Neutral Citation Number: [2013] IEHC 568

THE HIGH COURT

JUDICIAL REVIEW

[2012 No. 760 J.R.]

BETWEEN

SHANNON LNG LIMITED AND SHANNON LNG ENERGY LIMITED

APPLICANTS

AND

COMMISSION FOR ENERGY REGULATION

FIRST NAMED RESPONDENT

AND

IRELAND,

SECOND NAMED RESPONDENT

AND

THE ATTORNEY GENERAL

THIRD NAMED RESPONDENT

AND

BORD GAIS ÉIREANN

NOTICE PARTY

JUDGMENT of Mr. Justice Cooke delivered the 11th day of December 2013

1. The present proceeding comes before the Court as a telescoped application for leave to apply for and for judicial review of a decision (the "Contested Decision") made by the first named respondent (the "CER"), on the 29th June, 2012, by which it is alleged that it unlawfully purports to set new methodologies for the calculation of tariffs relating to the use of and access to the transmission system and pipeline network for transport and delivery of natural gas in the State owned and operated by the Notice Party including two undersea inter-connectors to the transmission network in the United Kingdom. In particular, an order of certiorari is sought quashing the Contested Decision together with a variety of declaratory reliefs directed at establishing the invalidity of the basis and reasons for the CER's making of that decision.

Introduction.

2. All natural gas which is currently distributed within the State for supply to end users whether industrial, commercial or domestic, originates in sources of supply which are located off-shore. Those supplies are distributed over an on-shore transmission system or pipeline network which belongs to the Notice Party, Bord Gais Éireann, ("BGE") and which is operated by it through a wholly owned subsidiary called "Gaslink". Through this onshore transmission system gas is supplied to end users located in the major population centres of Dublin, Cork, Limerick and Galway and surrounding areas. It comprises a ring main between the major centres of Dublin, Cork, Limerick and Galway with exit points and distribution spurs to other population centres or large commercial consumers such as generating stations.

3. At the moment natural gas imported from outside the State arrives at the ring main at two points north of Dublin. A further small part of the total supply enters the transmission system from the Kinsale Head gas field at Inch in Co. Cork. At least 90% of the total supply is imported from the United Kingdom through the two undersea pipelines called "inter-connectors" owned by BGE which run from Moffat in Scotland and which come ashore to join the ring main at the two points situated at Loughshinny, Co. Dublin and Gormanston, Co. Meath.

4. The first of the interconnectors was built by BGE in 1993 and is laid from the natural gas custody transfer point at the British Gas Compressor Station near Beattock near Moffat in Scotland; onshore to the Scottish coast, then on the sea bed to the "Pig Trap" at the BGE Shore Station at Ballustree near Loughshinny where it connects to the BGE ring main. This inter-connector was constructed pursuant to an Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Ireland done on 30th April 1993 which recognised that it was to be constructed to satisfy the demand for natural gas in Ireland. It also contained provisions whereby the latter would take such measures as were available to it to ensure that the competent authorities in Northern Ireland and in the Isle of Man might opt to connect pipes to the interconnector to facilitate transport of natural gas to those areas and that the operator of the interconnector would facilitate access and connection to it for that purpose. These options were subsequently taken up. This interconnector accordingly has an under-sea exit point and connecting pipeline to the Isle of Man. Secondly, from the onshore station in Dublin a South-North pipeline transports natural gas to Northern Ireland where it is distributed by a subsidiary of BGE, "BGE-NI". At a point between its commencement at Moffat and the Scottish coast line there is also an exit connection to a pipeline which transports gas to Northern Ireland through another sub-sea pipeline which comes ashore north of Belfast. This Scotland-Northern Ireland Pipeline (S.N.I.P) is operated by a third party.

5. In 2001-2002 BGE laid a second pipeline and a further inter-Government Agreement was concluded for it on 24th September 2004. Although to date natural gas has been transported through the inter-connectors and on the South-North pipeline in one direction only namely from Scotland, since December 2011, "virtual reverse flow arrangements" have been in place at Moffat which will allow "virtual flow" of supply in the opposite direction, thereby permitting trading of gas from the Irish market to the UK market.

6. One of the central areas of dispute in this proceeding concerns the status of these two inter-connectors; how they may be treated for tariff setting purposes and whether the gas which is delivered through them may be correctly treated as entering the BGE transmission system at Moffat in Scotland (as the respondents assert,) or only at the two above arrival points (as the applicants contend). It is not claimed that the CER has no power under the relevant legislation to set tariffs for access to and use of the interconnectors; the dispute concerns the methodology proposed to be adopted for that purpose and the legality of treating the interconnectors as an integral part of the entire BGE transmission infrastructure rather than as a separate facility the costs of which must be distinctly accounted for and recovered from the undertakings which make actual use of them.

7. A new source of supply is planned to be provided in the near future at Bellanaboy, Co. Mayo, from the Corrib gas field off the west coast. A pipeline from that source has been laid to join with the Galway/Dublin section of the onshore transmission system. It is anticipated that this new source of supply will become operational in 2015.

8. The first named applicant ("Shannon LNG"), is a company established in 2003 for the purpose of developing a terminal on the southern bank of Shannon estuary near Tarbert, Co. Limerick, through which it proposes to import cargos of liquefied natural gas (LNG) which will be shipped to the State and supplied to the on-shore transmission system through a new 26 km long pipeline which it will construct for that purpose from the terminal to the BGE transmission system near Foynes in Limerick. Shannon LNG is a wholly owned subsidiary of a quoted US company, Hess Corporation, which has widespread international interests in gas and oil business with 13,800 employees in 23 countries. The second named applicant ("Shannon Energy"), is a sister company of the first named applicant and also a wholly owned subsidiary of Hess Corporation. The commercial plan of the applicants is that the Shannon Energy will enter into an agreement with the Shannon LNG to use all of the capacity of the latter's new terminal at Foynes and, as a "network user", will sell natural gas to wholesale buyers and large consumers such as power stations within the State.

9. It should be noted that insofar as the issues raised in this case are directed at the legality of the tariff regime proposed in the Contested Decision for access to the BGE transmission network, it is the second named applicant that is primarily concerned. As the first named applicant will contract to supply all of its imports to the sister company, it is the latter that will access the network and be required to pay the impugned tariffs.

10. It is the anticipated effect of the arrival of these two new sources of supply of natural gas on the market in the State from the Corrib and Shannon operations which has brought about the process of research, investigation and industry consultation on the part of the CER which has resulted in the Contested Decision and led to its conclusion that reform of the current regulatory regime for that market is necessary. That conclusion is disputed by the applicants who have participated in and contributed to the consultation process.

11. Liquid natural gas or "LNG" is natural gas when cooled to become liquid and, as such, can be transported and supplied by ship over long distances on terms which are competitive with natural gas in its vapour form supplied by pipeline. Supplies of LNG will be delivered by shippers to the new terminal where it will be "re-vapourised" that is, reconverted into natural gas, by Shannon Energy and then supplied onwards through its pipeline to an entry point on the BGE transmission system at Limerick. Its ultimate customers will then take their purchased supplies from the appropriate exit point on that system through the local distribution network. Once in operation therefore, Shannon Energy and its shipper/suppliers will be in competition for end customers with the undertakings delivering supplies over the interconnectors from the United Kingdom, and with those delivering from the Kinsale source and from the Corrib field source. The project has been in the course of planning, development and implementation since 2003 and has involved an investment on the part of the applicants to date of €49 million approximately. The full cost including the terminal and the pipeline is estimated to amount to €600 million.

12. Briefly stated, the applicants' complaint is that the CER has acted, and proposes to act, unlawfully by the alterations it intends to make in the manner in which the BGE transmission network and interconnectors are treated for regulatory purposes and the basis upon which the tariffs for access to and use of the infrastructures are calculated and fixed. In particular, the applicants assert that the Contested Decision is unlawful as incompatible with the requirements of the relevant legislative provisions and with general provisions of European Union law by:

> (1) eliminating the distinct treatment for tariff purposes of the interconnectors by regarding them as an integral part of BGE's transmission system or infrastructure:
>
> (2) charging of a tariff for access to the transmission system based upon a two part tariff comprised of a "Long Run Marginal Cost" (LRMC) element and a "revenue shortfall" element and not upon actual costs incurred by BGE;
>
> (3) granting an unnotified state aid to BGE contrary to Article 108 TFEU; and placing BGE in a situation in which it will abuse its dominant position by requiring the applicants to cross-subsidise its operating costs of a part of the infra-structure they do not use. On these grounds the measures decided to be adopted in the Contested Decision are claimed to be ultra vires the statutory competence of the CER and incompatible with the requirements and conditions of the relevant legislation.

