

Submission

UÉ Revenue Control 4 (2025-2029) Submission

Revenue Allowances Paper
*(incl. reconciliation of IFRS to Regulatory
Opex and Capex)*

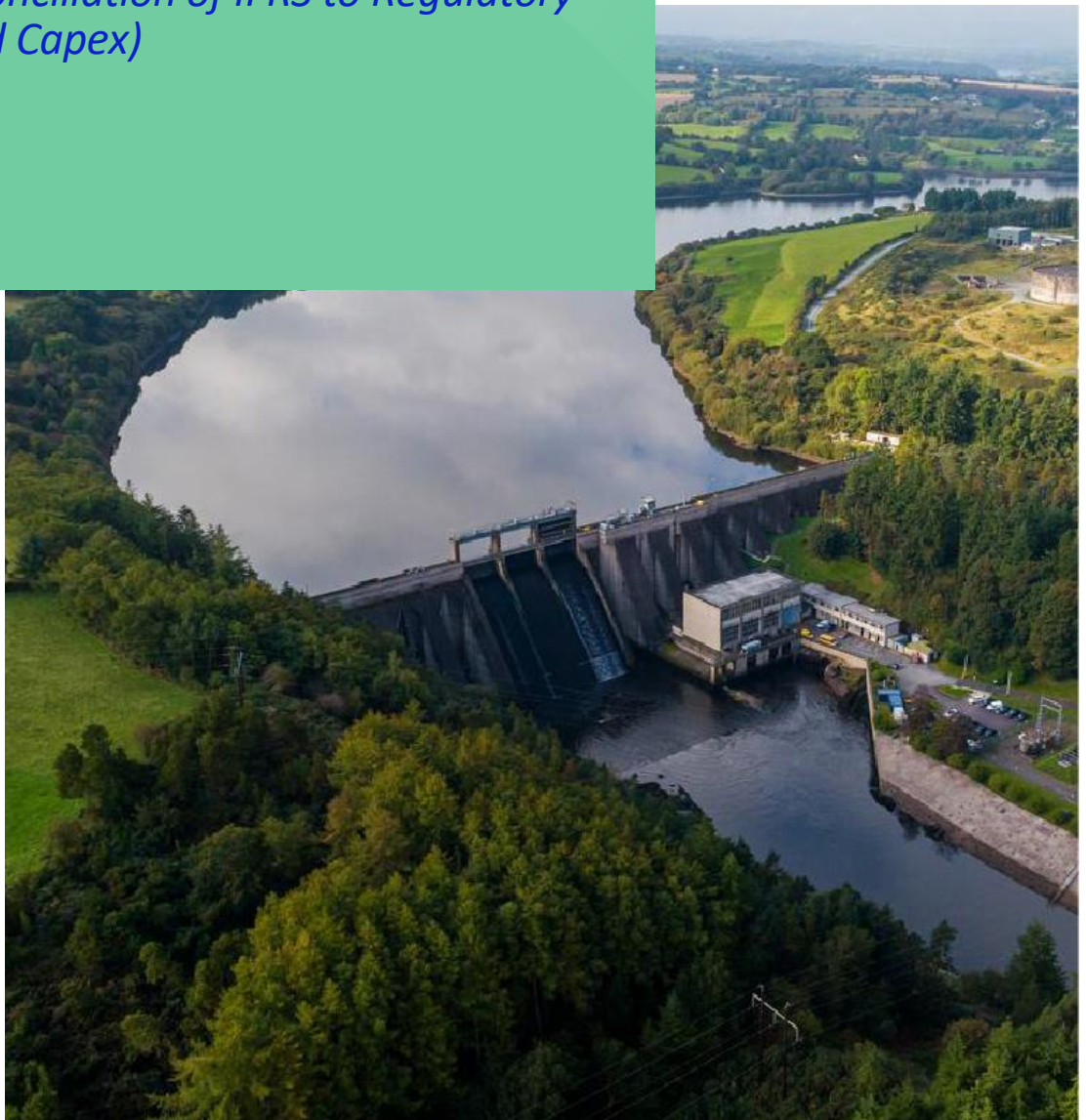


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1 Executive Summary

Under legislative provisions, Uisce Éireann (UÉ) is required to submit to the Minister of Housing, Local Government and Heritage a multi-annual Strategic Funding Plan (SFP). In summary, the SFP sets out the capital and operational costs likely to be incurred over a multi-annual period and how these costs are expected to be recovered, from customers and government funding. The funding allocations set out in the SFP reflect the upper ceiling that would be provided by the Government to fund UÉ's operations and investments, with final funding allocations being confirmed based on the outcome of the Commission for Regulation of Utilities (CRU) revenue control process.

