MINUTE

EUROPEAN COMMISSION

SECRETARIAT-GENERAL

Brussels, 27.7.2010
SG-Greffe(2010) D/ 11621

PERMANENT REPRESENTATION
OF IRELAND TO THE EUROPEAN
UNION
Rue Froissart, 50
1040 BRUXELLES

Subject: NOTIFICATION PURSUANT TO ARTICLE 297 OF THE TFEU

The Secretariat-General would be obliged if you could forward the enclosed Decision of the Commission to the Ministry for Foreign Affairs.

For the Secretary-General

Karl VON KEMPIS

Encl. : **C(2010)5300**

IE

Commission européenne, B-1049 Bruxelles / Europese Commissie, B-1049 Brussel - Belgium. Telephone: (32-2) 299 11 11.
Office: BERL 8/384. Telephone: direct line (32-2) 296.88.09. Fax: (32-2) 292.07.94.

http://ec.europa.eu/dgs/secretariat_general
E-mail: karl.von-kempis@ec.europa.eu

EUROPEAN COMMISSION

Brussels, 26.7.2010
C(2010) 5300

Subject: Exemption decision on Shannon LNG

Dear Sir,

I am writing with reference to the decision adopted by the Commission for Energy Regulation granting exemption from certain parts of the Gas Directive 2003/55/EC for the Shannon LNG terminal as received by the Commission on 27 April 2010.

The Commission has now completed its analysis of the decision and supporting material. The conclusion of this analysis is that the Commission requests the modification of the exemption decision.

The details are set out in the Annex to this letter.

Yours sincerely,

For the European Commission,

Dacian CIOLOŞ
Member of the Commission

Mr. Dennis Cagney
Commissioner
Commission for Energy Regulation
The Exchange,
Belgrad Square North, Tallaght,
Dublin 24
Ireland

Annex

1. On 15 April 2010 the Irish energy regulator, the Commission for Energy Regulation (CER) approved a request for an exemption from regulated Third party Access under Article 22 of Directive 2003/55/EC for an LNG Terminal on the Shannon estuary.

2. Article 22 provides that "Major new gas infrastructures, i.e. interconnectors between Member States, LNG and storage facilities, may, upon request, be exempted from the provisions of Articles 18, 19, 20, and 25(2), (3) and (4) under the following conditions:
    a. the investment must enhance competition in gas supply and enhance security of supply;
    b. the level of risk attached to the investment is such that the investment would not take place unless an exemption was granted;
    c. the infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that infrastructure will be built;
    d. charges are levied on users of that infrastructure;
    e. the exemption is not detrimental to competition or the effective functioning of the internal gas market, or the efficient functioning of the regulated system to which the infrastructure is connected"

3. The decision referred to at paragraph 1 was transmitted to the Commission and received at the Commission on 27 April 2010. According to the provisions of Article 22 (4) the Commission may request that the regulatory authority or the Member State concerned amend or withdraw the decision to grant an exemption.

4. One correspondent, Safety before LNG, submitted a reaction to the Commission, dated 28 April 2010, concerning the CER decision.

5. On 9 June 2010 the Commission wrote to CER requesting further information. The CER replied on 24 June 2010, including an attached letter from the project promoter, Shannon LNG Limited (hereinafter Shannon LNG) dated 22 June 2010, addressing the several points raised in the Commissions' request for information.

6. Below are set out a description of the project, the view of CER in its decision document and related documents, an outline of discussions between Shannon LNG, CER and Commission staff , and the view of the Commission based on all the information which it has received in relation to this exemption.

Description of the project.

7. Shannon LNG proposes to construct a liquefied natural gas (LNG) import terminal on a site located on the Shannon Estuary on the west coast of Ireland. The terminal will be connected to the Irish gas transmission system via a 26 KM gas pipeline. This pipeline is not part of the exemption request and will be subject to regulated third party access.

8. The site is currently owned by Shannon Development (a regional development body) with whom Shannon LNG has negotiated a purchase option following a call for proposals from Shannon Development.

9. Shannon LNG is a wholly owned subsidiary of Hess LNG Limited, a joint venture of the Hess Corporation and Poten and Partners. It is envisaged that Hess LNG Limited will establish a company, TradeCo, which will enter into a long term terminal use agreement for the terminal at Shannon, and also enter into LNG purchase and shipping agreements with upstream LNG suppliers and will seek to sell gas to wholesale purchasers in Ireland.