The Legislative Context

13. The Commission for Energy Regulation is a public regulatory authority established under s. 8 of the Electricity Regulation Act 1999, and subsequently given its present name by s. 5 of the Gas (Interim) (Regulation) Act 2002. It has the statutory functions, powers and duties assigned to it by s. 9 of the Act of 1999 (as amended). These include an obligation to monitor the level and effectiveness of the opening up to competition and the development of markets for the supply of electricity and gas; powers to take action in order to prevent distortion or restriction of competition in the supply of gas to final consumers; and powers to monitor the implementation of rules relating to the roles and responsibilities of transmission system operators, distribution system operators, suppliers and customers and other market parties in the gas sector.

14. The CER acts as an advisory body to the Minister for Communications, Energy and Natural Resources in relation to the development of the electricity and gas networks in the country. The duties of the CER include the promotion of competition and safety in the electricity and natural gas undertakings in the State, of ensuring the continuity and quality of these services along with renewable, sustainable or alternative forms of energy, making sure that no unfair discrimination occurs between applicants for or holders of licenses consents and authorisations or between them and State-owned operators.

15. The issues in this case arise in the context of the legislative regime at European Union level which both enables and regulates the operation of an internal market within the Union in which natural gas can be traded across and through the local and national

transmission systems of all of the Member States. As the opening recitals to the principal measures mentioned below record, the achievement of such an internal market in pursuance of the Treaty objectives has been progressively implemented since 1999 with the aim of providing consumers with real choice in sources of supply and the achievement of gains and efficiency, in competitive pricing, higher standards of service and security of supply. As already mentioned, this Member State as an island has until now participated in that internal market principally by means of the BGE interconnectors to the transmission system of the United Kingdom as the nearest Member State.

16. For the purpose of the issues arising in this case the principal relevant provisions are those contained in a number of instruments known as the "Third Energy Package" being a series of legislative measures adopted by the European Parliament and the Council on 13th July 2009 with a view to completing the implementation of the single markets in both natural gas and electricity. Those now relevant to the gas sector are the "Third Gas Directive" namely, Directive 2009/73/EC of the European Parliament and the Council of 13th July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (OJ L211/94); and Regulation (EC) No 715/2009 of the European Parliament and the Council of 13th July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No.1775/2005 (OJ L211/36). (These measures will be referred to in this judgment as the "Directive" and the "Regulation" respectively.) (A further measure, Regulation (EC) No.713/2009 established the Agency for Cooperation between Regulators.)

17. The Regulation was adopted as an approximation of laws measure under Article 95 E.C. (now Article 114 TFEU) and, as its title indicates, contains the detailed conditions governing the terms upon which the Member States are to operate their transmission systems for natural gas including the terms upon which the transmission systems in one Member State may be connected to a system in another Member State and access be made available to users of the transmission system upon non-discriminatory and competitive terms. The conditions include provisions governing the setting of tariffs for access and use of the transmission systems and the basis upon which regulatory supervision for that purpose is to be exercised by the competent regulatory authorities of each Member State in relation to the recover of costs by the operators of the transmission systems.

18. The Directive, on the other hand, has its primary legislative basis in the right of establishment provisions of Article 47EC (Now Article 53 TFEU) and sets out the rules to be applied in common by the Member States in opening up their markets to inter-State trade in natural gas by removing obstacles to cross border transactions in the product and by unbundling supply and production functions from those of network operations. Accordingly, much as in other markets such as those of electricity or telecommunications which are dependent upon extensive and expensive network infrastructures, the provisions of the Directive are concerned with prescribing the conditions which will enable competition to take place for the ultimate benefit of domestic and commercial consumers between undertakings producing and supplying the product and between undertakings offering services in transport, storage and distribution.

19. In broad terms therefore the aim of the establishment of the internal market in natural gas is to bring about a single market for the supply, purchase and trade in natural gas across the territory of the Union by opening up and integrating the national markets; by enabling producers to supply gas across inter-state systems by having access to distribution networks on non-discriminatory and transparent terms; and by giving users or consumers the ability to avail of a diversity of suppliers in a competitive and secure market. The steps to be taken to achieve these objectives involved the establishment of an independent regulator by each Member State equipped with powers to promote the "unbundling" of vertically integrated undertakings, that is, the separation the activities of transmission system operation from those of production and supply. The regulators are to foster investment in infrastructure and particularly the construction of interconnectors between the different national or regional distribution networks or grids thereby ensuring that new entrant suppliers can access the different networks and that consumers and users can exercise a choice of supplier from across the entire market.

20. These aims are reflected in recitals 56-58 of the Directive:

> • "With a view to creating an internal market in natural gas, Member States should foster the integration of their national markets and the cooperation of system operators at Community and regional level, also incorporating the isolated systems forming gas islands that persist in the Community.
>
> • The development of a true internal market in natural gas, through a network connected across the Community, should be one of the main goals of this Directive and regulatory issues on cross border interconnections and regional markets should, therefore, be one of the main tasks of the regulatory authorities, in close cooperation with the Agency where relevant.
>
> • Securing common rules for a true internal market and a broad supply of gas should also be one of the main goals of this Directive. To that end, undistorted market prices would provide an incentive for cross-border interconnections while leading, in the long term, to price convergence."

21. The Regulation contains similar explanatory recitals including recital (7) which reads:

> "It is necessary to specify the criteria according to which tariffs for access to the network are determined, in order to ensure that they fully comply with the principle of non-discrimination and the needs of a well-functioning internal market and take fully into account the need for system integrity and reflect the actual costs incurred, insofar as such costs correspond to those of an efficient and structurally comparable network operator and are transparent, whilst including appropriate return on investments, and, where appropriate, taking account of the benchmarking of tariffs by the regulatory authorities.

The Directive.
22. The following relevant definitions are contained in the Directive :

> ***"natural gas undertaking"*** means a natural or legal person carrying out at least one of the following functions: production, transmission, distribution, supply, purchase or storage of natural gas, including LNG, which is responsible for the commercial, technical and/or maintenance tasks related to those functions, but shall not include final customers
>
> ***"transmission system operator"*** means a natural or legal person who carries out the function of transmission and is responsible for operating, ensuring the maintenance of, and, if necessary, developing the transmission system in a given area and, where applicable, its interconnections with other systems, and for ensuring the long-term ability of the system to meet reasonable demands for the transport of gas

"system" means any transmission networks, distribution networks, LNG facilities and/or storage facilities owned and/or operated by a natural gas undertaking, including linepack and its facilities supplying ancillary services and those of related undertakings necessary for providing access to transmission, distribution and LNG

"interconnector" means a transmission line which crosses or spans a border between Member States for the sole purpose of connecting the national transmission systems of those Member States

"interconnected system" means a number of systems which are linked with each other

"system user" means a natural or legal person supplying to, or being supplied by, the system.

23. Article 13 of the Directive sets out the responsibilities and duties of system operators including LNG system operators in respect of the transmission, storage and operation of facilities. They are to operate, maintain and develop facilities which are secure, reliable and efficient in order to secure an open market with due regard to the environment and ensuring adequate means to meet service obligations. They must not discriminate between system users and must provide other system operators with the sufficient information to ensure that the transport and storage of natural gas may take place in a manner which is compatible with the secure and efficient operation of the interconnected system. Rules for balancing the gas transmission system must objective, transparent and non-discriminatory.