This paper summarises the UÉ approach and basis for the projected revenue allowances included in the SFP, so that the CRU can clearly understand how UÉ has applied the regulatory model for the SFP / Revenue Control 4 (RC4) period of 2025-2029.

The revenue allowances are calculated and based on the current regulatory model / building blocks method.

UÉ's detailed operational and capital requirements are set out in separate RC4 submissions for CRU review. However, in the Appendix of this paper, the bridges of **1. IFRS to regulatory operational costs** and **2. IFRS to regulatory capital costs** are included. This is to ensure that the reconciliations between the operational and capital costs presented in the SFP versus the equivalent regulatory figures are clear and transparent, particularly with regard to the adjustments UÉ has made.

2 Background and Overview

2.1 UÉ Regulatory Model

UÉ is a regulated utility, and a building blocks method is applied by the CRU to determine its total revenue allowance. The level of revenue is reflective of the investment in the Regulated Asset Base (RAB) and recovery of efficiently incurred operational costs. The regulated model follows a 'HICP – X' methodology, where cost allowances adjust for annual inflation and for expected efficiency improvements over time.

The revenue that is recovered from UÉ's non-domestic customers and from Government subvention during each revenue control period can be divided into the following separate categories / building blocks:

1. Revenue to cover UÉ's efficiently incurred operational costs during the period,
2. A return on capital invested in UÉ's RAB, through application of the weighted average cost of capital (WACC),
3. Revenue to cover depreciation of UÉ's RAB, and
4. K-Factor

Excluding the impacts of any potential k-factor, the revenue structure allows for the **reimbursement of opex and capex** costs incurred (via building blocks 1 and 2) and revenue to cover **depreciation** (free cash flow, via building block 3).

Total allowed revenue currently comprises of subvention income and non-domestic revenue, with future excess usage charges to form part of the regulated revenues on introduction and implementation.

As noted above, the revenue value includes allowances for operating costs, return on capital costs, depreciation and an adjustment for revenue relating to the previous revenue control period(s) which is known as a k-factor:

2.2 Allowed Revenue Calculation



	Total Allowed Revenue	Non-Domestic Revenue	Domestic Revenue
Allowed Revenue Calculation	Calculated based on the regulatory model , with recovery of operating costs, return on capital invested (WACC), depreciation allowance and k-factor.	Calculated with reference to the % of total revenue that should be allocated to non-domestic customers, aligned to CRU approved tariffs and consumption forecasts.	Calculated with reference to the % of total revenue that should be allocated to domestic customers, representing the balancing figure once non-domestic revenue projection is determined.

UÉ’s calculation of its projected allowed revenue total for 2025-2029 is aligned to the building blocks method and **includes UÉ’s estimated k-factor**. The allowed revenue has been calculated by treating 2025 as a stand-alone year (due to the timings of Government 2025 budget versus the CRU’s RC4 determination) with impact of the k-factor and smoothing over remaining four years of RC4 (*i.e.*, 2026-2029) as provisionally agreed with the CRU. **All building blocks** are subject to CRU review and approval.

2.3 Domestic vs Non-Domestic Apportionment

The domestic versus non-domestic apportionment is currently based on subvention income versus non-domestic revenue.

Under this approach, costs are allocated to UÉ’s customer groups (domestic and non-domestic) by using cost drivers such as the share of water delivered, population equivalent (a measure of the load/strength of wastewater), or the number of connections. The relative costs of serving each customer group are calculated ensuring equitable and cost reflective tariffs are calculated. The CRU’s 2019 decision on the Non Domestic Tariff Framework (NDTFR) established that c. 23% of UÉ’s total allowed revenue should be allocated for recovery from non-domestic customers with the remaining c.77% allocated to the domestic customer group. As the harmonised

tariff framework represented a movement away from individual Local Authority (LA) charges, transitional arrangements were approved by the CRU.

While it was therefore recognised that the optimal allocation could not be recovered immediately through non-domestic revenues, it was intended that billing transitions over RC3 2020-24 would move the achieved rate close to the optimal allocation; 77% domestic / 23% non-domestic. However, UÉ has been unable to increase non-domestic revenue at the expected rates due to the impacts of COVID-19, resulting in delays to the NDTFR harmonization, which was originally due to begin on 1st of May 2020 and was then postponed to 1st of October 2021. As a result, UÉ has not recovered the full amount of allowed revenue set out in the RC3 regulatory decision and further details have been set out in UÉ's RC3 K-Factor submission.