10. Shannon LNG writes that TradeCo and Shannon LNG wish to secure a significant portion of their LNG under long term arrangements to underwrite the financial viability of the terminal investment, permit the financing of the terminal and secure term sales commitments with down stream buyers on the Irish market.

11. Shannon LNG considers that TradeCo will only be able to enter into the long term LNG sale and purchase agreements to the extent that it can secure similar long term access to the regasification terminal, requiring a full Article 22 exemption.

12. Over 90% of Irish gas is imported through the United Kingdom. Wholesale Irish prices reflect the National Balancing Point ("NBP") price level in the UK plus an additional transportation charge. The Corrib gas field under development will have a relatively short production life (approx 6 years). At present there is only limited storage available domestically.

13. Shannon LNG Phase one of the project will amount to a peak capacity 17 mcm per day (planned base load of 11.3 mcm per day, or approximately 4 bcm per year). Shannon LNG has stated that it may in the future decide to expand the capacity (phase two), and the maximum capacity after expansion will be 28.3 mcm per day. According to the documents submitted to the Commission, Phase one could meet approximately half of Ireland's annual demand and half of its peak demand. Shannon LNG phase two could meet almost the entire Irish annual and peak demand.

14. Shannon LNG indicates that it considers that NBP will continue to set the price in Ireland, and states that its profitability is based on the avoided UK transmission tariffs.

CER exemption decision

15. The Irish regulator CER issued a consultation document on 23 July 2009, and issued a Decision paper on 15 April 2010 on Shannon LNGs request for an Article 22 exemption. CER favours granting a 25 year exemption for 100% of the capacity of Shannon LNG.

16. As a condition for the exemption CER requires Shannon LNG to implement effective rules according to which unused capacity is released ("Use It Or Lose It arrangements") taking account of the particular features of natural gas demand in Ireland and any reasonable requirements of the CER in relation to the contents of such a policy.

17. CER reserves the right to reconsider the exemption should there be a material change in the competitive structure of the Irish wholesale gas market as described in its decision paper.

18. CER does not propose to require a procedure for testing market demand (in particular an "Open Season process[1]") to ensure the terminal is correctly sized to meet market demand for LNG regasification capacity .

Market Definition

19. CER distinguishes between the wholesale market, involving shippers who predominantly source gas in the UK, and who should therefore be considered in a UK and Ireland context, and the retail market. This is in line with their decision making over recent years (e.g. in Gas Capacity Statements). CER states that their *"immediate concern is not primarily with whether Shannon LNG's gas could or could not be sold outside Ireland but rather with conditions of competition that potential customers of Shannon LNG located in Ireland may face"*[2]. This view is based on the expectation that the interconnectors between Ireland and the UK will remain uncongested which CER considers to be the key feature of the competitive structure of the Irish wholesale gas market.

The investment must enhance competition in gas supply and enhance security of supply

20. CER states that there is little doubt that Shannon LNG will enhance Ireland's security of gas supply. This is as a result of the increased geographical diversity of sources of gas that Shannon LNG would provide as well as the increased capacity margin.

21. CERs view that the Shannon LNG investment enhances competition is based on the fact that the investment will add to the margin between available capacity and demand, and that this in itself should add to the competitive pressures within the market, although it accepts that the likely scale and price impact of these competitive pressures is likely to be small.

22. CER considers it implausible that a hypothetical monopoly supplier in Ireland could permanently and profitably raise the price of order of 5%-10%, as it would only be a short time before customers in Ireland would source their gas directly in the UK[3]. The Commission understands this as meaning that CER considers that even if Shannon LNG were able to secure a large share of the Irish wholesale gas market, this market would remain contestable.

23. CER accepts that Hess has a very small share of the current gas market in the UK and Ireland. On this basis it also implicitly accepts Shannon LNG's argument that it would involve disproportionate effort to hold an Open Season given that this would only give capacity to an existing large supplier on the UK or Irish markets, which could reduce the beneficial effect on competition.

The level of risk attached to the investment is such that the investment would not take place unless an exemption is granted.

---

[1] ERGEG Guidelines for Good Practice on Open Season Procedures 21 May 2007 Ref: C06-GWG-29-05c
[2] P 18 CER Consultation Document.
[3] P 19 CER Consultation Document.