24. Other relevant provisions in the Directive include:

• Article 32 (1) which deals with third party access to the system:

> "Member States shall ensure the implementation of a system of third party access to the transmission and distribution system, and LNG facilities based on published tariffs, applicable to all eligible customers, including supply undertakings, and applied objectively and without discrimination between system users. Member States shall ensure that those tariffs, or the methodologies underlying their calculation are approved prior to their entry into force in accordance with Article 41 by a regulatory authority referred to in Article 39(1) and that those tariffs — and the methodologies, where only methodologies are approved — are published prior to their entry into force."

• Article 35 which sets out the basis for refusal of entry to the system:

> "(1). Natural gas undertakings may refuse access to the system on the basis of lack of capacity or where the access to the system would prevent them from carrying out the public service obligations referred to in Article 3(2) which are assigned to them or on the basis of serious economic and financial difficulties with take-or-pay contracts having regard to the criteria and procedures set out in Article 48 and the alternative chosen by the Member State in accordance with paragraph 1 of that Article. Duly substantiated reasons shall be given for any such a refusal.
>
> "(2). Member States may take the measures necessary to ensure that the natural gas undertaking refusing access to the system on the basis of lack of capacity or a lack of connection makes the necessary enhancements as far as it is economic to do so or when a potential customer is willing to pay for them. In circumstances where Member States apply Article 4(4), Member States shall take such measures"

• Article 41-1 (a) which lays out the duties and powers of a regulatory authority to fix tariffs on the system:

> The regulatory authority shall have the following duties:
>
> (a) fixing or approving, in accordance with transparent criteria, transmission or distribution tariffs or their methodologies
>
> and 41-1(f) which places the duty on the system operator to ensure no cross subsidies exist:
>
> (f) ensuring that there are no cross-subsidies between transmission, distribution, storage, LNG and supply activities

• Article 41-4 (b) places an obligation on regulatory authorities to carry out investigations into the functioning of the natural market and empowers system operators to decide upon and impose any measures to ensure effective competition and to ensure the proper functioning of the market. The regulatory authority is also tasked to cooperate with the national competition authority, financial market regulators or the Commission in regards to investigations surrounding competition law.

> 41-4 (d) places a further duty on regulatory authorities to put into place proportionate and dissuasive penalties on natural gas undertakings which do not comply with their duties under the Directive or any legally binding decisions of that authority.
>
> Article 41-6 sets out the responsibilities of the regulatory authorities in setting out, approving and fixing the terms and conditions for the a range of services including the connection and access to national networks, the provision of economic and appropriate balancing services (including incentivising network users to balance their output) and access to cross-border infrastructures.
>
> Article 46-10 sets out the powers of regulatory authorities to modify the terms and conditions regarding tariffs and other methodologies:
>
> Regulatory authorities shall have the authority to require transmission, storage, LNG and distribution system operators, if necessary, to modify the terms and conditions, including tariffs and methodologies referred to in this Article, to ensure that they are proportionate and applied in a non-discriminatory manner. In the event that the access regime to storage is defined according to Article 33(3), that task shall exclude the modification of tariffs. In the event of delay in the fixing of transmission and distribution tariffs, regulatory authorities shall have the power to fix or approve provisional transmission and distribution tariffs or methodologies and to decide on the appropriate

compensatory measures if the final tariffs or methodologies deviate from those provisional tariffs or methodologies.

The Regulation.
25. The Regulation sets out conditions for access to the natural gas transmission networks in the EU Member States. Its general objectives are to set "non-discriminatory rules" for access to natural gas transmission networks, liquid natural gas facilities and also to facilitate the emergence of a functioning and transparent wholesale market for natural gas harmonised between the member states. Its main focus is the harmonisation of tariffing principles.

26. Article 2-2 of the Regulation stipulates that the definitions contained in the 2009 Directive which are relevant for the application of the Regulation also apply. The exception to this is the definition of "transmission" which reads as follows:

> **"transmission"** means the transport of natural gas through a network , which mainly contains high-pressures pipelines, other than an upstream pipeline network and other that the part of high-pressure pipelines primarily used in the context of local distribution of natural gas, with a view to its delivery to customers, but not including supply"

27. Another relevant definition is that of "network user":

"'Network user' means a customer or a potential customer of a transmission system operator, and transmission system operators themselves in so far as it is necessary for them to carry out their functions in relation to transmission."

28. Article 13 of the Regulation sets out the basis for tariffing access to the networks. The main thrust of Article 13 is to ensure that any tariffs calculated and approved by the regulatory authorities take into account the actual costs incurred, and are non-discriminatory to network users. Furthermore tariffs are to be set "separately for every entry point into or exit point out of the transmission system". Tariffs calculated on the basis of contract paths were to be prohibited following a transitional period after the 3rd September 2009.

29. Article 27(1) of the Regulation sets out the penalties that will apply in cases of infringements of the Regulation. The penalties provided for must be effective, proportionate and dissuasive.

Gas Act 1976 (as amended) S.10A
30. The provisions of the Regulation are, of course, of direct effect and thus binding upon the State without need of transposition. The implementation at national level of the earlier Directives in the previous "Energy Packages" replaced by up this 2009 Directive has, however, been somewhat complex having required legislation such as the Gas (Interim Regulation) 2002 and a series of statutory instruments which culminate, in effect, in the European Communities (Internal Market in Natural Gas) Regulations 2005 and SI 630/2011. For the purpose of the issues considered later in this judgment, however, the provisions immediately relevant to the exercise of the CER competence in making the Contested Decision are those found in s. 10A of the Gas Act 1976 (as amended).

31. The provisions of that section which are immediately relevant can be cited or paraphrased as follows. In subs. (1) the following definitions are set out:

> **"Facility"** means a transmission or distribution line, an LNG facility or an actual gas storage facility;
>
> **"Pipeline Operator"** means the holder of a natural gas licence in respect of the operation of a distribution or transmission pipeline'
>
> **"Third party Access"** means – (a) in the case of a downstream natural gas pipeline, the transportation of natural gas through a pipeline operator's pipeline, and (b) in the case of an LNG facility access to and use of an LNG facility under the control of the operator . . ."

32. Subsection (2) gives effect to the basic obligation of facility operators to grant access to their facilities. It provides that where an operator receives an application from an eligible customer in respect of access to a downstream facility, the operator must offer to enter into an agreement for that access subject to terms and conditions which may be specified in directions issued by the CER under subsection (5).

33. Subsection (3) enables an operator to respond with an offer which may include an offer to grant access at a rate or for a volume different from that requested with part of the CER to examine the reasons why such a counter offer has been made.

34. Subsection (4) empowers the Commission by direction to specify the matters to be included in an agreement for third party access including terms and conditions relating to price.

35. Under subs. (8) where an operator refuses to offer to enter into an agreement under the section, the reasons for the refusal must be given by notice to the applicant. The CER is then the competent authority to settle disputes in relation to such offer and refusal.

36. Finally, subs. (17) of 10A is at the centre of the applicants' arguments. The material parts read as follows:-

> "(a) Subject to para. (b) and subs. (19) an operator shall, within such time as the Commission may direct, prepare a statement for the approval of the Commission setting out the basis upon which charges are to be imposed –
>
> > (i) for third party access to a facility of an operator, and
> >
> > (ii) for connection to a facility operated by that operator.
>
> (b) The Commission may –
>
> > (i) give directions to an operator from time to time in respect of the basis for charges for third party access to, or connection to, a facility under the control of the operator, and
> >
> > (ii) issue a direction specifying those classes of operators to whom para. (a) does not apply.

(c) Notwithstanding the generality of para. (b), directions given by the Commission under the subsection may provide for -

(i) the methods of charging to be included in the statement to be prepared by an operator,

(ii) the form and extent of the information to be provided by an operator to applicants.

(iii) the form of charges and information about those charges to be included in the statement to be prepared by the operator,

(iv) the procedure to be adopted in the submission by an operator of a statement of charges and the approval by the Commission of such statement and

(v) the nature of the information to be provided to applicants seeking third part access to, or connection to a facility under the control of the operator and its presentation and transparency."

An operator is required to comply with such directions from the CER.

37. Subsection (e) provides

"a charge for third party access to, or connection to a facility under the control of the operator shall be calculated in accordance with directions given by the Commission under this section so as to enable the operator to recover –

(i) the appropriate proportion of the costs directly or indirectly incurred in carrying out any necessary works, and

(ii) a reasonable rate of return on capital represented by such costs.