An allowed revenue split of 81.8% domestic and 18.2% non-domestic was arrived at as part of the Government Budgetary Revised Estimates decision for 2021 and was determined by calculating the total allowed revenue for the year and subtracting non-domestic revenue. This split was reflected in the Government Estimates for 2021, 2022 and 2023 and UÉ maintained alignment to this in its funding request for 2024¹. The level of subvention requested is calculated as the amount that maintains the 81.8% / 18.2% split between subvention and non-domestic revenue, given forecast non-domestic revenue for the following year. This is done to maintain the domestic versus non-domestic apportionment throughout an increasing operational and capital profile. This approach was discussed and agreed with the DHLGH as part of our funding requests.

Following a re-assessment, the up-to-date optimal allocation has moved to c.76% domestic / c.24% non-domestic (as referenced in the CRU's July 2024 decision on the Non-Domestic Tariff Framework). UÉ's SFP / RC4 projections for 2025 are moving to a domestic versus non-domestic split of 79.2% / 20.8%². The reason for the delta is an expected transitional phase over a number of years (particularly in relation to Trade Effluent tariffs), with an allocation of 76.5% / 23.5%³ forecast to be achieved in 2029⁴. Given UÉ's capital investment profile, the WACC and Depreciation building blocks will continue to drive growth in allowed revenues. Longer term affordability and tariff sustainability is therefore an issue which merits consideration.

1 The Government's 2024 budget allocation to UÉ was lower than UÉ's request.

2 The Government's 2025 budget allocation to UÉ is lower than UÉ's request (capital ask is fully aligned, but change in funding mix).

3 Based on a projection of expected growth in non-domestic revenue over the RC4 period, but subject to CRU decision(s) on Non-Domestic tariffs over the period, including any transition arrangements.

2.4 Return on Capital Invested (WACC) and Depreciation

In order to produce a full SFP submission, including a projection of allowed revenues, a provisional WACC value was required by UÉ. Recognising that the RC4 process would determine the ultimate WACC for 2025 to 2029, the CRU indicated that for the purposes of the SFP calculations, UÉ should continue to align to peers, and adopt a provisional WACC at **3.65%**.

UÉ has applied this in its calculation of allowed revenue for the SFP / RC4 period. However, it is important to note the impact of a peer WACC in the context of the scale of UÉ's proposed capital investment programme and therefore growth of its RAB.

The estimated RAB projection, on which the 'return on capital' and 'depreciation' building blocks are based (incorporating certain assumptions and thus subject to change), is set out below:

RAB Profile 2025-29* (€m - Nominal)	2025	2026	2027	2028	2029
Closing RAB	9,626	10,945	12,531	14,831	17,748

* RAB based on 2024 Forecast and SFP 2025-2029

Depreciation is calculated in the SFP as per the existing methodology previously determined by the CRU.

2.5 Non-Domestic Tariff Framework Review (NDTFR)

In October 2021, UÉ implemented the CRU approved national harmonised charging regime. The NDTFR harmonized these 500+ tariffs nationally into one suite of tariffs, with some customers facing increases as a result. This created a more transparent and equitable system of charging for non-domestic water and wastewater customers.

The non-domestic tariffs were implemented on the 1st of October 2021, with transitional arrangements (including bill capping) in place until 30th of September 2024.

The updated NDTFR decided by the CRU in July 2024 provides for:

- An updated suite of tariffs to apply from 1st of October 2024 to 30th September 2025 that reflect up-to-date revenue and customer input data. This ensures costs are allocated across tariff classes and services in an equitable and transparent manner and in line with the framework's cost allocation rules.
- A national set of harmonised charging arrangements to apply to **connections licensed to discharge trade effluent** into UÉ's wastewater network. However, these charges will not come into effect until 1st October 2026.

A key objective of tariff reform is to have an equitable system of charges where all connections pay cost-reflective tariffs and thus pay the same price for the same service. Furthermore, extended bill capping is an additional cost that is currently carried by the Exchequer. Therefore, the CRU has decided that all non-domestic connections should transition to the prevailing cost-reflective tariffs for water and wastewater services (excluding trade effluent) by the 1st October 2026. A consultation on transition arrangements for trade effluent charges to apply from 1st October 2026 is expected in 2025.

These changes are designed to align to national and EU policy objectives and promote conservation, greater cost reflectivity, more efficient price signals to customers and create stronger incentives to reduce the volume and strength of trade effluent discharged into the wastewater network.

