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The Exchange  
Belgard Square North  
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Dublin 24  
Ireland

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First Union Lists of Projects of Common Interest – Project 5.2  

Twinning of Southwest Scotland Onshore System (SWSOS) between Brighouse Bay and Cluden

Dear Denis  

We write in relation to the above and specifically further to the publication by the EU Commission on 21st November 2014 of the EU Commission List of Actions selected for receiving financial assistance under CEF-Energy.

Background to the Projects of Common Interest Process  

As you are aware, the Project of Common Interest No. 5.2, the twinning of the southwest Scotland onshore system (“the Project”), has been selected as a Project of Common Interest for the purpose of EU funding within the CEF-Energy programme pursuant to the terms of Regulation (EU) No. 347/2013 (“the TEN-E Regulation”).

You will recall that the Project was entered into the First Union List of Projects of Common Interest as published by the EU Commission on 14 October 2013. The Project promoter is Gaslink Independent System Operator Limited and the Project sponsor is BGE (UK) Limited. The sponsor will be responsible for the execution of the project.

Since the selection of the project as a Project of Common Interest, both the promoter and the sponsor have been taking steps under the TEN-E Regulation and CEF-Energy for the purpose of advancing and ultimately executing the Project. As a National Regulatory Authority (“NRA”) under the Regulation, the CER is aware that the Project promoter and sponsor have engaged both with the CER and also with Ofgem and NIAUR under the terms of Chapter IV of the Regulation. In particular the promoter and the sponsor have engaged with the NRAs with respect to cost-benefit analysis under Article 11 of the Regulation. In addition, the project sponsor and promoter have engaged in discussions with the CER concerning cross-border cost-allocation (CBCA) within the terms of Article 12 of the TEN-E
Regulation\(^1\). The outcome of the CBCA process was that it was agreed on 24\(^{th}\) June 2014 that there would be no allocation of costs to other relevant jurisdictions (i.e. Northern Ireland and Great Britain) and that therefore 100\% of the costs of the project would be allocated to the Republic of Ireland.

Furthermore, the Project promoter and sponsor have participated in the CEF-Energy First Call for Funding, and submitted the Project application to the facility on 18\(^{th}\) August 2014. On 21\(^{st}\) November 2014, the EU Commission published the List of Actions selected for receiving financial assistance under CEF-Energy and the Project was identified as being eligible for the sum of €33.76m. Of the 248 projects on the First Union List of Projects of Common Interest, only 34 projects were identified as being eligible for funding.

The majority of the money being awarded (€647m) is earmarked for 6 major works projects of which the Project received the 4\(^{th}\) highest allocation. It is significant that the Project, located in the Ireland/UK region, received such a sizeable allocation of CEF funding.

The €33.76m is a significant contribution to the projected capital costs of executing the Project. The Project promoter and sponsor met with the EU Commission Innovation & Networks Executive Agency ("INEA") at their request on the 20\(^{th}\) November 2014 to discuss plans to implement the Project, were a Grant Agreement to be signed. INEA, as the CEF-Energy funding agency, requires the promoter and sponsor to regularly update it on Project progress and on steps taken within the TEN-E Regulation.

On the 26\(^{th}\) November, the Project promoter and sponsor received confirmation from INEA that our application for financial assistance successfully passed the evaluation under the CEF Energy 2014 call. Further engagement with INEA is expected in January in order to progress matters relating to a Grant Agreement.

**The SWSOS Network**

The Project has been promoted by the promoter and sponsor as being critically important to enhancing the Security of Supply for the natural gas industry in Ireland, the wider energy industry, and indeed the economy of the country. A failure on the single section of pipeline, in the absence of alternative sources of supply, would lead to a loss of supply to the entire island for a period ranging between 2 to 14 days. Were a section of one of the parallel pipes to fail, the SWSOS would still have the capacity to transport the required gas flows via Moffat. Therefore, with the Project, we ascribe what is for all intents and purposes an almost zero probability of supply outage.

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\(^1\) Investment Request Letter to CER 31\(^{st}\) October 2013; CBCA proposal to CER 7\(^{th}\) November 2013; Meeting with CER, Ofgem and NIAUR on 21\(^{st}\) February 2014; Provision of further information as requested by CER over the period December 19\(^{th}\) 2013 to 1\(^{st}\) April, 2014; Letter to CER acknowledging draft CBCA decision on 28\(^{th}\) May 2014.
Other benefits to the gas system from this project include increased system flexibility, reduced compressor fuel usage and increased entry capacity availability. However security of supply remains the most critical reason for undertaking the project.

