Fitzwilliam Hall,
25 – 26 Fitzwilliam Place,
Dublin 2.

Mr. Clive Bowers,
Commission for Energy Regulation,
The Exchange,
Belgard Square North,
Tallaght,
Dublin 24.

15 August 2008

Re: Consultation on Transmission Tariff Methodology and Regulation in Ireland and Northern Ireland

Dear Clive,

As part of the Common Arrangements for Gas (CAG) project, the regulatory authorities published a consultation entitled "Transmission Tariff Methodology and Regulation in Ireland and Northern Ireland" on the 27th of June 2008.

Before responding to some of the issues raised in the consultation paper, we would reiterate the following points made in our letter to the CER dated the 16th of May 2008:

- A robust set of principles for entry tariff design should first be established by the regulatory authorities, in agreement with industry representatives, before evaluating the various tariff options;
- The pipeline owners / operators should be tasked to develop entry tariffs consistent with the agreed set of principles – we believe this approach will put the onus on finding a satisfactory solution on the parties best placed to achieve it; and
- We believe there are serious risks associated with evaluating the various options using a financial model. Any solution that is not founded on a set of principles which are shown to be sustainable by testing over a wide range of expected market conditions will be constantly subject to challenge and will not provide the necessary regulatory stability.

Although not in the context of the CAG project, Shannon LNG submitted correspondence to the CER in April 2007 regarding transmission tariffs (see Annex 1). The correspondence included a proposal on an entry tariff methodology that would produce reasonably stable tariffs over a long term period. The methodology was consistent with the following principles:

- Entry tariffs are calculated based on the actual costs associated with the entry infrastructure – gas from different supply points can compete on the basis of its fundamental economics;

- Entry tariffs should facilitate gas supply competition between entry points in Ireland;

- There should be no cross subsidies between entry points – this encourages competition and efficiency;

- Entry tariffs should be reasonably stable and predictable over the long term; and

- Entry tariff design should encourage efficient, necessary and market driven investments in natural gas infrastructure in the future.

We suggest that a set of principles such as that outlined above should be developed and agreed by industry representatives in conjunction with the regulators, before proceeding to detailed assessment of entry tariff options.

We therefore do not believe it is appropriate to comment on some of the detailed questions posed in the consultation paper until there is agreement on a set of entry tariff principles. We outline some high level comments on the consultation paper below.

Postalised Entry Tariffs

The Department of Communications, Marine and Natural Resources commissioned a report in 2000 on an appropriate tariff structure for Ireland. Some extracts of the reports key findings are quoted unabridged below[1]:

- *A fully postalised tariff regime could be expected to raise costs in the long term.*

- *A fully postalised system would impose a tax on indigenous production and cross-subsidise the existing interconnector, promoting inefficiency and higher prices in the long run.*

- *A fully postalised system is discriminatory and would be inefficient, as it cross-subsidises imported gas. For example, gas deliveries from Kinsale would be forced to contribute to the cost of the existing interconnector, even though Kinsale gas does not use the asset. Such discrimination is clearly incompatible with the Gas Directive.*

- *The Full Postalised Tariff would require an alternative supplier to pay for a substantial part of BGE's network (interconnector) for which that alternative supplier would have no need, while also bearing the cost of his own infrastructure…In effect, the application of the Full Postalised Tariff to a privately funded supplier is a subsidisation of BGE.*

- *Full Postalisation is incompatible with the EU Gas Directive.*

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[1] New Pipeline Authorisation and Third-party Access Tariffs for the Natural Gas Network in Ireland - July 2000, The Brattle Group. http://www.dcenr.gov.ie/NR/exeres/4722B54B-70B0-44B5-A215-3B23075F1F4D.htm

In light of the findings detailed above, we do not understand why the regulatory authorities continue to consider postalised entry tariffs, or any variation thereof, as a viable option.

Increase to Irish Balancing Point Price /
Mitigating the effect of declining interconnector utilisation

The consultation paper (section 2.1.3 and 2.1.4) suggests that new gas supply sources coming on-stream will increase the Irish Balancing Point (IBP) price. It is the assumption that annual interconnector revenue remains constant as throughput potentially declines that increases the interconnector tariff and the subsequent IBP gas price. New supply sources coming on-stream should put downward pressure on the IBP price if the transmission entry tariff is designed appropriately.

At the time the Government approved the proposal for the second interconnector, the press release stated that BGÉ and the private sector would fund the project and that separate entry tariffs would be introduced[2]. This is the basis upon which the second interconnector was approved.

Direct deliveries of natural gas to Ireland, such as expanded domestic production or LNG, should be able to benefit from their lower transportation costs (i.e. their fundamental economics) over gas imported from the UK, but should not receive a windfall as a result of quirks in the tariff design. For this reason, we believe the owners of the interconnectors should be tasked to develop long term stable tariffs that comply with a robust set of tariff design principles.

From the options presented in the consultation paper on how declining interconector utilisation is dealt with, there appears to be merit in further examination of smoothing of the interconnector tariff over a long term period in combination with profiling the recovery of depreciation according to throughput.

Assessment Criteria

The stated goal of the CAG project is to ensure "….that variations in the price and conditions on which gas is bought and sold will be determined by market conditions and economics, not by variations in regulatory arrangements".

If the stated goal is to be achieved, we suggest that the assessment criteria should include the criteria that transmission entry tariff design should allow gas supply projects to compete on the basis of their fundamental economics.

We hope these comments are helpful and we look forward to participating further in the consultation process.

Yours sincerely,

Martin Regan

Martin Regan

Enclosure: Annex 1 - Copy of Shannon LNG letter sent to the Commission for Energy Regulation dated the 16th of April 2007 with attachment.

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[2] Press release dated 27th February 2001