24. CER considers that the scale of the investment is such that *"it is difficult to conceive [...] of the [CER] approving a project of this scale if it were being promoted by the system operator with all the costs and risks being borne by the general gas customer"*

The infrastructure must be owned by a natural or legal person which is separate [...] from the system operators on whose systems that infrastructure will be built.

25. CER accepts that Shannon LNG is a completely separate entity to the Irish transmission system owner, Bord Gáis Éireann and operator Gaslink.

Charges are levied on users of that infrastructure

26. CER accepts that the system proposed by Shannon LNG, whereby it will charge a fee to its sister company TradeCo to recover the capital and operating costs of the terminal, meets the criterion that charges are levied on users of the infrastructure.

The exemption is not detrimental to competition or the effective functioning of the internal gas market or the efficient functioning of the regulated system to which the infrastructure is connected.

(i) exemption not detrimental to competition

27. CER is satisfied that for as long as the interconnectors with the UK are not congested – which, as already noted, they consider a key feature of the competitive structure of the Irish wholesale gas market – an exemption will not have a detrimental effect on competition. The CERs conclusion in this regard is in the context of a condition that Shannon LNG introduces effective Use It or Lose It provisions.

(ii) exemption not detrimental to effective function of internal market

28. CER considers that the Shannon LNG project is likely to increase gas supplies and diversify trade flows within the EU, and therefore is not detrimental to the internal market. It also points out that the project could free up network capacity and demands on competing sources of gas elsewhere within the EU.

(iii) effective functioning of the Irish regulated gas network

29. CER considers that the exemption will not be detrimental to the effective functioning of the Irish regulated gas network for a number of reasons: Shannon LNG will provide an additional point of pressure support to the Irish system; there will be a "Connected Systems Agreement" between the Irish TSO and Shannon LNG; Shannon LNG will operate under a licence which will require them to comply with relevant gas industry technical codes and standards

Discussions between the Commission and CER and Shannon LNG

30. Prior to the approval by CER of the exemption request and the transmission of that approval to the Commission, Commission staff held a number of meetings with CER and also with the developer Shannon LNG.

View of Commission

31. The Commission has reviewed the CER decision paper, and the related consultation paper, taking into account the submission of Shannon LNG, the additional information provided by CER and Shannon LNG including information provided at meetings between both CER and Shannon LNG and the Commission. This was done in the light of the provisions of Article 22, the Commission staff working document on Article 22 of Directive 2003/55/EC concerning common rules for the internal market in natural gas and Article 7 of Regulation (EC) No 1228/2003 on conditions for access to the network for cross-border exchanges in electricity (hereinafter "the interpretative note"), as well the decision making practice of the Commission in relation to Article 22 exemption requests.

32. The Commission's consideration of the criteria set out in Articles 22(1) (a), (b) and (e) in particular was in the context of the view set out at Paragraph 17 of the interpretive note that exemptions are an exception to the general rule of regulated Third party access and tarification. Such exceptions have to be limited to what is strictly necessary to realise the investment and the scope of the exemptions has to be proportionate.

The investment must increase security of supply

33. On the basis of its review of the documents submitted by CER and by the developers the Commission considers that the requirement in Article 22(1)(a) that the investment increases security of supply is met. This consideration is supported by the fact that it facilitates gas from a new source of supply and facilitates the flexibility of supply of gas in Ireland.

The investment must enhance competition

34. In relation to the requirement set out in Article 22(1)(a) that the investment must enhance competition, paragraph 37.4 of the interpretative note sets out that evidence should be provided as to *"the way in which capacity is (to be) allocated including the result of any market demand test conducted by the project promoters or information on any market demand test which is planned".*

35. Box 3 of the interpretative note makes clear that *"Testing market demand is a crucial element to evaluate the riskiness of a project and to assess to what extent the planned project enhances competition and security of supply. Market demand is usually tested via so-called Open Season procedures, but other methods may be acceptable as well (e.g. network development plans)".*

36. Market testing in general and open season procedures in particular justify the project dimensions and ensure that it meets effective demand. The goal of an open season is to size, tailor and allocate capacity on an efficient, transparent and non-discriminatory basis. This is also reflected in the ERGEG Guideline for Good Practice for Open Season Procedures [4]. Where an investment/exemption comes with a significant potential for expansion, with possibly significant economies of scale, which has the

[4] ERGEG Guidelines for Good Practice on Open Season Procedures 21 May 2007 Ref: C06-GWG-29-05c

effect of making competing infrastructure projects less likely, these considerations continue to be relevant for as long as the expansion potential exists.