The gas network is critical to the Irish economy. Ireland and Northern Ireland are currently highly dependent on gas flows via Moffat, being the main source of gas supply from Great Britain to the island of Ireland. This dependence poses a significant security of supply risk. In 2012, the International Energy Agency noted that “Ireland has limited indigenous fossil fuel resources – the country remains dependent on imported oil and gas and will remain so in the long term... Ireland is thus vulnerable to a gas supply disruption, and would benefit significantly if there were a greater diversification and flexibility of supply in terms of entry points and sources... The interconnectors are critical to the gas supply for Ireland.” This viewpoint backed up the statement by the ESRI in their 2011 Review of Irish Energy Policy that Ireland is vulnerable to any difficulties with a single pipeline.

As part of its 2012 decision in relation to the Price Control 3 process, the CER stated that they and their consultants were of the view that there was a case for the twinning of the SWSOS network in the longer term.

**The Long Term View**

In its most recent Ten Year Network Development statement, Gaslink forecast that Corrib flows will decline from 2019/2020. Despite Corrib potentially providing up to 74% of annual demand for the Republic of Ireland it will only be able to provide up to 40% of the forecast winter peak gas requirement. Moffat will continue to be the significant marginal supply source for Ireland and any outage on the interconnector infrastructure would have serious repercussions for the Irish energy system and economy, a point which was also made in the 2011 ESRI paper.

We believe that the success in obtaining grant aid towards the Project necessitates all concerned parties (CER, the TSO, Industry, Government) giving serious consideration to progressing the Project in order to deliver it within the proposed timelines. The acceptance of the grant aid requires agreeing to be bound to conditions in the associated agreement with the European Commission which commits to timelines which would deliver the project by end Q4 2016/Q1 2017.

While the availability of the Corrib Entry point reduces the reliance of the Irish Energy System on the Moffat Entry point it will not eliminate it, either in the short or long term, and the twinning the SWSOS will be required within the next 5 to 10 years regardless of flows from Corrib.

There is significant benefit of undertaking the Project in the near-term at a cost of €60m (inclusive of the grant aid), relative to the total cost of the project of €93.8m (without the grant aid) at a later date. Our analysis (attached) shows that the cost in Net Present Value terms of recovering the €60m spent in 2016 would be €13m less than if the full €93.8m were spent 5 years later with no grant aid (the Regulated Rate of Return of 5.2% is used as
the discount rate in the analysis). This analysis only takes into account the cost that the gas customer would be underwriting through the tariff and does not account for the benefits of the Security of Supply for the 5 year period or indeed any of the other benefits previously highlighted.

The impact on gas customer of the inclusion of c.€60m in the Transmission RAB will result in a negligible increase for the domestic gas customer – less than 0.5%. As you are no doubt aware, this is due to the fact that the end price paid by almost all gas customer's bills is inclusive of both a distribution and transmission tariff, and the fact that energy commodity prices and taxation make up the majority of those bills.

The analysis that we have previously shared with the CER shows that the transmission element of the transportation cost of gas sourced via Moffat will increase by only 3%. The security of supply benefits that the project will deliver should be viewed as delivering excellent value for money for all gas customers.

As highlighted, the grant aid award is contingent on the project progressing in line with the submitted timelines. If the PCI grant monies are not availed of in 2015, there is no guarantee that monies would be allocated to the project at some point in the future. Having been successful in the first PCI List, it was taken as given that we should not submit the project for the 2nd PCI List. The 3rd call is unlikely to occur until 2016/17. A key success factor for this proposal was the maturity of the project – its urgency and the ability of the Project to be delivered in a timely fashion was clearly demonstrated. The number of projects from around Europe scoring highly in this regard will without doubt increase with each ensuing PCI list. As the competition for a diminishing CEF Fund increases, so too will the risk that we would not be successful in securing the same amount of funding in the future, if any at all.

A further aspect of the PCI competition that will mitigate against our being successful in the future is the introduction of an Energy System Wide Cost Benefit Analysis that will assess the impact of each project on the entire energy system of Europe. The weighting attached to this project will be negligible in comparison to much larger projects being proposed in other parts of mainland Europe.

It would be impossible for anybody to estimate with any degree of confidence that grant aid may be available for any individual project for subsequent CEF funding awards.

**Investment Request**

Consequently, we now revert to the CER as the designated NRA for the purpose of initiating discussion on the approval of the Project and the inclusion of costs in the Transmission Asset Base within the terms of the TEN-E Regulation and specifically Article 13. Given that the PCI process is designed to accelerate projects that provide increased security of supply benefit, we have been presented with tight timelines by the INEA. Therefore we would request that the CER consider this as a pressing matter as we would foresee that the INEA will expect conclusion of the Grant Agreement process in early Q1 2015.
Yours sincerely

Aidan O Sullivan
Gaslink Independent System Operator
Project Promoter

Padraic O Connell
BGE (UK) Limited
Project Sponsor

cc: John Melvin, CER