(f) the Commission, solely, shall determine that which constitutes an "appropriate proportion" referred to in para. (e)(i) and a "reasonable rate of return" referred to in paragraph (e)(ii).

The Contested Decision
38. As already indicated, the Contested Decision was prompted by the need for a re-examination of the existing tariffs and of the regulatory treatment of the interconnectors in the light of the arrival of the two new sources of natural gas supply mentioned above. At present the gas flow through the interconnectors accounts for over 90% of gas supplied to the State with the result that, at least in recent years, the fixed costs of the interconnectors amounting to approximately €50 million per annum have been borne by bulk of the customers taking those supplies by payment of a single entry tariff combined with the common exit point tariff. (Prior to 2005 a "point to point" capacity system had been used based upon shippers entering into "Standard Transportation Agreements" under which gas was transmitted over a chosen "contract path" from a nominated entry point to a nominated exit point. One of the policy objectives of the 2009 Package has been to eliminate contract path systems and install an "entry/exit" capacity regime so that charges are based exclusively on the supply placed onto the system and exiting it and not on the distance between a the points used or on the use of a particular part of the infrastructure.) Because the supplies to the interconnectors constituted such a dominant part of the supply in the State, the Irish wholesale price for the product was largely determined by the price, referred to as the "national balancing point price" in the United Kingdom plus the cost of transporting the gas to Ireland. For this reason the Irish market is referred to as being essentially a "price taker" and would so remain as long as the interconnectors remain the marginal source of gas supply.

39. On the assumption that the two new sources of supply would lead to a reduction in the volume of gas flowing through the interconnectors, the CER considered it obvious that the single entry tariff charged to the shippers using the interconnectors would have to rise in order to cover the costs of the system. The annual revenue attributed to the interconnectors has been approximately €15 million which is recovered through a tariff based in part upon a capacity charge element as to 90% and 10% recovered through a commodity charge. The former is the charge for reserving space to flow gas on the interconnector and the latter is the charge for gas molecules actually transported through the pipeline. A user of the interconnector will book capacity periodically and pay for it whether it is actually taken up or not. The commodity charge, on the other hand, relates to the actual use made by volume.

40. The existing tariff regime predates the establishment of the CER and derives from a policy directive given by the Minister for Public Enterprise in 2001 at the time of the construction of the second interconnector and became known as the "Irish entry/postalised exit" tariff. (The term "postalised" derives from the concept of the postage stamp and connotes the delivery of a public service at a single uniform charge irrespective of the distance over which delivery takes place.) Under that regime BGE charges a separate entry tariff for the two existing points of entry – Moffat and Inch - and a further single tariff for all exit points on the transmission system. The Moffat entry tariff is based upon remunerating the aggregate values of the two interconnectors such that the actual costs incurred by BGE both in current maintenance and operation of the interconnectors and the historic costs of investment and depreciation are and have been identifiable in accountancy terms and quantified accordingly. According to the applicants, the actual cost thus attributable to the interconnectors has accounted for approximately one third of BGE's recoverable costs in respect of its transmission infrastructure. Thus the central problem which the CER sought to address was the question as to how and by whom the continuing costs incurred by BGE in the operation and maintenance of unused capacity on the interconnectors (referred to as "stranded costs") would be met following the reduction in flow volumes and hence in revenue after the arrival of the new supplies from the applicants and the Corrib project.

41. The particular operative rulings which are the subject matter of the applicants' challenge to the Contested Decision are contained in an instrument entitled "Decision Paper" dated the 29th June, 2012 and bearing the reference CER/12/087. The decision has, accordingly, a narrative form and is made up of 27 pages in its main part supplemented by a series of annexes making the document as a whole some 62 pages in length. It is to be read in conjunction with a number of earlier documents issued by the CER including: Proposed Decision - The Regulatory Treatment of the BGE Interconnectors (CER/12/013); Consultation (2) – The Regulatory Treatment of the BGE Interconnectors (CER/11/112); and Consultation – The Regulatory Treatment of the BGE Interconnectors in Relation to Security and Supply (CER/11/002). Those documents form the basis of, or arose out of, a consultation process between the CER and interested parties which effectively commenced in January 2011, with the issue of the third of the above papers.

42. The manner in which the CER reached its conclusions on the basis of the consultation process and the responses received to the earlier proposal is usefully summarised in an opening section of the Decision headed "Executive Summary". For present purposes its

material elements can be paraphrased as follows:-

- The existing transmission entry tariff regime needs reform because, without reform and assuming the investments in the interconnectors are not to be "stranded", the availability of new sources of gas will increase the unit entry tariff and possibly significantly, and this will increase the wholesale price for gas in Ireland. This would be inefficient and damaging to both consumer interests and the country's energy competitiveness.

- The CER is committed to a tariff policy which recognises and rewards new entry when shown to be efficient by reference to other entry in particular to entry from the UK through the interconnectors which, it assumes, will continue to be the marginal source of gas supply for the foreseeable future.

- The CER will base its tariff policy on "forward-looking Long Run Marginal Cost (LRMC) considerations" rather than on historic costs considerations – for example a prescribed portion of the historic costs of the interconnectors which would be deemed to constitute an efficient pricing rule to new investors.

- This preference for the forward-looking LRMC approach is grounded on sound economic principles; the specific circumstances of the Irish gas system; avoiding arbitrary regulatory judgment calls which would arise with the historic based approach; and on compatibility with the applicable EU rules.

- It is recognised that there are risks and challenges in moving to the LRMC based tariff so that it would be important to ensure full transparency and "stakeholder involvement" in establishing that methodology. This is to be done by establishing a Networks Tariff Liaison Group.

- The LRMC based tariff regime will require a mechanism to deal with possible revenue shortfall and the CER proposes that the chosen mechanism will be designed so as not to mitigate or take from the premium or differential available to developers of efficient new sources of gas entry.

- The European Commission's DG energy has advised that the treatment of the interconnectors as an integral part of the transmission system and the basing of tariffs on the LRMC at each entry point are, in principle, compatible with EU rules.

- The new tariff regime will come into effect in October 2014 and the work of the networks tariff liaison group in developing the precise methodology for obtaining LRMC based tariffs at each entry point is to be commenced shortly.

43. In conducting its researches and consultations the CER identified five options which are set out in s. 2 "Overview" of the Contested Decision at paragraph 17. These were:

Option 1: "Do Nothing": that is, continue the current tariff structure and allow the interconnector tariff at Moffat to rise. It was considered that competition between different sources of supply would not be sufficient to counter upward pressure on wholesale gas prices at least so long as Ireland remained a "price taker" such that shippers through the new sources of supply would have incentive to "price up" to the Moffat price to the detriment of consumers. This option would result in higher gas prices in Ireland.

Option 2: "Strand all or Part of the ICs": This would involve "stranding" or leaving out of consideration all or part of the investment costs attributable to the interconnectors by ceasing to ask the transmission customers to underwrite them.

Option 3: "Keep the Premium but Cap": This would involve retaining the interconnector tariff but capping it at a level deemed more efficient than at present and transferring any shortfall in revenue resulting from it to be borne by the "onshore network". In other words, any shortfall in the interconnector tariff below what was necessary to recover the full costs concerned would recouped by BGE from entry tariffs elsewhere in the transmission system.

Option 4: "Remove Premium": This envisaged removing entry tariffs completely and allowing BGE to recover all costs from a fully postalised regime regardless of the geographic source of the gas.