37. An open season procedure generally consists of two phases[5]

- the assessment of the market's need (involving a preparatory phase and detailed open season notice), and
- the sponsors proposed capacity allocation and binding agreements.

38. There is no obligation on Shannon LNG to hold an Open Season process as part of the CER exemption decision. Shannon LNG have indicated that they do not wish to hold an Open Season procedure. Both Shannon LNG and CER consider that there have been sufficient market tests through the exploratory discussions which Shannon LNG has held with potential investors. Shannon LNG also stated that they "carried out the first step of an Open Season through meeting market participants". They consider that as no third party has expressed interest in capacity and the terminal is big enough to meet demand on the island of Ireland, there are no concerns regarding the undersizing of the terminal[6]. Shannon LNG wrote to CER and the Commission that "despite an extensive search, Shannon LNG has not in fact received or rejected any proposals from any third party to join the project as an investor or a long-term capacity user. No potential user has suffered discrimination". Shannon LNG also pointed to the public process by which it was awarded the right to lease the lands owned by Shannon Development for the purpose of constructing and operating an LNG terminal[7].

39. CER has stated that its view of the Irish market is that there is not a realistic possibility that an Open Season procedure would result in additional investors coming forward. Both Shannon LNG and CER consider that an Open Season procedure would result in unwarranted delay to the project at this stage. Shannon LNG considers that this amounts to a delay of three to four years, as the design and implementation has the potential to require them to go back to the public planning process.

40. CER and Shannon LNG also point out that the South Hook LNG terminal in the UK was not required to hold an open season procedure as a condition of its exemption request. On this point, it is important to note that for the UK Regulator the lack of an open season was a negative factor in its consideration of the Hook exemption request. Moreover, there were a number of special factors in the Hook decision related to the then new type of ships which would be used to transport the LNG (this was also a factor in the decision to grant a 25 year exemption)[8].

41. Both CER and Shannon LNG point out that the interpretative note acknowledges that an Open Season procedure is not the only way of testing the market.

42. The Commission considers that alternatives to an Open Season should provide an equivalent rigour in the assessment of market demand, and should guarantee an

---

[5] See also ERGEG Guidelines referred to under 4.

[6] Shannon LNG presentation to the Commission 8 April 2010. Slide 17.
[7] Shannon LNG letter to CER 17 February 2010
[8] Ofgem Final Views Application by South Hook LNG Terminal. November 2004. http://www.ofgem.gov.uk/Europe/Archive/267-04.pdf

equivalently efficient outcome, following a transparent and non-discriminatory procedure. Bilateral discussions between a developer and potential investors, which take place outside any formalised procedure, do not provide the same degree of rigour as a full open season procedure. However they may form an element in the preparatory phase of the first step of an open season procedure. In the context of Shannon LNG, the issue is whether this preparatory phase was sufficient to justify not holding a full open procedure or other more developed market testing. This must be considered in the context both of the initial investment and potential expansions of the investment.

43. Meetings between Shannon LNG and potential investors can be separated into two phases, before and after to the acquisition of Shannon LNG by Hess corporation in April 2006. Those which took place prior to April 2006 were described by Shannon LNG as *"part of a process to identify a suitable investor"* and they go on to note that despite meeting with many potential investors, including Irish energy companies and international oil and gas companies including LNG terminal operators, only Hess was willing to invest in the project.[9] Once Hess LNG acquired Shannon LNG, it is clear that its intention was to develop the terminal for its own use only, considering that *"a multi-user terminal was considered to be non viable"* and that Shannon LNG needed full control over the terminal capacity to optimize the facility utilization[10].

44. As a consequence, in considering the adequacy of the market test for the initial sizing of the terminal, only discussions held by Shannon LNG in the period prior to April 2006 are relevant. The Commission considers that those meetings which took place subsequent to April 2006 cannot be considered to be equivalent to the initial phase of an open season procedure, as it is clear that, at that stage, Shannon LNG had no intention of making any capacity available to third parties.

