

# Information on the methodology used to set the regulated revenue of the transmission system operator

In accordance with Article 19 and Annex I of European Union Regulation 2024/1789, to ensure transparency regarding the methodologies, parameters, and values used to determine the allowed or target revenues of transmission system operators.

JOINT STOCK COMPANY “CONEXUS BALTIC GRID”

2025



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## 1. Responsible entity

The Public Utilities Commission (hereinafter – the Regulator) develops and approves methodologies related to tariff calculation, capital cost, and the calculation of the regulatory asset base for the natural gas transmission system service. The Joint Stock Company “Conexus Baltic Grid” (hereinafter – the natural gas transmission system operator), in accordance with the methodologies established by the Regulator, performs the tariff calculation, which is reviewed and approved by the Regulator. The Regulator calculates and determines the rate of return on capital (the weighted average cost of capital, or WACC).

## 2. Methodology

### a) Overall methodology

The revenues from the natural gas transmission system service are determined using the revenue cap method, in accordance with the [Public Utilities Commission’s Board Decision No. 1/7 of July 13, 2023, “Methodology for Calculating the Natural Gas Transmission System Service Tariff”](#) (hereinafter – the tariff methodology). The calculation is based on a cost base that includes the following expenses necessary for the effective provision of the natural gas transmission system service:

- 1) Capital costs (depreciation and the cost of capital)
- 2) Operational costs (tax expenses, operating expenses)
- 3) Revenue adjustment for the previous regulatory period (if a new regulatory period begins) or tariff period (if a new tariff period begins).
- 4) Mutual compensation between transmission system operators of the unified natural gas transmission entry-exit system (hereinafter – ITC) (reduces allowed revenues).

Allowed revenues are equal to the eligible costs minus the mutual compensation within ITC. Allowed revenues apply to the national transmission system and the cross-border transmission system (exit to Lithuania). Revenues from the national transmission system are generated from the fee for using the exit point for supplying Latvian users, which is calculated by dividing the national transmission system revenues by the forecasted natural gas consumption during.

The regulatory period is set from December 1, 2023, to September 30, 2026, and includes two tariff periods:

- 1) December 1, 2023, to September 30, 2025 (22 months)
- 2) October 1, 2025, to September 30, 2026 (12 months)

## **b) Methodology to set the regulatory asset base (RAB)**

The regulated asset base (RAB) is determined in accordance with the [Public Utilities Commission’s Board Decision No. 1/12 of August 29, 2022, “Methodology for Accounting and Calculating Capital Costs”](#) (hereinafter – the capital cost methodology).

The value of the regulated asset base (RAB) includes:

- I. Intangible assets;
- II. Fixed assets (land plots, real estate (buildings and structures); technological equipment and machinery; other fixed assets and inventory);
- III. Payments recorded as assets for participation in international natural gas transmission infrastructure development projects;
- IV. Liabilities arising from decisions on the allocation of investment costs adopted in accordance with Regulation (EU) No. 347/2013 of the European Parliament and of the Council of April 17, 2013, on guidelines for trans-European energy infrastructure, which repeals Decision No. 1364/2006/EC and amends Regulations (EC) No. 713/2009, No. 714/2009, and No. 715/2009.

RAB does not include financial investments, accounts receivable, securities and equity participations, cash, inventories, costs related to the creation of fixed assets and unfinished construction projects, costs related to the creation of intangible assets, as well as the portion of asset value financed by financial assistance or support from the state, municipality, foreign entities, the European Union, or other international organizations and institutions. It also excludes fixed assets or portions thereof acquired through user-paid connection fees, and fixed assets or portions thereof acquired free of charge. RAB does not include value changes resulting from the revaluation of assets or portions of assets created using funds from other parties.

**i) Methodology to determine the initial (opening) value of the assets as applied at the start of the relevant regulatory period and when incorporating new assets to the RAB**

Assets are recorded at their acquisition value in accordance with international accounting standards.

**ii) Methodology to re-evaluate assets**

1) Asset revaluation methodology – the most recent revaluation of fixed assets was carried out in 2020. The revaluation was performed by independent certified appraisers, who determined the depreciated replacement value: the initial value, accumulated depreciation, and residual value for each revalued fixed asset. The cost approach method was used in the revaluation, based on average construction and acquisition costs in Latvia.

2) In RAB value calculations, the balance sheet value at year-end from the most recent publicly available annual financial statement is used for assets or parts of assets, excluding the impact of any revaluation performed after December 31, 2021.

3) According to capital cost methodology, natural gas transmission system operator that performed its most recent asset revaluation or partial revaluation by December 31, 2020, may use indexed RAB values for the period from the last revaluation until December 31, 2021, in the tariff project calculation for determining capital cost values, provided that justification is submitted to the Regulator and the average annual (January–December) change in the consumer price index is applied.