Option 5: "Move to LRMC Entry Tarriff Regime". This formed the basis of the solution ultimately preferred by the CER and is a variation of Option 3, under which a "cap" would be put upon the "premium" available to the shippers at the two new entry points by reducing the differential they would otherwise enjoy as compared with the entry charge at Moffatt. This would involve altering the basis of the Moffat entry charge from the current actual cost recovery for the interconnectors to a charge comprising two elements. The first element is the "long run marginal cost" (LRMC) of transporting gas from the entry point to the transmission system. This would be modelled on forward-looking rather than historic considerations and any shortfall in the revenue thus recovered would be made up by a second element or "revenue shortfall". One of the crucial features of this option, accordingly, is the abolition of the distinct or separate treatment of the interconnectors and the aggregation of all BGE's recoverable costs by reference to all of its infrastructure assets known as the "regulated asset base" (RAB). This option's effects are described in the Overview as follows:

> "The 'Irish system' in this context would include all transmission assets on the regulated asset base which would no longer differentiate between onshore and offshore assets. LMRC tariffs would probably still leave a shortfall on required revenues. To deal with this, it would be assumed that total required transmission revenues would be allocated 50:50 between entry and exit. The likely shortfall from LRMC tariff revenue from this 50% entry share would be recovered from all entry points. While the precise details of financing the revenue shortfall were not spelt out, the basic intention was that these should not affect the basis differential payable tot eh developer at an efficient new entry point."

44. The Contested Decision then describes how these options were set out in a "Proposed Decision Paper" issued in February 2012 (CER/12/013) and reviews the submissions received in the consultation process. Responses were received from 19 organisations or individuals (including Shannon LNG) and were considered and evaluated. (The responses are set out in further detail in appendix l of the Decision). It acknowledges that some respondents made it very clear that they would only give a final view on the LRMC methodology when they were given more detail of elements such as 50:50 split, common charging etc. It also acknowledged complaints made about lack of prior consultation on LRMC and the absence of a timescale. This review of the results of the consultation process led to the effective elimination of options 1, 2, and 4. The CER said:

"No substantive or convincing case has been put to the CER … as to why the CER should reconsider its position on these options. Neither has the CER itself, on reflection, reason to reconsider its earlier thinking on these options. Options 3 and 5 are then considered and explained in greater detail."

45. Between paragraphs 30 and 68 of the Contested Decision, the CER sets out the analysis which forms the basis of its choice as between options 3 and 5 and in doing so replies to some of the objections or observations that had been raised in the responses received during the consultation process. It emphasises that the policy of the CER is to retain a basic differential or premium in order of provide incentives to new entry provided that any new entry is efficient. At para. 29 it cautions: "Thus it could be the case that a low or zero differential might be appropriate in the event that a further new entry might be considered unnecessary or inefficient".

46. In paragraphs 30 – 53 the Contested Decision discusses and analyses the choice between providing that incentive as calculated on a historic basis (Option 3) or on a forward looking basis (Option 5). In the Proposed Decision Paper of the 17th February, 2012, the CER had already indicated its preference for the forward looking LRMC approach. That approach was considered to be well grounded in economic theory, the idea being to set tariffs to reflect the costs of providing an incremental unit of output at the different entry points on the system. Users will continue to purchase output at an entry point so long as this is more valuable to them than the cost of investing in incremental output at that point. Thus, where an entry point on the Irish system has a lower LRMC than the marginal entry point at Moffat, an LRMC based tariff based regime will either encourage shippers to source their gas at that entry point and/or reward producers to develop that entry point by allowing them price their gas up to, or very near to the higher LRMC tariff prevailing at Moffat. In this way efficient new sources of gas entry would be encouraged. By the same token, the higher LRMC cost of investing in incremental output at Moffat is avoided or delayed to the benefit of gas customers. (See para. 33).

47. The Contested Decision acknowledges the difficulties and complexities involved in moving to an LRMC based regime and accepts that there would be a need to ensure transparency and acceptance by industry of the methodology chosen for calculation of the tariffs. The CER viewed as critical the fundamental advantage provided by the LRMC approach that it would apply sound economic principles to the specific circumstances of the Irish gas system. No Irish users have long term contracts on the interconnectors so that there would not appear to be much prospect or commercial rationale for shippers to enter into long term contracts now or in the future at the Moffat entry point. (See para. 48). This absence of long term contracts at Moffat means that all shippers are contractually free to switch their supply source from Moffat to any other entry point when it is commercially attractive to do so. Accordingly, Moffat was deemed likely to continue to represent the "price to beat" for developers at other entry points as it had done in the past for the Inch entry point. This was considered to be the key distinguishing feature of the Irish gas transmission system. The CER therefore concluded that given the specific features of the Irish gas system and the continuous presence of the "price to beat signal" at Moffat, the use of LRMC to set entry tariffs would lead to more efficient outcomes for the industry as additional supply is only likely to come on to the system if it is efficient. (See para. 53).

48. In paragraphs 54 – 65 the Contested Decision then deals with the question of how an LRMC tariff revenue shortfall would be met. The manner in which the system would operate is described in para. 55. Because the LRMC tariffs are looking at future costs considerations there is the possibility that revenue produced would be insufficient to meet those required to finance the historic assets already in place. A supplemental revenue stream would therefore be necessary to make up any shortfall.

49. The preferred option (see para. 55) was to establish a single capacity charge common to all entry points which would be levied in addition to the location's specific entry charges. As explained elsewhere, in practical terms entry tariffs would be determined by auctions of capacity at each entry point with a reserve price being set. The overall entry/exit charging system would be similar to that used in the UK with the total revenue requirement for the transmission system operator (BGE) being divided equally between entry and exit – a 50/50 split. Where auctions of entry capacity fail to recover the full 50% of the revenue requirement this would be made up by the additional charge at all entry points. This exposé of its thinking makes it clear however, that the CER had come to no final decision on the details in question and it remained "open to arguments on different splits and these will be teased out in the planned Networks Tariff Liaison Group". (Para. 57).

50. In paras. 58 - 65 the CER then sets out by way of a tentative illustration, a series of indicative tariff differentials designed to illustrate the order of magnitude of a basis differential that might arise for developers under an LRMC based tariff regime. It is acknowledged that these were calculated for the CER by the BGE based upon a high level of assumptions and without including the common charge element of the expected final tariff. The LRMC methodology will ultimately need to be determined in consultation with stakeholders and approved by the CER, and the resulting LRMC as calculated under the agreed methodology may produce different results. (Para. 63).

51. The Contested Decision ends with a section headed "Conclusion and Next Steps" as follows:

> "[86] The CER concludes that the current gas transmission entry tariff regime will be reformed on the following lines;
>
> > (i) The current distinction between offshore and onshore assets for tariff setting purposes will cease. The IC's will be treated as an integral part of the transmission system no different to other assets.
> >
> > (ii) The entry points to the system will be located where assets transporting gas from outside the system actually join up with the assets comprising the integrated system or regulated asset base (RAB). So, the entry point for gas from GB will be at Moffat.
> >
> > (iii) Tariffs at each entry point will be set separately on an LRMC basis.
> >
> > (iv) A premium, or differential, in entry tariff levels will be retained to reward efficient new entry and will not be mitigated by the mechanism to be introduced to compensate for a revenue shortfall from LRMC entry tariffs.
> >
> > (v) The investments in the IC's will not be stranded.
>
> [87] The CER intends issuing a direction to the TSO (Gaslink) to effect these reforms pursuant to s. 14 of the Gas (Interim) (Regulation) Act 2002, with effect from the 1st October, 2014. Before doing so, however, the CER will be establishing and chairing a Network Tariffs Liaison Group to deliberate on the methodology for deriving the definitive LRMC tariffs for each entry point to the system. The group's deliberations will form an important input to the approval of the final methodology for calculating entry tariffs which will be a matter for the CER. The CER will shortly be writing to stakeholders inviting them to participate in the liaison group."

52. It will be noted that although the "decision" sets out five main elements in the reform to be undertaken in the gas transmission entry tariff regime, the full detail of the new regime to be introduced on the 1st October, 2014, has not be finalised and is expressly to be the subject of further deliberations in the proposed liaison group particularly in relation to the formulation of the basis for the definitive LRMC tariffs for each entry point. Both the CER and BGE have raised expressly an objection that the present proceeding is premature for that reason. A preliminary issue therefore arises and is dealt with later in this judgment as to whether (a) there has been any sufficiently definitive exercise of a statutory decision-making power on the part of the CER to render the measure in question liable to judicial review; (b) whether, having regard to the arguments raised in relation to the use of an LRMC methodology, the application is premature; and (c) whether, having regard to the outstanding deliberations required in order to fix the actual tariffs for each entry point, any obligation on the part of the State to notify the new regime as an alleged State aid under Article 108.3 TFEU has arisen.