45. Based on an analysis of the request for exemption and other documentation submitted by Shannon LNG the Commission accepts that its business plan requires access to the initial capacity of 17 mcmd (approximately 6 bcmy). Therefore the Commission accepts that the proposed initial sizing of the terminal represents the minimum necessary terminal sizing for the project to proceed (see below for more detail).

46. However, once initiated, the Shannon LNG terminal will effectively preclude any development of alternative LNG projects in Ireland, *inter alia* due to the size of the Irish market and the impact on potential investors in competing infrastructure of the potential for expansion at Shannon LNG. Without an effective market test, expansion of LNG in Ireland would depend solely on the risk appetite, access to capital and access to upstream contracts of Shannon LNG. Parties who for whatever reason are able to access financing or gas on more favourable terms to Shannon LNG should be able to bring this competitive advantage to the market.

47. The Commission does not accept that the complexities of operating a multi-user terminal in Ireland are such that any such additional capacity could only be efficiently operated by Shannon LNG. Most LNG Terminals have multiple users, and any potential difficulties can be effectively addressed in the various agreements which would in any case be necessary between the different users and the operator of the Shannon LNG terminal.

---

9 Letter of Shannon LNG to CER 22 June 2010.

10 Ibid.

48. Further, taking into account prior knowledge in the LNG sector of the organisation of open seasons, the Commission cannot subscribe to Shannon LNG's view that the carrying out of an open season procedure would delay the project by three to four years.

49. It is over four years since there was any exchange between Shannon LNG and market participants which would allow them to express their interest in either investing or acquiring long-term capacities in the project. Therefore formal market testing regarding expansion of Shannon LNG, overseen by the CER, is required to ensure that criterion (a) of Article 22, requiring that the investment must enhance competition in gas supply, is fully met. This is in line with the view set out at paragraph 35 of the interpretative note that the competition assessment has a strong forward-looking element.

50. A formal market testing which follows the principles of an open season procedure as described in the ERGEG Guidelines for Good Practice can be considered to be adequate. The preparatory phase should begin as soon as practical. This preparatory phase should take place in the context of the existing permits received in the course of the public planning process and avoid any unnecessary delay to the project.

Downstream competition

51. Neither Shannon LNG nor Hess LNG currently participate in the retail market in Ireland. According to Shannon LNG, TradeCo will sell gas on the wholesale market in Ireland. It does not envisage restricting its counterparties in any form. Shannon LNG also indicated during meetings with Commission staff that it would make contracts with customers on the most advantageous basis in terms of long term, short term contracts etc.

52. Paragraph 34 of the interpretative note sets out that *"If a dominant undertaking [...] <u>could</u> become an indirect beneficiary by booking important amounts of capacity with the direct beneficiary, a positive competition assessment is unlikely in the absence of conditions that effectively address the competition concerns".* This can be a concern where either capacity, or the gas available from such capacity, will be contracted by the dominant undertaking in a long-term contract. The potential for Shannon LNG to supply large parts and, if the extension is realised, even the whole of the Irish market, renders this a particular concern.

53. The Irish gas incumbent BG Energy continues to enjoy significant market shares on the Irish retail markets following full liberalization in July 2007. According to the Irish regulator, BG Energy is the dominant supplier of gas in the retail market for gas suppliers to the residential sector and, arguably, the retail market for gas supplies to the small I&C sector[11]. This is confirmed by Gas Market Update – 2010 (Q1).

54. In this context, it is relevant that Shannon LNG has left entirely open the contracting practises it would employ. It should also be noted that the CER has not retained the ability in its exemption decision to remedy such anti-competitive business strategy,

---

[11] E-mail of 7/05/2010

should it occur. In such circumstances, the Commission can not consider that the conditions of paragraph 34 of the interpretative note are met.

55. Caps on capacity to be purchased by dominant companies have already been used before by the CER. For example, Condition 3 of the natural gas storage licence granted to Marathon Oil Ireland Limited [12] stipulated that this licensee was not allowed, without the prior approval of the CER, to contract with any one party for access to the Storage Facility for a period longer than three years. Also, the licensee was not allowed to contract with any one party for access to more than 75 percent of the capacity of the storage facility without the prior approval of the CER, which would not be given for a period longer than 12 months. In the case of the East-West-Cable between Ireland and the United Kingdom (connection to Wales), the license order stipulated that the beneficiary would not contract with any dominant undertaking, whether in generation or supply, for capacity over forty per cent (40%). Moreover, the project promoters have undertaken to cap the capacity available to any one party at 70%. If this cap were reached the CER would have to undertake a competition analysis before that party could purchase additional capacity[13].

