



Irish Offshore
Operators'
Association

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Barry Hussey,

Commission for Energy Regulation,
The Exchange,
Belgard Square North,
Tallaght,
Dublin 24

30 January 2015

By email: bhussey@cer.ie

Re: Consultation CER14795 – Twinning of Scotland Onshore System

Dear Barry,

IOOA's members welcome the opportunity to comment on this consultation paper. IOOA's members note that both peak and annual Irish gas demand have fallen drastically in the last few years. From Gaslink's Network Development Statement (NDS) 2014 it is forecasted that peak demand will increase by 6% between 2014 and 2023 but base demand will drop by 2% over the same period. Based on the above IOOA's members are surprised that GNI wishes to proceed with the twinning project at this time.

CER Investment Approval Benchmarks - In the CER Commentary section of the NDS 2014, the CER stated that investment by GNI in its twinning project must be necessary, appropriate and efficient before the CER will approve expenditure on the project. It is clear that approving investment in the twinning project at this time is neither necessary nor appropriate nor efficient. The key question is whether the CER should approve the twinning project in 2015 due to the availability of the grant monies (36% project costs) when clearly the project is neither necessary nor appropriate nor efficient.

History of Inefficient Investment - There has been a history of inefficient investment at Moffat by GNI; IC2 has only actually been required on a low number of occasions and it is one of the main reasons that the tariffing regime for the GNI network is currently changing. IOOA's members are concerned that if the twinning project is approved at this time that the CER is making the same mistake again – approving investments in infrastructure that will not be required with the Irish consumer picking up the cost of the inefficient investment.

If the CER proceeds with approving GNI's twinning project then the CER should give a commitment that the building of the twinning project will not lead to additional stranded capacity at Moffat that the Irish consumer will be required to pay for.

Market Uncertainty – IOOA's members are concerned that GNI wishes to proceed with the twinning project in 2015 when it is not required at a minimum until 2020 and there is huge uncertainty around the inputs that determine the twinning project's requirement in the first place. Many factors in the coming years may change the gas supply / demand outlook for Ireland postponing or negating the need for this project (e.g. development of SLNG, tie back of satellite



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gas fields at Corrib / Inch, ramp up of bio methane supplies, construction of Ireland France electricity interconnector, impact of renewables, effects of efficiency and SMART metering on Irish gas demand, or policy change to provide extension of PSO levy to peat generation stations).

The CER in the NDS 2014 acknowledges that longer term forecasts by their nature are less reliable. The CER also states that with the new network codes, potential changes to the Irish electricity system due to I-SEM market structure and increasing levels of renewables that *"it is difficult to say with confidence what gas demand will be in the medium term"*. In addition, the CER in its Cross Border Cost Allocation (CBCA) for the twinning project (CER 14137a) states that it is unable to allocate the benefits of the twinning project between the South and the North due to the uncertainty of benefits that the project will provide.

NDS 2012 outlined that the potential constraint at Moffat would occur in 2014/15 and again in 2018/19. NDS 2013 and NDS 2014 outlined that the potential constraint at Moffat may occur in 2020/21. The requirement and timing for the twinning project will probably change in future NDSs. It is farcical with all this level of uncertainty around what gas demand / supply picture will be in 2020 and that the twinning project is essence shovel ready so can be operational from date of approval in less than two years that the CER or GNI can be supporting the twinning project at this time. The CER should delay approving this project, as any prudent responsible company should, until it is absolutely certain that the project is required and meets the CER benchmarks of being necessary, appropriate and efficient.

Net Present Value (NPV) Benefit – GNI forecast a NPV benefit of €12.7million with proceeding with the project now when compared to developing the project in five years' time with no grant aid. The level of the peak gas demand at Moffat for 2020/21 and 2021/22 forecasted in NDS 2014 is lower than that forecasted for 2014/15; therefore the project could not be considered as being required until 2022/23 thus halving the perceived NPV benefit. If the project were to be postponed until 2024 the perceived NPV benefit will be eroded. It should also be noted that if grant aid of 18% or greater was received in 2020 then the NPV analysis presented by GNI would determine that waiting to develop the twinning project in five years' time would be the better option. The NPV benefit forecasted by GNI does not take account of whether the asset is actually needed and the NPV of the project from an Irish consumer's perspective will of course be very negative if it transpires it is not required.

The risk associated with this project and whether it is actually required is high. If a merchant operator were considering investing in such a project a higher rate of return would be required to reflect the riskiness of this project; Gaslink in its Energy Call for Proposals document (Section 3.16 - CER14795b) propose a merchant project discount rate of 10%. If a 10% rate of return is used then the NPV benefit of completing the project now disappears when compared to completing the project with no grant funding in 2020. IOOA's members would require a rate of return greatly in excess of 10% which means that even with the availability of the grant that a merchant operator would not proceed with this project. It is perverse that since GNI can socialise any under recovery on the twinning project due to inefficient investment then it can justify a positive perceived NPV benefit of investing now before infrastructure is required whereas a private business would choose



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to forgo the opportunity for grant aid due to the riskiness associated with revenues from this project.

