll forward of AusNet's TAB values over the 2018–23 period.

Table 7-2 AER's final decision on AusNet's tax asset base roll forward over the 2018–23 period ($ million, nominal)

	2018	2019	2020	2021	2022[a]	2023[b]
Opening TAB	707.3	763.5	815.6	868.7	944.1	1003.7
Capital expenditure[c]	101.5	102.5	98.7	113.3	103.1	61.1
Less: tax depreciation	45.4	50.3	45.7	37.9	43.4	22.9
Final year asset adjustment						5.3
Closing TAB	**763.5**	**815.6**	**868.7**	**944.1**	**1003.7**	**1047.3**

Source: AER Analysis.

(a) Based on estimated capex. We expect to update the TAB for actual capex at the next review.

(b) The half year period of 1 January to 30 June 2023. Based on estimated capex.

(c) Net of disposals.

Standard and remaining tax asset lives as at 1 July 2023

For this final decision, we accept the majority of AusNet's revised proposed standard tax asset lives and the method used for calculating its remaining tax asset lives for all its existing

12 AER, *Draft decision, AusNet Gas Services Access Arrangement 2023–28, Attachment 7 – Corporate income tax*, December 2022, p. 17.

13 AusNet, *Response to information request #028*, 15 March 2023.

asset classes.[14] [15] We also accept the revised proposed standard and remaining tax assets lives of the new ‘Cathodic protection - post 1998’ asset class, which is consistent with our draft decision.[16] AusNet’s revised proposed standard tax asset lives are consistent with our draft decision, and we confirm our position that they are broadly consistent with the values prescribed by the Commissioner for taxation in ATO ruling 2022/1 and the *Income Tax Assessment Act* (ITAA).[17]

Consistent with the draft decision, we also accept AusNet’s revised proposal to apply the weighted average method for calculating the remaining tax asset lives as at 1 July 2023. This method is a continuation of the approved approach used in the 2018–23 period and applies the approach as set out in our roll forward model (RFM). However, we have updated the remaining tax asset lives as at 1 July 2023 to reflect the amendments we made to the opening TAB value as at 1 July 2023.[18]

Table 7-3 sets out our final decision on the standard and remaining tax asset lives for AusNet. We are satisfied that these lives are appropriate for application over the 2023–28 period. We are also satisfied these 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.[19]

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14 In its revised proposal AusNet reintroduced the new asset classes that were renamed to ‘Transmission pipelines - post 2023’, ‘Distribution pipelines - post 2023’ and ‘Service pipes - post 2023’ which have a shorter standard asset life of 50 years. While this does not affect the standard tax asset life for the relevant assets as they are consistently set at 20 years, we are not approving the introduction of these new asset classes.

15 For this final decision we have not assigned a tax standard asset life or tax remaining life to the ‘Cathodic protection’ asset class since it has no forecast capex or opening TAB. This change is presentational and does not impact revenue. Consistent with our draft decision and AusNet’s revised proposal, the forecast capex for these assets is allocated to the ‘Cathodic protection - post 1998’ asset class.

16 AER, *Draft decision: AusNet Gas Services Access Arrangement 2023–28, Attachment 7 – Corporate income tax*, September 2022, pp. 18–19.

17 ATO, *Taxation Ruling TR2022/1 – Income tax: effective life of depreciating assets (applicable from 1 July 2022),* p. 179.

18 With the exception of ‘Buildings’, ‘Capitalised Leases 1 July 2023’ and Equity raising costs’ asset classes. There is no forecast capex allocated to the ‘Buildings’ and ‘Equity raising costs’ asset classes, while the tax remaining life for the ‘Capitalised Leases 1 July 2023’ asset class reflect the average of remaining terms of leases as at 1 July 2023.

19 NGR, r. 87A(1).

Table 7-3 AER's final decision on AusNet's standard and remaining tax asset lives as at 1 July 2023 (years)

Asset class	Standard tax asset life[a]	Remaining tax asset life[b]
Transmission pipelines	20.0	25.7
Distribution pipelines	20.0	34.2
Service pipes	20.0	36.4
Cathodic Protection	n/a	n/a
Supply regulators/Valve stations	20.0	29.6
Meters	15.0	12.1
SCADA and remote control	10.0	7.2
Other - IT	4.0	2.9
Other - non-IT	4.0	3.5
Buildings	35.0	12.2
Land	n/a	n/a
Capitalised leases 1 July 2023	n/a	6.6
Cathodic protection - post 1998	20.0	20.7
Equity raising costs	5.0	0.5

Source: AER analysis.

(a) All new assets use the diminishing value method of tax depreciation.

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

n/a Not applicable. We have not assigned a standard tax asset life and remaining tax asset life to some asset classes because the assets allocated to them are non-depreciating assets or there is no forecast capex allocated to the asset class.

7.2 Assessment approach

For this final decision, with the exception for the value of imputation credits (gamma), we have followed 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.[20]

The gamma input for AusNet is 0.57 for this final decision. This is consistent with the 2022 *Rate of Return Instrument*, which requires us to use a gamma value of 0.57.[21] Refer to Attachment 3 for further discussion on this matter.

20 AER, *Draft decision: AusNet Gas Services Access Arrangement 2023–28, Attachment 7 – Corporate income tax*, September 2022, pp. 8–14.

21 AER, *Rate of Return Instrument*, February 2023, p. 19.

Glossary

Term	Definition
2018 tax review	2018 review of the regulatory tax approach
AER	Australian Energy Regulator
ATO	Australian Tax Office
AusNet	AusNet Gas Services
capex	Capital expenditure
ITAA	Income Tax Assessment Act 1997
NGR	National Gas Rules
opex	Operating expenditure
PTRM	Post-tax revenue model
RFM	Roll forward model
RIN	Regulatory Information Notice
SaaS	Software as a Service
TAB	Tax asset base