**iii) Explanations of the evolution of the value of the assets**

The RAB value is fixed for the entire regulatory period as at December 31, 2022, and is set at EUR 221 853.2 thousand

**iv) Treatment of decommissioned assets**

Decommissioned assets are removed from the RAB after they are written off or sold.

The natural gas transmission system operator may recover asset write-off costs related to investments made before the end of the useful life of the written-off assets, if such investments were made in accordance with the 10-year development plan of the natural gas system operator approved by

the Regulator. Asset write-off costs are adjusted by deducting revenues from the disposal of the written-off asset.

#### v) Depreciation methodology applied to the RAB, including any changes applied to the values

The minimum depreciation periods for different asset groups are specified in Annex 3 of the capital cost methodology.

#### c) Methodology to set the cost of capital

The cost of capital is determined based on the capital cost methodology, which defines the calculation of the return on capital (Weighted Average Cost of Capital or WACC).

#### d) Methodology to determine the total expenditure (TOTEX) or, if applicable, operational expenditure (OPEX) and capital expenditure (CAPEX)

Capital costs are calculated based on the capital cost methodology. The RAB base and WACC rate are fixed for the entire regulatory period. When determining the amount of revenue adjustment at the beginning of a new regulatory period, the capital cost adjustment is taken into account, which is defined as the difference between the planned and actual capital costs during the regulatory period.

Operational costs are calculated based on the tariff methodology. Operational costs include the transmission system operator's technologically and economically justified expenses necessary for the efficient provision of the transmission system service. Operational costs include:

- Operating expenses (costs of natural gas losses and technological processes, personnel and social costs, costs necessary for regular property maintenance and performed maintenance repairs, other business activity costs).
- Tax expenses.

Total costs consist of capital costs (depreciation and the cost of capital), operating costs, and tax expenses.

#### e) Methodology to determine the efficiency of the cost

No cost efficiency methodology is applied.

#### f) Methodology applied to set the inflation

The forecast for inflation and changes in nominal gross wage corresponds to the projections by the Bank of Latvia.

#### g) Methodology to determine premia and incentives

The cost efficiency coefficient is applied to the natural gas transmission operator in accordance with the tariff methodology. It is applied to the costs calculated from the total costs of the national and cross-border transmission system, excluding the regulatory account revenue adjustment, natural gas supply costs, applicable taxes, and mutual compensation between ITC natural gas transmission operators.

#### h) Non-controllable costs

Non-controllable costs include:

- 1) Cost increases caused by inflation.
- 2) Cost increases in personnel expenses due to changes in nominal gross wages.
- 3) Changes in the price of natural gas related to the gas consumed for technological processes and losses.
- 4) Natural gas costs related to energy security reserves.
- 5) Justified actual unforeseen costs due to changes in external regulatory acts or emergency situations, which occurred in the previous or current tariff period of the respective regulatory period and cannot be recovered otherwise.

#### i) Services provided within the company holding

The Joint Stock Company “Conexus Baltic Grid” operates as an independent company. Services from the group are purchased in insignificant volumes. Tariff methodology does not specify requirements regarding the purchase of services from a group company.



### 3. Values of the parameters used in the methodology

#### a) Detailed values of the parameters that are part of the cost of equity and cost of debt or weighted average cost of capital expressed in percentages

The rate of return on capital is calculated in accordance with the capital cost methodology.

The real WACC rate for the regulatory period from 01.12.2023 to 30.09.2026 is 2.72%, which was in effect at the time of the tariff project approval, in accordance with the [decision No. 177 of the Public Utilities Commission dated 22 September 2022, "On the rate of return on capital for the calculation of the tariff project for natural gas transmission system, natural gas distribution system, and natural gas storage services."](#) Detailed information on the included values is available in the decision.

#### b) Depreciation periods in years applicable separately to pipelines and compressors

The minimum depreciation periods for the respective assets, as specified in Annex 3 of the capital cost methodology, are:

- 1) Natural gas pipelines and steel pipelines – 60 years
- 2) Compressors – 20 years

#### c) Changes to the depreciation period or in the acceleration of the depreciation applied to assets

There have been no changes to the depreciation period, and no accelerated depreciation has been applied to the RAB assets. The depreciation rates applied in the tariffs correspond to the minimum depreciation periods specified for different asset groups in the capital cost methodology.

#### d) Efficiency targets in percentages

According to [the Regulator's decision No. 119 of 26 October 2023 "On the natural gas transmission system service tariffs of the Joint Stock Company Conexus Baltic Grid"](#), the transmission system operator must achieve a 1.25% cost savings during the regulatory period. This is applied to costs calculated from the total costs of the national and cross-border transmission

system, excluding the regulatory account revenue adjustment, natural gas supply security costs, applicable taxes, and mutual compensations between natural gas transmission system operators within the ITC.