The Applicants' Grounds of Challenge.

53. The applicants' grounds for the reliefs claimed as set out in s. (e) of the statement of grounds extend over some 32 pages and take up 93 paragraphs, together with (in the case of para. 51) some additional 20 sub paragraphs. It is perhaps no slight upon the creative talents and desire for comprehensiveness on the part of the draftsman to suggest that the core of the claim can be reduced to a lesser number of principal assertions of illegality and that these can be taken as acceptably summarised in the written legal submissions on behalf of the applicants (see para. 19) as follows:

> (a) As a result of the Contested Decision, the applicants will be compelled to pay for infrastructure which they will not use and they will be therefore forced to cross-subsidise BGE and other network users using the interconnectors;
>
> (b) There is no legal basis for compelling the applicants to pay for infrastructure they do not use;
>
> (c) The relevant legislation prohibits the imposition on the applicants of any requirement to cross-subsidise other network users who continue to use the interconnectors;
>
> (d) Tariffs imposed must be based on actual costs incurred;
>
> (e) The Contested Decision grants an unnotified State aid which cannot be put into effect until the European Commission has decided on its compatibility;
>
> (f) BGE will be compelled by the Contested Decision to abuse a dominant position by combining the costs of the interconnectors with those of the onshore transmission system, thus compelling the applicants to pay for interconnector infrastructure which they do not use and thus permitting BGE to secure for itself a competitive advantage on the secondary market for the delivery of gas onshore to Ireland in which the notice party will be in competition with the applicants.

54. Essentially, therefore, the applicants' case is based broadly upon two limbs. First, the abolition of the infrastructure distinction between the onshore assets and the interconnectors so as to treat BGE's assets in their entirety as an integral infrastructure for tariff purposes is argued to be incompatible with the relevant legislation and thus ultra vires the powers of the CER. In particular, the proposed new treatment of the interconnectors and transmission system infringes the mandatory conditions of Article 13 of the Regulation. Secondly, the Contested Decision is alleged to infringe EU law because (a) it will effectively require that the applicants cross-subsidise BGE's operation of the interconnectors and competitors using the interconnectors, and thus amount to unlawful State aid contrary to Article 108 TFEU; and (b) it will necessarily require or enable BGE to abuse its dominant position as sole operator of the transmission system thereby distorting competition between it and (*inter alia*) the applicants on the market for delivery of gas to the Irish market.

55. It is appropriate to consider first the grounds based upon the alleged infringement of the provisions of the Directive and the Regulation. Before doing so, however, it is necessary to outline the approach the Court considers it should adopt as to the criteria of illegality and the standard of review that falls to be applied for these purposes. It is also necessary to address the issue already mentioned in paragraph 52 above as to whether the Contested Decision is amenable to judicial review given the explicitly incomplete character of the decision in paragraphs 86 and 87 of its Conclusion and the respondents' claim that the present challenge is therefore premature.

The Scope and Standard of Review

56. The present proceeding is brought by way of judicial review of the Contested Decision and is not therefore the exercise of a particular right of statutory appeal such as is contained for, example, in s. 111(2) of the Postal and Telecommunications Services Act 1983 (as amended by Regulation 4 of the European Communities (Mobile and Personal Communications) Regulations 1996 in respect of licensing decisions of the (then) Director of Telecommunications Regulation; or in s. 24 of the Competition Act 2002 in the case of decisions on mergers by the Competition Authority. The proceeding is brought by way of judicial review because, pursuant to s. 32 of the Electricity Regulation Act 1999, as substituted by s. 15 of the Gas (Amendment) Act 2000, a decision of the present kind on the part of the CER may only be challenged by way of application for judicial review under O. 84 of the Rules of the Superior Courts and then subject to the particular conditions as to notification and time limits contained in that provision. It is to be noted, however, that in Article 41 of the Directive which sets out the duties and powers of the regulatory authorities charged with responsibility for supervising the operation of the internal market of the gas sector in the Member States, particular provision is made for judicial review of the decisions taken by regulatory authorities. Paragraphs 15 – 17 of Article 41 provide:-

> "15. Complaints referred to in paragraphs 11 and 12 shall be without prejudice to the exercise of rights of appeal under Community or national law.
>
> 17. Decisions taken by regulatory authorities should be fully reasoned and justified to allow for judicial review. The decisions shall be available to the public while preserving the confidentiality of commercially sensitive information.
>
> 18. Member States shall ensure that suitable mechanisms exist at national level under which a party affected by a decision of the regulatory authority has a right of appeal to a body independent of the parties involved and of any government."

57. Accordingly, while the present proceeding is by way of judicial review, it is an important consideration that what is sought to be challenged is a particular type of decision on the part of a regulatory authority responsible for administering and supervising the conditions under which a commercial activity licensed in the public interest is carried on. The CER is, accordingly, a public authority responsible under its governing statutes and in accordance with the objectives required to be achieved under the EU internal market

legislation, which is required to set policy for the sector in question and, as the very subject matter of the present proceeding illustrates, to carry out the necessary research, analysis and consultation in order to make the complex economic, technical, financial and policy choices which are necessary to give effect to the efficient operation of the fully open but regulated gas market.

58. In the judgment of the Court, it is appropriate when judicial review is sought of an administrative decision of the kind embodied in the Contested Decision, to ensure that the appropriate approach and standard of review is adopted by reference the nature of the grounds advanced. As already indicated above, the applicants' challenge to these aspects of the Contested Decision is essentially two-fold. It is argued on the one hand that the CER has erred in law by deciding to abolish the distinction between the onshore assets and the interconnectors thereby infringing the particular provisions of the Directive and the Regulation and acting *ultra vires.* On the other hand, it is also submitted as outlined above, that insofar as the Decision adopts or proposes to adopt a new tariff setting regime based upon the choice of a particular cost recovery methodology (LRMC) it is failing to comply with essential requirements of that legislation because, of necessity, the tariffs and methodology chosen for the calculation of tariffs will not "reflect actual costs incurred"; will involve cross- subsidies between network users; and will fail to be non-discriminatory when set separately for every entry and exit point on the transmission system contrary to the requirements of the Regulation. Clearly, the latter grounds are of a different character because they directed at the choice of methodology and at the technical economic, financial and accounting assessments which underlie the CER's preference for the LRMC approach and not merely based upon an alleged error of law in construing the provisions in question.

59. There have, of course, now been many decisions by courts both at national and European level, including the Irish Courts, in which detailed consideration has been given to the approach that should be adopted in judicially reviewing decisions made by expert regulatory bodies such as the CER. In the view of the Court, the procedural distinction between judicial review under O. 84 and a statutory appeal is unlikely to have a major practical bearing upon the approach the Court should take where the decision under review is one made by a national regulatory authority established, as in the present instance, pursuant to an EU law obligation for the purpose of supervising the operation of a sector of the Union-wide internal market. The essential obligation of the national court is to provide the parties with an effective remedy and the outcome ought not to be dependent upon the nuances of distinctions in national procedural laws.

60. That proposition is of course subject to the proviso that legislation providing for statutory appeal procedures will frequently lay down specific conditions adapted to the nature or the exigencies of the administrative or regulatory regime in which the appealed decision has been made and thus expressly narrow or expand the scope or depth of the review to be undertaken. This can be illustrated for example by the appeal prescribed under Regulation 4 of the European Communities (Electronic Communications Networks and Services) (Framework) Regulations 2011, (S.I. No. 333 of 2011) against decisions of the Commission for Communications Regulation. That regulation implements Regulation 4 of Directive 2002/21/EC of the European Parliament and the Council of 7 March 2007 (the Framework Directive) which requires the Member States to provide a right of appeal to an appeal body (which may be a court) which "shall have the appropriate expertise to enable it to carry out its functions effectively" and "shall ensure that the merits of the case are duly taken into account". (Such an appeal has been the subject of a judgment of this Court of 14th August 2013 in *Vodafone Ireland Ltd v. Commission for Communications Regulation.* [2013] IEHC 382). Clearly, the scope of such an appeal is significantly wider than that of the present judicial review of the legality of the Contested Decision.