56. Imposing limits to the beneficiary's discretion is consistent with previous Commission decisions pursuant to Art 22, in particular, its decision of 20 January 2010 concerning EDF's Dunkirk LNG terminal. Indeed, the Commission considered in that case that it was a necessary and proportionate measure guaranteeing the reinforcement of competition on the French retail markets that GDF SUEZ, the French gas operator dominant in the various French gas retail markets, could not reserve on a long-term basis a capacity surpassing 1 Gm^3/year (i.e. about 10% of the Terminal's initial capacity, without possible extensions).

57. In the present case, where Shannon LNG seeks to retain all capacity at the projected terminal for it self so as to resell all landed market gas to the Irish market, any limits to the beneficiaries discretion will have to apply to its volume of gas sales. In setting this limit, the Commission took account of the capacity of the Shannon LNG capacity relative to the Irish gas consumption and the level of congestion and capacity bookings in the interconnectors between Island of Ireland and the UK. The Commission considers that the Irish market is contestable once dominance has been reduced to 50%. This is as a result of the high levels of interconnection with the UK and its uncongested status. Therefore a relatively high cap - 50% - is appropriate, compared to the situation in Dunkirk, where a significantly lower cap was imposed.

The level of risk attached to the investment is such that the investment would not take place unless an exemption was granted

58. The interpretative note identifies two main risks determining the assessment of riskiness of an investment – the risk of non use of an investment and the risk of a change in costs and/or revenues in the future. The risk of non-use of infrastructure is related to the ability of users to ensure effective upstream supply and downstream demand.

---

12 http://www.cer.ie/CERDocs/cer06101.pdf

13 Interpretative note, box 4. REGULATION (EC) No 1228/2003 EXEMPTION ORDER as issued by the Irish Commission for Energy Regulation

59. As noted above, CER have stated that it is unlikely that they would support a project such as the Shannon LNG terminal if it was underwritten by consumers in general. As set out by Shannon LNG and by CER, the Irish TSO has considered and rejected the possibility of building an LNG terminal. CER state in their letter of 24 June that *"the Government White Paper on Energy published in 2007 did, it is true, address the possibility of ...LNG in the context of meeting Ireland's long term gas supply requirements. However [it] was considered strictly as commercial projects to be encouraged"*.

60. Producers prefer to sell their LNG in long term-contracts to guarantee the return on their investments; therefore Shannon LNG can only market its capacity if it can guarantee long-term capacity reservations in LNG terminals to its customers.

61. The Commission notes that the fact that CER would not support the Shannon LNG project if it was underwritten by consumers rather than by Shannon LNG is not a sufficient justification for granting an exemption from rTPA, since a company other than Shannon LNG or the Irish TSO could potentially build the terminal whilst accepting the regulated tariffs proposed by the CER.

62. However, in the absence of a guaranteed revenue stream from consumers in general, these risks must be borne entirely by the project promoter. Given the size of the Shannon LNG terminal related to the Irish market, the need to secure supplies of LNG and the ease with which Irish gas consumers can access the UK market these risks are significant enough to justify the need for an exemption. As already noted, based on analysis of the request for exemption and other documentation submitted by Shannon LNG the Commission accepts that its business plan requires access to the initial capacity of 17 mcmd (up to 6 bcmy).

63. However, the Commission is of the opinion that an exemption of more than 20 years is not necessary. In this context it is relevant that the vast majority of other exemptions for LNG terminals have been limited to 20 years or less. There are no particular technical aspects of the Shannon LNG proposal which suggest that it is exposed to particular risks in development. Long term contracts necessary to secure the investment generally run for not more than twenty years. A reasonable range of potential rates of return for a project such as Shannon LNG can be met under plausible scenarios in relation to utilisation and gross margin. Any residual risk remaining after that time is sufficiently small not to warrant an exemption.

The infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form

64. There are no reasons to consider that the requirements of Article 22(1)(c), that the infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that infrastructure will be built, are not met.

Charges are levied on users of that infrastructure are not met.

