



3 May 2007

Mr J PIHLATIE
Head of Unit
Competition DG
EUROPEAN COMMISSION
Brussels B1049
Belgium

Subject: State aid No. 571/2006-Ireland RES-E support programme.

Dear Mr Pihlatie,

1. By letter dated 23rd April my authorities provided additional information regarding the REFIT support programme. The data quantified the “cost of balancing” and the “technology balancing cost” as a proportion of investment costs. My authorities have asked me to forward the following additional clarifications regarding the distribution of the remaining “unallocated” investment costs to the “market price equalisation cost” benchmarked at a price of €57 MWh to calculate the total potential transfer of state resources as notified below.

2. The “market price equalisation cost” is essential to ensure the participation of suppliers for 15 years. Its purpose and effect is to maintain the economic equilibrium of participating suppliers if the average market price of electricity to other competing suppliers who are not participating in REFIT falls and the latter would therefore enjoy a competitive advantage. My authorities submit that proportionate compensation to maintain economic equilibrium is permissible.

3. The “market price equalisation cost” is currently at zero. This will remain the case as long as production costs incorporating international fuel costs average at €57 MWh or higher. Ireland is approximately 90% dependent on fuel imports to meet its energy needs. This high dependence delivers an electricity market particularly sensitive to international oil/gas prices. This can be demonstrated by viewing the annual changes in the “Best New Entrant price” or “BNE” for electricity production where which is done in the following table.

4. Table C BNE prices 2002 -2006

Year	BNE Price* ¹
2002	€44 MWh
2003	€47 MWh
2004	€48MWh
2005	€53 MWh
2006	€66 kWh

¹ <http://www.cer.ie/en/searchresults.aspx?page=1&query=BNE&searchAttachments=false>

5 The changes in the foregoing table are due primarily to rising wholesale prices for gas (to fuel a 400 MW CCGT plant). It can be noted that at 2006 prices a reduction of the order of 14% would be required to bring the BNE back from €66 MWh to €57 megawatt hour*² (MWh).

6 As stated above (par 3) the “market price equalisation cost” is currently at zero and will remain so as long as gas prices deliver a BNE price above €57 MWh. Table B row 8 in my previous communication quantified the “unallocated” investment costs remaining after the distribution of such costs to the “cost of balancing” and the “technology balancing cost”. The following table details the possible distribution of the “unallocated” investment cost to the “market price equalisation cost” without exceeding total investments costs if the averaged market cost/price of a new entrant CCGT plant falls in years 1, 3, or 6.

7 Table C distribution of “unallocated” capital costs.

	Category→	Wind Large	Wind Small	LFG	Biomass/ hydro
		€/MWh	€/MWh	€/MWh	€/MWh
1	Unallocated capital cost distributed per MWh for 15 years – from table “B”.	€268	€235	€190	€342
2A	Unallocated capital value distributed over 15 years	€17	€15	€12	€22
2B	Permissible reduction below €57 without exceeding capital costs.	30%	26%	21%	39%
3A	Unallocated capital value distributed over 12 years	€22	€20	€16	€29
3 B	Permissible reduction below €57 without exceeding capital costs.	39%	35%	28%	50%
4	Unallocated capital value distributed over 9 years	€30	€26	€21	€38
4B	Permissible reduction below €57 without exceeding capital costs.	52%	46%	37%	66%
5	Market price	€57	€57	€57	€57
6	Notified market interest in REFIT	89%	9%	1%	1%

8. It can be noted in the first instance that in the most intensive case (lfg), market prices could fall 21% below €57 MWh (tracking a proportionate fall in gas/oil prices) and remaining at that level for 15 years without the accumulated state resource exceeding the (unallocated) investment cost. In addition as notified in par 5 above prices would have to fall 14% to price-match at €57. The accumulated reduction in gas prices would therefore be of the order of 35% from 2006 prices to match capital costs for accumulated state resources to match capital costs in the case

² The technology balancing cost has already been offset against the investment costs in Table “B” and the benchmark price across all technologies is €57 MWh.

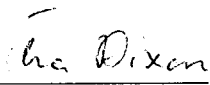
of landfill gas (lfg). If the gas price remain at or about 2006 values for 3 years the continuing reduction thereafter would have to exceed 42%. (28% + 14%) for the following 12 years in the case of lfg and of the order of 50% (35%/39% + 14%) in the case of the dominant technology wind (c98%) to match capital costs.

9. On the basis there is no conventional wisdom predicting any significant fall in fossil fuel prices continuing for 15 years of the order required it can be reasoned that the accumulated state resources will not exceed investment costs under reasonable assumptions.

10. In conclusion my authorities submit that the payment of proportionate compensation to undertakings to maintain economic equilibrium to ensure the execution of a project of common European interest that the open market will not deliver is necessary if Ireland is to deliver an obligation addressed to it in Directive 2001/77/EC efficiently. My authorities further submit that activation of the "market price equalisation cost" is dependant on future gas/oil/electricity prices and the foregoing assumptions are reasonable and based on those assumptions the total state resources transferred will not exceed investment costs.

11. As stated in my previous letter my authorities are available to provide any additional clarifications.

Yours sincerely,



Una Dixon
Energy Attaché