Incremental Capacity - The CER has stated in its decision on the previous twinning project consultation (section 9.3.5 of CER 12196) that "*additional network investment should be based on an assessment of market demand*" and "*it may be appropriate to carry out a market test as part of any future decision on subsequent major reinforcement of the onshore Scotland network*". The CAM network code on incremental capacity provides for this as well. At a minimum a market demand test should be implemented for this capacity to determine that the long term market interest in this capacity – to date this has not been completed by GNI and capacity bookings at Moffat do not indicate that additional capacity is required by industry.

Physical Reverse Flow – The consultation states that the twinning project is a prerequisite for physical reverse flow with 40% of the physical reverse flow costs associated with the twinning project – IOOA's members note that twinning of onshore Scotland is not required for physical reverse flow; based on existing capacity in IC1 it is possible (with some modifications but not twinning) that flows twice the size of the Corrib field could be reverse flowed without twinning.

In addition, the CER should only consider building infrastructure to support physical reverse flow when there is a market requirement for such a service. If physical reverse flow is required in Ireland, the construction of the infrastructure to support this should be underwritten by the parties requiring the service and not by the general consumer at this time. If there is merit in a joint project then it should be advanced as such with all the benefits and costs clearly considered on both sides. Furthermore, alternatives like realising access to Northern Ireland via current connectors could be more economic.

Security of Supply – The CER in its consultation states that the security of supply benefit alone provided by the twinning project is justification in itself for the project. IOOA's members reject this claim; the twinning project does not necessarily improve security of supply - if an emergency occurs and gas is not available from GB then there is no security of supply benefit from the twinning project. Security of supply is better served through diversity of supply such as indigenous gas fields, LNG terminals, bio methane, shale gas, alternative sources of generation and access to other electricity markets; twinning of one pipeline does not necessarily increase the security of supply to a country and cannot be the basis to justify the capital expenditure.

End User Costs – Changes in the tariffing methodology are on-going in part due to inefficient investment at Moffat which may increase end user tariffs. Nevertheless, GNI is willing to increase costs to consumer further by building additional infrastructure that is not required. GNI in its Energy Call for Proposal submission (CER14795b) stated that "*a tariff increase would cause further affordability issues for domestic customers*" yet in it is looking to increase the interconnector network tariff by 6.27% for a project that is clearly not required at this time.

Cross Border Cost Allocation (CBCA) - The CBCA agreement letter issued by the CER (CER14137a) in May'14 stated that "*the CER's view, in light of the recent decline in throughput the Irish interconnectors, is that this increase in tariffs could not be sustained at present.*" This was



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based on a NPV cost to the end consumer of €47.9million (appears that a 50% grant was assumed as part of the modelling exercise by GNI). The NPV cost to the end user as outlined in the CER 14795c is now €60million (grant proposed is 36%). Why has the CER changed its position in eight months when the expected costs from twinning in NPV terms will be €12.1million higher than that outlined in the CBCA?

GNI outlined that building the twinning project and pushing costs of €47.9m (50% overall project costs) onto end users will not push up end user tariffs but if the 100% cost of the project is applied then transmission tariffs will increase by 10%. How could this be the case? IOOA's members are at a loss as to how this could occur.

IOOA's members are concerned that whilst Northern Ireland customers will receive 12% of the perceived benefits of the proposed twinning project that Northern Ireland customers will not be paying for any of the costs of using the proposed twinning project. Is this fair to the Irish consumers? If Northern Ireland customers whom are solely reliant on the Moffat entry point for gas supply do not require the twinning project then should customers in Ireland with multiple entry points require it?

Peak Day Alternatives - A sizeable element of Irish peak demand is power generation, presumably in a low wind scenario. Has the CER or GNI considered the market based mechanisms as an alternative to committing to a capital project now for what may be a potential issue in 2020 and for what is surely of short duration (e.g. switch a power station to GO/HFO or offer interruptible capacity to consumers and interrupt on the peak day)? Using market based alternatives will give better price signals to consumers in such a peak event rather than years of smeared project costs where everyone pays irrespective of their peak contribution. Committing to the twinning project at this stage will dampen peak day market signals. It seems improper that the CER would allow GNI to commit to this capital project when market based alternatives, for what is period of short duration, are available.

IOOA's members thank the CER for the opportunity to respond to this consultation and are available to discuss the contents of this letter with the CER if required.

Yours sincerely,

Steve Boldy
Chairman IOOA Gas Sub-Committee and on behalf of:

Azeire Petroleum
Cairn Energy,
Chrysaor,
Eni,
ExxonMobil,



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San Leon Energy,
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Shell,
Statoil,
Vermilion Energy Ireland,
Woodside.

Cc: Patrick Shannon Chairman IOOA
IOOA Management Committee
IOOA Gas Sub-Committee