UÉ has incorporated the CRU's decision paper of July 2024 within the SFP / RC4 projections, with certain assumptions made post 30th September 2025 (acknowledging that CRU decision(s) on tariffs and transition arrangements are expected over that period).

As outlined earlier, the output of UÉ's latest cost allocation analysis indicates that non-domestic customers should contribute c.24% of its total allowed revenue, which is a slight increase from the share of c.23% determined in 2019.

3 Revenue Allowances

3.1 Total Allowed Revenue

The table below sets out UÉ's projection of allowed revenues included in the SFP, including a forecast of recovery from each source.

Allowed Revenue Analysis *(€m Nominal)	2025	2026	2027	2028	2029
Allowed Revenue	1,652	1,924	2,034	2,150	2,273
Subvention	1,308	1,515	1,566	1,650	1,738
Excess Usage Charges	0	0	1	1	1
Non-Domestic Revenue	344	409	467	499	534
Domestic %	79.2%	78.7%	77.0%	76.8%	76.5%
Non-Domestic %	20.8%	21.3%	23.0%	23.2%	23.5%
Subvention YoY growth %	19.3%	15.8%	3.4%	5.4%	5.5%
Non-Domestic YoY growth %	26.1%	18.8%	14.1%	6.9%	7.1%

Table 3.1 * Allowed Revenue based on 2024 Forecast and SFP 2025-2029

Year on year uplift in allowed revenue in 2025 versus 2024 is €283m.

There is a total increase of €642m in subvention and €261m in non-domestic revenue projected over the 5-year period. On a percentage basis, this equates to a 59% uplift by the Exchequer by 2029 (versus 2024), and a 96% uplift from the non-domestic customer base.

The tables below provide a further breakout of non-domestic revenue projections.

3.2 Non-Domestic Revenue

Core Non-Domestic (€m⁵)	2025	2026	2027	2028	2029
Core baseline	221	248	318	381	434
NDTFR Uplift	26	69	62	51	25
Other Uplift	1	1	1	1	1
Total Core Revenue	248	318	381	434	460

Miscellaneous Non-Domestic (€m)	2025	2026	2027	2028	2029
Trade Effluent ⁶	19	21	26	32	41
Non-Trade Effluent	1	1	1	1	1
Fluoridation	5	5	5	5	5
Total Miscellaneous Revenue	26	28	33	39	47

Total Non-Domestic (€m)	2025	2026	2027	2028	2029
Total Non-Domestic Revenue	344	409	467	499	534

⁵ These projections were developed at a point in time for SFP purposes and include certain assumptions. It is acknowledged that the CRU has yet to make determinations on RC4 allowances and tariffs.

⁶ Reflects only TE revenue currently recorded as miscellaneous. Some TE customers are currently charged non-domestic tariffs and the projected revenue for these customers continues to be reflected as part of the non-domestic line.

4 Differences between Regulatory and Funding Model

UÉ's projection of allowed revenue in the SFP is calculated in line with the opex, WACC and depreciation building blocks, in addition to UÉ's estimated k-factor. UÉ's RC4 submissions will be reviewed by the CRU, with individual allowances set which will determine UÉ's actual allowed revenue over the 5-years.

On an annual basis, UÉ will submit its Exchequer funding request for the following year to the DHLGH. The expectation is that this funding request will be set in the context of UÉ's CRU approved allowances for that year. However, the funding decision by the DHLGH may potentially differ, due to the Government's annual budgetary process, with UÉ funding competing with other interests, macro-economic factors, and Government affordability.

UÉ determines its requested split of subvention between operational and capital, by allocating 100% of non-domestic revenue cash in the first instance against total operational expenditure. The balance of the operational funding requirement is then funded by current subvention. The remainder of subvention is allocated to capital. This has the effect of maintaining the current subvention at an appropriate level.

The operational and capital portions of allowed revenue from a funding perspective are not equal to the operational and capital building blocks under the regulatory model. This is due to the following:

- Delta between the non-domestic revenue figure and the non-domestic revenue cash collected in year (timing difference of tariff versus calendar year, lag in billing and level of bad debts each year), and
- Working capital differences (in line with credit terms, contract milestone payments, etc.) on costs incurred and costs paid for in a calendar year.

5 Challenges and Considerations

5.1 Allowed Revenue Profile

Allowed revenue is likely to continue to increase in line with growth in the RAB, with two of the three building blocks (excluding k-factor) being capital related. The RAB will continue to grow until such time as the annual capital expenditure value drops below the value of the depreciation component. This is likely to be a significant number of years away.

