

# Revenue Generating Guidelines

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## 1. INTRODUCTION

This guideline describes how revenues from projects funded by the EEA/Norwegian Financial Mechanism will have an impact on the grant rate. The potential for projects to generate income is generally recognised as a positive contribution to their long-term sustainability. As such, income-generating proposals should be encouraged rather than discouraged.

When revenue is generated by the project, it should pay for the operating costs and may also contribute to some capital costs of the project. This could mean that the project has the capacity to attract other sources of finance. Indeed, the resources generated can serve to reimburse the loans obtained from International Financial Institutions or from commercial institutions. The present value of the future excess profit (see definition below) should be considered in the calculation of the grant rate, as it reduces the need for grant financing.

Guidelines on revenue generating projects are referred to in Article 3.2.1 of the Rules and Procedures for the implementation of the EEA Financial Mechanism, Article 3.2.1 of the Rules and Procedures for the implementation of the Norwegian Financial Mechanism, Article 1.3 of the guidelines on individual projects, programmes and block grants and Article 5.2 and 5.4 in the application form user guide.

### 1.1 Definition

**'Profit'** is revenues less running costs including repayment of loans.

**'Profit margin'** is profit divided by revenues and expressed in percentage.

**'Excess profit'** is revenues multiplied by the sum of profit margin less 10 years Government bond interest (or equivalent) in the beneficiary state + 2%.

## 2. TAKING REVENUES AND PROFIT INTO ACCOUNT

The guideline provides a simple and transparent approach to considering issues of revenue generation and it is the obligation of the applicant to give a full explanation of all project income needs, revenue flows and profit generating potential during the projects economic lifetime.

### 2.1 Economic lifetime

The lifetime varies according to the nature of the investment. It is longer for civil engineering works (30-40 years) than for technical installations (10-15 years), or IT equipment (3 years). In the case of a mixed investment comprising civil engineering works and installations, the lifetime of the investment may be fixed on the basis of the lifetime of the principal infrastructure.

The lifetime may also be determined by considerations of a legal or administrative nature, for example the duration of the concession where a concession has been granted.

### 2.2 Estimation of future revenues and profit

The applicant is required to identify and estimate the future revenues and profit during the economic lifetime. The profit ("net revenue") equals estimated revenues less estimated running costs which include direct and indirect staff costs, consumables, maintenance & repair, publicity, etc., as well as financing costs (including repayments of loans).

### 2.3 Residual value

In the case of assets with a very long life, a residual value may be added to the end of the appraisal period to reflect their potential resale value of continuing use value.

### 3. SETTING THE GRANT RATE

It is the applicants' responsibility to identify, justify and calculate the potential profit and excess profit. The identification should cover the economic lifetime of the project.

Excess profit will have an impact on the grant rate offered. The following formulas illustrate such an impact:

Budget	Economic lifetime		
	Y1	Y2	Yn
Revenues	R1	R2	Rn
Running costs	RC1	RC2	RCn
Profit	R1 - RC1	R2 - RC2	Rn - RCn
<i>Profit margin (profit/revenues)</i>	$PM1 = (R1 - RC1) / R1 * 100 \%$	$PM2 = (R2 - RC2) / R2 * 100 \%$	$PMn = (Rn - RCn) / Rn * 100 \%$
<i>Government bond + 2 %</i>	GB + 2%	GB + 2%	GB + 2%
<i>Excess profit %</i>	$PM1 - (GB + 2\%)$	$PM2 - (GB + 2\%)$	$PMn - (GB + 2\%)$
<i>Excess profit EURO</i>	$R1 * [PM1 - (GB + 2\%)]$	$R2 * [PM2 - (GB + 2\%)]$	$Rn * [PMn - (GB + 2\%)]$
<i>Discounted excess profit</i>	$= \frac{R1 * [PM1 - (GB + 2\%)]}{[1 + (GB + 2\%)]^1}$	$+ \frac{R2 * [PM2 - (GB + 2\%)]}{[1 + (GB + 2\%)]^2}$	$+ \frac{Rn * [PMn - (GB + 2\%)]}{[1 + (GB + 2\%)]^n}$

The grant rate applied for will be reduced by the discounted excess profit.

The impact is further illustrated with the following scenario:

Budget	Economic lifetime							
	Y1	Y2	Y3	Y4	Y5	Y6	Y7	Yn..
Revenues	10	15	20	20	20	20	20	20
Running costs	10	13	15	15	15	15	15	15
<b>Profit</b>	<b>0</b>	<b>2</b>	<b>5</b>	<b>5</b>	<b>5</b>	<b>5</b>	<b>5</b>	<b>5</b>
<i>Profit margin (profit/revenues)</i>	0%	13%	25%	25%	25%	25%	25%	25%
<i>Government bond + 2 %</i>	8%	8%	8%	8%	8%	8%	8%	8%
<i>Excess profit %</i>	-	5%	17%	17%	17%	17%	17%	17%
<i>Excess profit EURO</i>	0	0.8	3.4	3.4	3.4	3.4	3.4	3.4
<i>Discounted excess profit</i>	14	<i>Discount rate equal government bond + 2%</i>						
<b>Impact on the grant rate:</b>								
Grant applied for	100.0	Assuming the co-financing rate is 15% the excess profit is reduced equally, e.g. $14 \times 0.85 = 11.9$						
Excess profit discounted	11.9							
<b>Grant offered</b>	<b>88.1</b>							

If the actual excess profits and/or the government bond interest deviate significantly from the budget the Financial Mechanism Committee and/or the Norwegian Ministry of Affairs might adjust the grant assistance during the project period.

#### 4. AUDITS AND FINANCIAL CONTROL

Audits and financial control are carried out in accordance with Article 6 of the Rules and Procedures of the EEA Financial Mechanism and Article 6 of the Rules and Procedures of the Norwegian Financial Mechanism.