61. Keane C.J. in considering this issue in the context of an appeal under s. 111 of the above Act of 1983 observed:

> "…it is also clear that the High Court in hearing the appeal must bear in mind that the Oireachtas has entrusted to the first defendant a decision of a nature which requires the deployment of knowledge and expertise available to her, her staff and consultants retained by her, but not available to the Court".

(See *Orange Ltd v. Director of Telecoms (No.2)* [2000] 4 I.R. 159 at 184). That passage introduced an often cited passage from a judgment of the Canadian Supreme Court in *Canada (Director of Investigation and Research) v. Southam Inc.* [1997] 1 S.C.R. 748:

> "An appeal from a decision of an expert tribunal is not exactly like appeal from a decision of a trial court. Presumably if Parliament entrusts a certain matter to a tribunal and not (initially at least) to the courts, it is because the tribunal enjoys some advantage the judges do not. For that reason alone, review of the decision of a tribunal should often be on a standard more deferential than correctness. . . . I conclude that the . . . standard should be whether the decision of the Tribunal is unreasonable. This is to be distinguished from the most deferential standard of review, which requires courts to consider whether a tribunal's decision is patently unreasonable. An unreasonable decision is one that, in the main, is not supported by any reasons that can stand up to a somewhat probing examination. Accordingly, a court reviewing a conclusion on the reasonableness standard must look to see whether any reasons support it. . . ."

62. It is also important, in the view of the Court, to bear in mind that where a regulatory authority is required to take decisions involving policy choices and considerations such as the formulation of commercial strategies and the assessment of future trends in demand, supply or prices, the decision will not necessarily be "wrong" to the extent of being unlawful simply because another approach can be shown to be possible or even preferable. There may be more than one perfectly acceptable solution and it is the expert regulatory authority and not the court to which the judgment as to the appropriate choice is delegated. The point was made by the Competition Appeal Tribunal for England and Wales in its judgment on a series of appeals against determinations made by the regulator for the telecommunications sector in that jurisdiction (OFCOM) under the European Common Regulatory Framework for the mobile phone market, (at para. 82 of the judgment) in the following terms:-

> ". . . There may, in relation to any particular dispute, be a number of different approaches which OFCOM could reasonably adopt in arriving at its determination. There may well be no single "right answer" to the dispute. To that extent, the Tribunal may, while still conducting a merits review of the decision, be slow to overturn a decision which is arrived at by an appropriate methodology even if the dissatisfied party can suggest other ways of approaching the case which would also have been reasonable and which might have resulted in a resolution more favourable to its cause."

63. That passage is obviously apt in the present case given that, as indicated in paragraph 43 above the CER has in the course of its analysis of the changing market conditions resulting from the arrival of the new sources of supply, identified, considered and consulted upon, several alternative approaches or solutions. So long as its chosen solution is within its powers to adopt and in its terms and effects compatible with the conditions and criteria prescribed by the relevant legislation; and provided it is proportionate to the problem to be solved and reasonable in striking the balance between competing interests and objectives, the Court cannot by way of judicial review substitute another solution.

64. It is, accordingly, in the light of that case law, that the Court approaches the applicants' arguments as to the unlawfulness of the Contested Decision as *ultra vires* the powers of the CER and an infringement of particular provisions in the governing legislation and of

EU law.

65. One further preliminary observation should be added. The issues raised in this case fall to be assessed on the basis that the power of the CER sought to be challenged is one of a national regulator within the framework of a Union-wide regime for the implementation of the internal market in natural gas and part of the wider programme for the achievement of the internal market in energy including electricity. To the extent that disputed issues of interpretation of this legislation are involved, and the solution is not be found in the ordinary meaning of the words used by the legislators, the function of the Court is to seek to resolve the dispute in a way which is compatible with the legislation and best serves the achievement of its objectives. In that regard the overriding objective which the national regulators in this sector are charged with ensuring is the creation and maintenance of an efficient, integrated and competitive market across the European Union for the benefit of the various categories of consumers of natural gas whether domestic, commercial or industrial.

66. It must also be borne in mind that when looking at specific articles of a Regulation or a Directive it is important not to approach them on precisely the same basis as one might approach a section in an Act of the Oireachtas or a statutory instrument which is applicable only to the conditions subsisting in this Member State or in its markets, or to its social and economic conditions. It is important to avoid the inclination to construe such provisions as if they are enacted solely to reform or address the existing market conditions or regulatory regimes as we know them in this Member State. Frequently, the provisions found in legislation of this character and which implement the objectives of the internal market, have been formulated, negotiated and adopted in order to accommodate and realign the circumstances of markets and regulatory regimes which, for reasons of history, economics or administrative culture may be radically different from those with which we are familiar or have taken for granted as the background against which the measure is to be applied. Thus, for example, one the main thrusts of the applicants' challenge in this case has been directed at the manner in which the Contested Decision proposes to integrate for tariff setting purposes the offshore infrastructure comprising the interconnectors with the onshore transmission network. The applicant strongly objects to the removal of a tariff for the entry point at Moffat based upon the separate recovery of the costs of the interconnectors. However, as pointed out below, the relevant provisions must be construed bearing in mind that they are applicable to all interconnector transmission pipelines both on-shore and sub-sea, irrespective of length. As already mentioned, one of the policy objectives which underlies the manner in which the internal market in this area is to be achieved is a move away from tariff regimes based upon "contract paths" that is, tariffs for transmission based upon the distance over which the supplier's gas flow is carried by the system operator.

Evidence

67. This case has been heard on affidavit and very extensive evidence, partly of a factual character but mainly of a technical nature, has been placed before the Court. On behalf of the applicants the principal evidence has been furnished in the grounding affidavit and a supplemental affidavit of Mr. Patrick Power, Managing Director of the applicant companies. Expert evidence in support of the applicants has been furnished by consultants of the Brattle Group, Mr. Carlos Lapuerta and Mr. Daniel Harris. That Group is an international consultancy firm specialising in economic and financial analysis in the energy sector including electricity and natural gas. As mentioned elsewhere in this judgment, experts within the Brattle Group have been engaged extensively in providing research, analysis and advice for the European Commission and the agencies involved in the liberalisation process towards implementing the internal market in the energy sector.

68. The main affidavits on behalf of the CER have been provided by Mr. Denis Cagney its Director of Gas, Renewables and Legal Affairs. Expert evidence in support of the CER has been adduced in the form of a report of Mr. Fabrizio Hernandez Pampaloni of NERA Economic Consulting. On behalf of BGE affidavit have been sworn by John Barry, Senior Executive and expert evidence has been furnished in the form of a report provided by Mr. Wynne Jones, Economist, of Frontier Economics dated the 5th November, 2012.

69. This expert evidence discloses a divergence of opinion on a number of issues and particularly as to the Article 13 arguments described later in this judgment. There is a disagreement especially as to the degree to which the use of an LRMC methodology to create differentials between entry point charges will ignore "actual costs" and give rise to cross-subsidies and discriminationory treatment. In the event the Court does not consider that it is necessary to reach any conclusive decision on those areas of expert disagreement because, for the reasons set out below, the grounds advanced on foot of those propositions, as advanced prior to the final fixing of the proposed tariffs, turn primarily on the questions of the interpretation of the legislation.

The Prematurity Objection.

70. So far as the objection on grounds of prematurity is concerned, it is necessary to draw a distinction between two aspects of the Decision as set out in its Part 5 "Conclusion and Next Steps" at paragraphs 86 and 87. (See para. 51 above). It is clear that the CER has reached a final conclusion to the effect that the existing transmission entry tariff regime will be reformed in a particular manner namely, by ending the current distinction between the onshore assets and the offshore interconnectors. Under the proposed new regime the interconnectors will be treated as an integral part of the transmission system "no different to other assets". It is also clearly the settled intention of the CER in making that reform that henceforth the entry points to the system are to be located where gas transported from outside that integrated system actually enters BGE's regulated asset base (RAB) so that, in particular, the entry point for gas shipped from the United Kingdom will be at Moffat in Scotland.