In addition, two large national strategic projects, WSP and GDD, are anticipated to incur significant levels of investment in the RC4 period ahead of completion in the 2030s. These two projects will drive increases in allowed revenue due to the growth in the RAB and depreciation.

The **affordability** of the increased levels of allowed revenue will be a key challenge and will place increased pressure on both the Exchequer (subvention) and non-domestic customers (tariffs). This affordability will have to be assessed over the RC4 period and beyond in the context of the known capital investment requirements which will span multiple revenue controls.

5.2 Polluter Pays Principle

The Water Framework Directive and in particular the **polluter pays** principle is a key consideration with respect to tariff setting and the apportionment between domestic and non-domestic revenues. Under the current approach to setting allowed revenues, an increasing RAB means achieving the balance between cost reflectivity and customer affordability is therefore a key challenge.

5.3 Peer WACC

The scale of UÉ's capital investment programme is unique amongst its peers. A peer WACC will drive increases in the 'return on capital' component of allowed revenue in line with the growth of the RAB. In late 2018, the CRU explored⁷ alternatives to its standard approach to WACC, taking into account the then recent change to the UÉ funding model which saw the domestic sector being funded from the Exchequer. Ultimately, the CRU decided⁸ to maintain the standard approach to WACC for RC3 but identified a need for future review to ensure suitable reflection of the funding arrangements in place. RC4 presents another opportunity for such a review. In this

⁷ CRU/18240

⁸ CRU/19/148

context, it is acknowledged that a Working Group on the Future Funding of Uisce Éireann has yet to conclude.

5.4 RAB Separation

in the context of the level of known capital needs across the water and wastewater asset base, a view could be taken that under the existing model, the current customer base will bear the undue burden of a legacy of underinvestment due to the 'catch-up' in capital investment required on an ongoing basis for the foreseeable future. An alternative to increasing non-domestic tariffs in line with the overall capital requirement and total allowed revenue, is potentially splitting the RAB between that relating to current / future customers versus that related to the past and the legacy under-investment.

5.5 Working Group on the Future Funding of Uisce Éireann

In the context of the above challenges and considerations, it is acknowledged that a Working Group on the Future Funding of Uisce Éireann has yet to conclude.

Appendix 1 – Reconciliation of IFRS to Regulatory Opex

Opex - 2022 prices (€m)	2025	2026	2027	2028	2029	Total
Total IFRS Opex	1,123	1,158	1,161	1,173	1,197	5,812
First Fix	(7)	(7)	(7)	(7)	(7)	(36)
Meter Maintenance	(0)	(0)	(0)	(0)	(0)	(2)
IT SAAS	(1)	(1)	(1)	(1)	(1)	(4)
UÉT	(18)	0	0	0	0	(18)
CIP Development Costs	(53)	(65)	(67)	(68)	(68)	(321)
Customer Strategies	(7)	(4)	(4)	(4)	(4)	(23)
CDS Regulatory Activities	(3)	(2)	(2)	(2)	(2)	(10)
Non-Domestic Bad Debt Provision	(28)	(31)	(29)	(29)	(30)	(146)
OBS provision - Wrap Around liability	(3)	(2)	(2)	(2)	(2)	(12)
IAS 19 Pension	(2)	(3)	(4)	(4)	(4)	(17)
Leases	5	5	5	5	4	23
Innovation cost funded through RC3 allowance	(3)	(1)	0	0	0	(4)
Total Regulatory Opex	1,003	1,046	1,050	1,061	1,083	5,242

Appendix 2 – Reconciliation of IFRS to Regulatory Capex

Capex - 2022 prices (€m)	2025	2026	2027	2028	2029	Total
Total IFRS Capex (excl. Capitalized Interest)	1,296	1,323	1,541	2,143	2,634	8,938
First Fix	7	7	7	7	7	36
Meter Maintenance	0	0	0	0	0	2
IT SAAS	1	1	1	1	1	4
UÉT	18	0	0	0	0	18
CIP Development Costs	53	65	67	68	68	321
Customer Strategies	7	4	4	4	4	23
CDS Regulatory Activities	3	2	2	2	2	10
OBS Liability Settlement	0	11	11	10	10	42
New Connections & Dev. Levies Revenue	(166)	(165)	(166)	(168)	(169)	(834)
Total Regulatory Capex	1,220	1,248	1,467	2,067	2,558	8,560

* Values in look forward submissions reflect updated 2024 inflation rates (from 2% to 1.7% based on Central Bank's quarterly bulletin).