65. The structure described by Shannon LNG in its application whereby the LNG terminal will be operated by Shannon LNG and charges are levied will be levied on Trade Co for the use of the LNG terminal meets the requirements of Article 22(1)(d).

The exemption is not detrimental to competition or the effective functioning of the internal gas market, or the efficient functioning of the regulated system to which the infrastructure is connected

66. As currently drafted, the exemption states that it *"shall come into force on the date on which Shannon LNG Limited notifies the Commission for Energy Regulation in writing that all commissioning activities have been successfully completed...and it is ready to commence commercial operations"*. The impact of the exemption for Shannon LNG for other potential LNG projects in Ireland has already been noted above in the context of the criterion that the infrastructure investment must enhance competition.

67. If Shannon LNG were to continue to enjoy the possibility of an exemption despite not proceeding with a project, this would act as a disincentive to investment by other investors in Ireland and, potentially, also in the United Kingdom. Therefore it is important that the exemption loses its effect in the event the infrastructure has not become operational after a period constituting a reasonable time for the construction and commissioning of the terminal. The Commission considers that this should be five years in line with the timing included in the Shannon LNG business plan. This should be extended to a period of seven years if as a result of the market test referred to at paragraph 45 there are significant changes to the initial configuration of the terminal.

68. Otherwise the Commission concurs with the assessment of CER that the exemption for Shannon LNG terminal is not detrimental to the effective functioning of the regulated system to which it will be connected as it will provide an additional point of pressure support to the Irish system; there will be a "Connected Systems Agreement" between the Irish TSO and Shannon LNG; Shannon LNG will operate under a licence which will require then to comply with relevant gas industry technical code and standards.

69. The Commission concurs with the assessment of CER that Shannon LNG will not be detrimental to the internal market. It will not only increase security of supply for Ireland by adding a new source of gas, but it will also facilitate trading between the UK and Ireland using backhaul (interruptible reverse flow), and could eventually support the introduction of physical reverse flow.

70. In reaction to the CER decision of 15 April 2010 correspondent wrote to the Commission on 28 April 2010, raising concerns that Shannon LNG could become the sole supplier for a number of power stations located in proximity to the proposed LNG terminal if they connected to the pipeline from the Shannon LNG terminal to the main transmission grid. The Commission does not share these concerns, after having asked for additional clarifications from CER. In their letter of 24 June 2010 CER stated *"it is considered the pipeline will be treated as part of the national transmission system and connected parties will have access to gas supply from it regardless of whether*

Shannon LNG is flowing gas". The pipeline from Shannon LNG to the existing Irish transmission system will therefore be subject to regulated third party access with the obligation to provide firm capacity to any customer connected to that pipeline, therewith effectively removing reasons for concern.

Conclusion

71. In view of the above the Commission requests that the CER amend the exemption decision such that:

    a. Shannon LNG shall be obliged to organise a formal market test for interest in capacity in the facility:
        i. This procedure shall be conducted in a transparent and non-discriminatory manner;
        ii. Shannon LNG shall be obliged to meet the demand of interested parties in capacity in the terminal at least up to the maximum capacity that is considered as the total of phase one and two of the project (i.e. 28,3 mcm per day), based on tariffs for the terminal services which offer a fair rate of return for the terminal operator;
        iii. The modalities for the market test for interest in capacity in the facility and its results shall be subject to review by the Commission for Energy Regulation;
    b. Shannon LNG and TradeCo shall be obliged to ensure, under the supervision of the CER, that it will not sell more than 50% of its gas in long-term contracts (i.e. contracts with a duration of more than 1 year) to an undertaking that supplies more than 50% in any of the Irish retail gas markets.
    c. The exemption shall lose its effect five years from its adoption in the event the infrastructure has not become operational, unless the Commission decides that any delay is due to major obstacles beyond control of Shannon LNG. The exemption shall lose its effect seven years from its adoption in the event the infrastructure has not become operational if as a result of the market test referred to at point a. there are significant changes to the initial configuration of the terminal.
    d. The exemption shall have a duration of twenty years from the date of the start of operations of the terminal.

72. Therefore, by virtue of the third subparagraphs of Article 22 of Directive 2003/55/EC, the Commission hereby requests the CER to amend its exemption decision accordingly within four weeks upon receipt of the present letter and to inform the Commission of this action.