#### e) Inflation indices

The following indices are applied to operating costs during the regulatory period:

	2024	2025	2026
Consumer Price Index (CPI) (year-on-year), %	2.3%	2.5%	2.5%
Nominal gross wage (annual change; %)	8.2%	7.8%	7.8%

#### f) Premia and incentives

Premia and incentives are not applied.

## 4. Values of costs and expenditure that are used for setting the allowed or target revenue in euro

#### a) RAB per asset type detailed per year until its full depreciation

Net value of RAB fixed assets at the end of the calendar year by type (thousand EUR):

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2022	2 307	200 452	17 270	1 824
2023	1 778	192 801	16 073	1 351
2024	1 388	184 969	14 898	949
2025	1 123	177 273	13 783	644
2026	876	169 672	12 708	439
2027	703	162 091	11 685	303
2028	557	154 541	10 718	208
2029	411	147 021	9 781	134

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2030	307	139 534	8 960	79
2031	204	132 074	8 166	34
2032	101	124 645	7 393	4
2033	0	117 226	6 638	3
2034	0	109 863	5 899	2
2035	0	102 625	5 175	1
2036	0	95 447	4 485	0
2037	0	88 373	3 840	0
2038	0	81 383	3 278	0
2039	0	74 617	2 767	0
2040	0	68 030	2 313	0
2041	0	61 645	1 895	0
2042	0	55 427	1 503	0
2043	0	49 372	1 224	0
2044	0	44 219	993	0
2045	0	40 010	817	0
2046	0	36 032	645	0
2047	0	32 633	501	0
2048	0	29 762	367	0
2049	0	27 434	276	0
2050	0	25 168	190	0
2051	0	23 123	106	0
2052	0	21 545	58	0
2053	0	19 997	32	0
2054	0	18 477	14	0
2055	0	17 596	1	0
2056	0	16 721	0	0
2057	0	15 872	0	0
2058	0	15 025	0	0
2059	0	14 178	0	0
2060	0	13 332	0	0
2061	0	12 495	0	0
2062	0	11 750	0	0
2063	0	11 007	0	0
2064	0	10 268	0	0
2065	0	9 579	0	0
2066	0	8 991	0	0
2067	0	8 407	0	0
2068	0	7 830	0	0

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2069	0	7 253	0	0
2070	0	6 676	0	0
2071	0	6 120	0	0
2072	0	5 660	0	0
2073	0	5 202	0	0
2074	0	4 749	0	0
2075	0	4 306	0	0
2076	0	4 086	0	0
2077	0	3 967	0	0
2078	0	3 855	0	0
2079	0	3 754	0	0
2080	0	3 663	0	0
2081	0	3 614	0	0
2082	0	3 566	0	0
2083	0	3 523	0	0
2084	0	3 480	0	0
2085	0	3 437	0	0
2086	0	3 394	0	0
2087	0	3 352	0	0
2088	0	3 310	0	0
2089	0	3 268	0	0
2090	0	3 226	0	0
2091	0	3 183	0	0
2092	0	3 141	0	0
2093	0	3 100	0	0
2094	0	3 059	0	0
2095	0	3 029	0	0
2096	0	3 000	0	0
2097	0	2 973	0	0
2098	0	2 946	0	0
2099	0	2 918	0	0
2100	0	2 892	0	0

i) Investments added to the RAB, per asset type

RAB is fixed for the entire regulatory period in the amount of EUR 221 853.2 thousand and investments are not added to it.

ii) Depreciation per asset type until the full depreciation of the assets

Depreciation by asset type in calendar years (thousand EUR):

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2023	478	7 648	1 197	457
2024	348	7 830	1 175	388
2025	246	7 693	1 115	295
2026	228	7 598	1 075	198
2027	167	7 578	1 023	130
2028	143	7 547	966	90
2029	142	7 517	937	71
2030	104	7 484	820	53
2031	103	7 457	794	44
2032	102	7 427	773	29
2033	101	7 416	755	1
2034	0	7 360	738	1
2035	0	7 235	724	1
2036	0	7 175	690	1
2037	0	7 072	645	0
2038	0	6 987	562	0
2039	0	6 763	511	0
2040	0	6 584	453	0
2041	0	6 382	418	0
2042	0	6 216	391	0
2043	0	6 054	279	0
2044	0	5 151	231	0
2045	0	4 208	177	0
2046	0	3 976	172	0
2047	0	3 397	144	0
2048	0	2 870	135	0
2049	0	2 326	90	0
2050	0	2 265	86	0
2051	0	2 044	84	0
2052	0	1 577	47	0
2053	0	1 548	26	0
2054	0	1 519	18	0
2055	0	881	13	0
2056	0	874	1	0
2057	0	849	0	0

