



BREXIT, ENERGY AND IRELAND

JUNE 2017

One year on from the UK's vote to leave the EU, FTI Consulting hosted a high-level panel discussion in Dublin on Thursday 22 June 2017 on the impact of Brexit on Ireland's energy markets and security. The panel comprised: Colin Spain, who established and leads Gaelectric's Energy Trading and Markets Services team and is responsible for the negotiation of commercial energy contracts and regulatory affairs; Timmy Dooley, TD, Fianna Fáil Vice President and Opposition Spokesperson on Communications, Environment and Natural Resources; Rodney Doyle, Executive Director of EirGrid and Market Operations & General Manager of SEMO, the Single Electricity Market Operator; Dr Pat McCloughan one of Ireland's leading consultant economists, active in a wide variety of work for central government departments, local authorities, national agencies, educational institutions and private sector organisations; Joseph Curtin, Senior Research Fellow with responsibility for climate change policy at IIEA, and project leader of the Climate-Smart Agriculture project. This Snapshot presents the main discussion points.

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The Brexit challenge

The uncertainty over Brexit represents the single biggest challenge of recent times to the economies of Ireland and Northern Ireland. The peace process is the people of the island of Ireland's greatest achievement in living memory. It has transformed relations on the island and promoted cross-border trade, economic development, cooperation and competition.

It is therefore encouraging to see due recognition of the special relationship between Ireland and the UK at the negotiating table and that the issue of the Irish border is one of the key fundamentals in negotiations from the EU's perspective. Education, tourism and energy are areas where the two parts of the island have cooperated for their mutual benefits, and the Single Electricity Market (SEM) combining Ireland and Northern Ireland has been one of the most important legacies of the peace process.

It has been a huge success, and has brought massive benefits to businesses and consumers on both sides of the Irish border, with a disproportionately positive impact particularly in Northern Ireland. It has also been and is of critical importance for the security of electricity supply and for the incorporation of renewable energy sources into the island's energy consumption, where both parts of the island are committed to achieving 40% of all electricity generated from renewable energy sources by 2020.

Single Electricity Market

The Single Electricity Market refers to the joint wholesale market which operates on the entirety of the island of Ireland, with the aims of meeting consumer demand for energy at the least-cost and maximizing reliability and security. The Single Electricity Market will, despite Brexit, still be binding as it has been signed into national legislation in both jurisdictions. The energy systems of Ireland and the UK are closely connected. This is not limited to the SEM, but includes gas as well as electricity. Ireland- UK bilateral arrangements are already in place to enable that cooperation.

The current SEM was not designed for the significant amounts of wind and solar now being generated in both jurisdictions of the island of Ireland. The wholesale market on the island is due to change considerably, also to take account of the requirements of the European Network Codes and the Target Model, including a change to four market timeframes.

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The new Integrated Single Electricity Market (I-SEM) is the next stage in the development of the SEM. I-SEM is intended to further liberalise and connect Ireland's electricity supply with that of Northern Ireland. Key elements of I-SEM include:

- active participation by supplier companies – submitting bids to purchase energy in the day-ahead and intraday markets;

- suppliers and generators paying / being paid based on prices and quantities determined through ex-ante (forward, day-ahead and intraday) trading, and
- cross-zonal power flows determined based on energy market trades and power flowing from the cheaper to the more expensive bidding zone.

Brexit puts that success and progress under threat. While there is broad consensus both north and south of the need for I-SEM to progress, with regulators in both jurisdictions fully supporting it, Northern Ireland will not be legally bound to comply with it once the UK leaves the EU.

Post-Brexit, Northern Ireland may no longer wish to continue with this development—particularly if EU funding is withdrawn. A hard Brexit which sees Northern Ireland outside of the Customs Union would threaten the current political will which underpins support for I-SEM. Furthermore, if the UK does not join even the European Economic Area, regulatory difficulties, increased transactional costs, and the possibility of tariffs on energy from the UK might make it impossible to operate the I-SEM.

Any settlement that would require a trading mechanism for the proposed north-south interconnector would represent a real barrier and challenge to the continuation of the Single Electricity Market. The north-south interconnector is critical to the ongoing success of the SEM and I-SEM: if one single part of the Single Electricity Market fails, all of the other elements could easily fall like dominoes.

It is an undeniable reality that Northern Ireland and Ireland compete with each other in certain economic activities and will continue to do so. Even if the Brexit vote had gone the other way, the competition for inward investment between both jurisdictions would be fierce, and it is only to be expected that Northern Ireland (and the other parts of the UK) will become formidable competitors in the coming years. Competition also appears to be creeping back into the all-island electricity market. For example in Northern Ireland, a number of large-scale solar PV projects and wind farms, such as the 46MW Bann Road Solar Farm, are coming on stream or planned, which will mean an appreciable potential diversification in renewable energy infrastructure. The proposed compressed air energy storage facility in Larne in Northern Ireland – the only part of the island where such a large-scale project can be accommodated, due to geological reasons – is another such example. Stakeholders south of the border are also alert to the link between renewable energy sources and

FDI, and there is a push now on in respect of alternatives like solar PV.

Energy security

Without appropriate action Brexit could have very negative impacts on Ireland's energy security and supply. Ireland depends on Britain for a consistent and cost-competitive supply of energy and electricity, and tariffs or increased transactional costs would jeopardize this. Ireland is also heavily reliant on the United Kingdom to ensure energy supply in the event of external shocks: the UK is currently obliged under EU law to extend certain support to Ireland in the event of a supply shock of any sort.

Ireland receives up to 40% of its gas supply from the UK, which is crucial to electricity generation. Natural gas is used to generate about 46% of electricity in Ireland, whose dependence on UK gas will likely increase once the Corrib gas field is depleted by about 2025. Furthermore, under the Oil Stocks Directive, part of Ireland's strategic oil reserve is held in the UK. In the absence of a solidarity agreement between the UK and Ireland, the UK could, in periods of energy shortage in the UK or globally, refuse to supply energy to Ireland, with devastating consequences.

Carbon pricing

Should the UK not join the EEA, it would also be free to set its own carbon pricing. If this price were set lower than the EU price, while this would mean cheaper prices for Irish consumers, it would represent a competitive disadvantage

for Irish producers. This could have negative ramifications on Ireland's ability to meet its renewable targets. If, however, UK carbon prices were higher than Irish carbon prices, the cost of energy would be higher for Irish consumers, although Irish producers would have a competitive advantage. Ireland could, in response, create a tax on Irish producers to bring its carbon floor up to UK levels. Because this would likely disincentivise Irish energy production, including renewables, this would likely have a negative impact on Ireland's overall energy security and ability to meet environmental targets.

A key topic for Brexit negotiations

Ireland's official opposition party Fianna Fáil believes it is therefore vital to ensure Ireland's energy interests are well represented in Brexit negotiations. That party wants Ireland to lobby hard for UK membership of the EEA or, failing that, for arrangements to be made for the UK to continue to operate a smooth and efficient interconnected energy market. Whether the peculiarities of the all-Ireland energy markets will be high on the agenda remains to be seen – but there is clear concern in Dublin on this key issue, as there is much at stake from an Ireland perspective, both north and south.

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