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2058	0	846	0	0
2059	0	846	0	0
2060	0	846	0	0
2061	0	836	0	0
2062	0	744	0	0
2063	0	742	0	0
2064	0	739	0	0
2065	0	688	0	0
2066	0	587	0	0
2067	0	584	0	0
2068	0	577	0	0
2069	0	576	0	0
2070	0	576	0	0
2071	0	555	0	0
2072	0	460	0	0
2073	0	457	0	0
2074	0	453	0	0
2075	0	442	0	0
2076	0	219	0	0
2077	0	118	0	0
2078	0	111	0	0
2079	0	101	0	0
2080	0	90	0	0
2081	0	48	0	0
2082	0	47	0	0
2083	0	43	0	0
2084	0	43	0	0
2085	0	43	0	0
2086	0	42	0	0
2087	0	42	0	0
2088	0	42	0	0
2089	0	41	0	0
2090	0	41	0	0
2091	0	41	0	0
2092	0	41	0	0
2093	0	41	0	0
2094	0	41	0	0
2095	0	29	0	0
2096	0	28	0	0

Calendar year	Intangible assets	Land, buildings, and engineering structures	Technological equipment and devices	Other fixed assets
2097	0	27	0	0
2098	0	26	0	0
2099	0	26	0	0
2100	0	26	0	0
2101+	0	789	0	0

## b) Cost of capital including the cost of equity and the cost of debt

WACC rate is determined by a [decision](#) of the Regulator's Board and is fixed for the entire regulatory period. For the regulatory period from 01.12.2023 to 30.09.2026, the real WACC rate is set at 2.72%.

Indicator	Label	Set value
Real weighted average cost of capital	$WACC$	2.72%
Risk-free rate	$r_f$	0.39%
Country risk premium	$r_c$	0.52%
Equity beta	$\beta_e$	0.74
Market risk premium	$r_m$	5.25%
Industry asset beta	$\beta_a$	0.41
Industry average debt-to-equity	$D/E$	1
Cost of debt	$r_d$	2.49%
Cost of equity	$r_e$	4.80%
Tax rate	$t$	20%
Equity-to-assets ratio	$\frac{E}{(D + E)}$	0.5
Debt-to-assets ratio	$\frac{D}{(D + E)}$	0.5
Consumer price index	$PCI_{izm}$	1.49%

### c) Operational expenditure

Expenditure (thousand EUR)	First tariff period (01.12.2023. -30.09.2025.)	Second tariff period (01.10.2025. - 30.09.2026.)
<b>Operating costs</b>	<b>27 911.7</b>	<b>16 746.4</b>
Natural gas transmission loss and technological process support costs	1 307.5	816.6
Personnel and social costs	8 676.1	5 279.9
Costs for regular property maintenance and performed operational repairs	5 541.7	3 234.7
Other operating expenses (including support functions)	12 386.4	7 415.2
<b>Taxes</b>	<b>820.6</b>	<b>447.6</b>

### d) Premia and incentives detailed separately per item

Natural gas transmission system operator must achieve a 1.25% cost savings during the regulatory period. This is applied to costs calculated from the total costs of the national and cross-border transmission system, excluding the regulatory account revenue adjustment, natural gas supply security costs, applicable taxes, and mutual compensation between FinEstLat natural gas transmission system operators.

## 5. Financial indicators

Indicators	2022	2023	2024
a) EBITDA (thousand EUR)	18 787	12 489	20 245
b) EBIT (thousand EUR)	8 466	2 529	5 106
c) EBITDA/RAB	1.09%	5.63%	9.13%
d) EBIT/RAB	0.49%	1.14%	2.30%
e) ROE	0.66%	0.60%	2.41%
i) RoCE	3.91%	1.15%	2.41%
ii) leverage ratio (net debt/equity)	0.32	0.27	0.17
iii) (net debt)/(net debt + equity)	0.24	0.21	0.14
iv) net debt/EBITDA	2.79	3.59	1.23

Definitions:

- a) earnings before interest, taxes, depreciation and amortisation (EBITDA);



- b) earnings before interest and taxes (EBIT);
- c) return on assets I (ROA) =  $\text{EBITDA} / \text{RAB}$ ;
- d) return on assets II (ROA) =  $\text{EBIT} / \text{RAB}$ ;
- e) return on equity (ROE) =  $\text{Net Profit} / \text{Equity}$ :
- i) return on capital employed (RoCE) =  $\text{EBIT} / (\text{equity} + \text{long-term liabilities})$ ;
- ii) leverage ratio =  $\text{net debt}^* / \text{equity}$ ;
- iii)  $\text{net debt} / (\text{net debt} + \text{equity})$ ;
- iv)  $\text{net debt} / \text{EBITDA}$ .

\* net debt = outstanding liabilities to financial institutions – cash and cash equivalents

## 6. Simplified tariff model.

A simplified calculation of the natural gas transmission system service tariff is available [here](#).