71. In taking that step in the process the CER is discharging the duty imposed upon it by Article 41(6) of the Directive which makes it responsible "for fixing or approving sufficiently in advance of their entry into force at least the methodologies used to calculate or establish the terms and conditions for…" *inter alia* "connection and access and access to national networks"… and "access to cross-border infrastructures…". The Conclusion in Part 5 also indicates an intention on the part of the CER to base the new tariff regime on the forward-looking LRMC methodology although it is clear from para. 87 that no final decision on the actual tariffs to be applied or on the details of the methodology to be employed in arriving at such tariffs will be taken until such time as the CER has deliberated upon the methodology in conjunction with the Network Tariffs Liaison Group. Nevertheless, the CER has committed itself to the choice of one specific cost allocation methodology for those purposes and the applicants' case is that the particular LRMC methodology is in principle incompatible with the conditions of the legislation irrespective of its final contents or formulation.

72. In the judgment of the Court, at least so far as these aspects of the Contested Decision are concerned, there can be doubt but that a sufficiently clear and definitive step has been taken by the CER in exercise of a particular statutory power to render that part of the Contested Decision susceptible of judicial review. At para. 3 of the Contested Decision, the CER states: "The legislative basis for the decision is s. 10A of the Gas Act 1976 (as amended by s. 14 of the Gas Interim Regulation Act 2004 and Regulation 2 of SI 320/2005)". (See paragraph 30 above.) That section of the Act of 1976 includes at para. (17)(b) a power on the part of the Commission to:

> "…give directions to an operator from time to time in respect of the basis for charges for third party access to, or connection to, a facility under the control of the operator;" and, in sub-paragraph (c) notwithstanding the generality of that provision, to give directions as to 'the methods of charging to be included in the statement to be prepared by an

operator'".

Furthermore, sub-paragraph (e) provides that a charge for third party access to or connection to a "facility" is to be calculated in accordance with directions given by the CER so as to enable the operator to recover "the appropriate proportion of the costs directly or indirectly incurred in carrying out any necessary works"; and "a reasonable rate of return on the capital represented by such costs". The term "facility" is defined in subs. (1) of 10A as meaning a "transmission or distribution pipeline, and LNG facility or a natural gas storage facility".

73. Clearly, therefore, the CER has in the Contested Decision explicitly sought to exercise the statutory powers it has under s. 10A and while the full terms of the decision do not finally fix the actual charges for third party access and connection to the facility or definitively settle the terms or content of the methodology by which the new tariffs will be ultimately calculated, a definitive and final decision has been taken which settles two material aspects of the reformed regime. First, it settles the treatment of BGE's system of offshore and onshore transmission assets as one integrated infrastructure thus ending the separate treatment of the onshore network and the interconnectors for tariff setting purposes. In those circumstances it cannot, in the judgment of the Court, be said that this part of the Decision is so incomplete or lacking in sufficient certainty as to its effect, that a challenge to it is without legal basis or that it must be characterised as premature.

74. Secondly, the CER has decided in principle to move to a tariff regime where the tariffs will be calculated separately for each entry point on an LRMC basis although it has not yet set any such tariffs and will not do so until the details of the particular LRMC methodology to be used have been discussed and formulated in the Liaison Group and then determined by the CER. The extent to which this aspect of the reform remains outstanding and incomplete is evident from the way in which the CER's approach is earlier described at paragraph 66 of the Contested Decision:

> ". . . The CER appreciates the need for a platform for meaningful stakeholder involvement in working out the final details of the plan LRMC based tariff regime. . . . A Network Tariffs Liaison Group will be established, to be convened by the CER and consisting of the system operator and representatives of the upstream and downstream gas sectors. The Liaison Group . . . will provide a forum to communicate and discuss ongoing network tariff issues of interest to the industry, for example the form of LRMC/locational signals, the balance between cost allocation and forward looking signals, the treatment of future investment in this context, dealing with under/over recoveries etc. for clarity, it will not be a policy making body. Policy issues that arise at the meetings will be considered and decided up separately by the CER as appropriate."

75. It is nevertheless clear that a decision has been made in principle which commits the CER to that LRMC-based approach for the future and to the abandonment of the existing basis of the current tariff regime. It is on this basis that the Liaison Group will be established and conduct its discussions with the interested undertakings. As such, the Court considers that the Contested Decision has to be taken as constituting a decision of sufficient substance and significance to render it susceptible to judicial review in this regard also, even if its ultimate impact on actual entry point tariffs cannot yet be ascertained or predicted.

76. Furthermore, one of the main grounds raised by the applicants is that the use of an LRMC methodology to set entry tariffs is, per se, incompatible with the requirement of Article 13 of the Regulation that the tariffs and the methodology used to calculate them must "reflect actual costs". In other words, the applicants say that the CER cannot approve any tariffs based upon an LRMC model irrespective of what the final details of the methodology may be, because a forward-looking approach of that kind cannot and will not reflect BGE's "actual costs". (See further paragraph 48 below.) If that argument is well founded, the CER's decision, even in principle, to move to an LRMC-based approach is arguably *ultra vires* Article 13. If that were to be the case, it is obviously in the interests of all parties including the CER that the issue be clarified in order to avoid delay and the investment of resources in formulating a methodology which might subsequently be struck down.

77. For these reasons the Court is satisfied that the objection raised as to the prematurity of these aspects of the present application and the argument to the effect that the Contested Decision is incomplete or merely preliminary to a later substantive exercise of the CER's statutory power, are unfounded at least so far as the Contested Decision can be seen to constitute an explicit exercise of the power in s. 10A of the Act 1976, to reform the existing tariff regime in two respects namely, (a) by ceasing the separate treatment of the onshore assets and interconnectors so as to treat the entirety of BGE's transmission system as an integrated infrastructure and (b) by adopting in principle an LRMC methodology as the future basis for entry point tariff calculation.

The Main Grounds

78. As already summarised above, the main grounds advanced by the applicants as to the invalidity or illegality of the Contested Decision are effectively as follows:

> i) Article 13 of the Regulation is infringed by setting entry tariffs on the basis of the proposed LRMC methodology together with a "revenue shortfall" mechanism or common charge because this will fail to reflect "actual costs incurred";
>
> ii) Article 13 will be infringed also because such tariffs set separately for the entry points will fail to avoid cross-subsidisation, to provide incentives for investment and will not facilitate competition;
>
> iii) The use of that methodology will involve the grant of unlawful state aid contrary to Article 107TFEU and has not been notified to the European commission contrary to Article 108(3) TFEU.
>
> iv) The Decision will compel BGE to abuse its dominant position in the market for the transmission of natural gas in Ireland in violation of Article 4(3) TEU, Article 102 TFEU and Article 41.3 of the Directive by integrating the costs of the interconnectors and the transmission system thereby compelling the applicants to pay for an infrastructure they will not use.

79. In the manner in which the issues raised by the applicants under the heading of Article 13 of the Regulation were expanded upon in legal submissions and oral argument there appear to be in effect two distinct questions to be addressed as follows:-

> (1) Do the provisions of the Regulation and the Directive require that an interconnector which spans the border between two Member States to connect the two national transmission systems of those Member States must be treated separately from the transmission systems for tariff setting purposes? In other words, is it contrary to the meaning of those provisions for the CER to designate for tariff setting purposes the point at which an interconnector from one Member State joins the transmission system of the second Member State on the territory of the latter, as the entry point to the national transmission system of the operator in the former Member State?

(2) If not, is it nevertheless incompatible in principle with the requirements of those provisions and particularly with Article 13 of the Regulation for the CER to require BGE to recover its revenue requirement through a two part entry tariff applied to network users such as the applicants, based on a forward-looking methodology for long run marginal costs specific to each entry point combined with a shortfall charge common to all entry points?

The First Limb.

80. In relation to the first of these issues the applicants' argument can be summarised as follows. The relevant legislation and particularly Articles 2, 13 and 41 of the Directive make a clear distinction between inter-State interconnectors and the rest of national transmission systems. They are given a distinct definition and are treated separately. Secondly, interconnectors as such have distinct characteristics and functions. They have distinct and ascertainable costs. Until now the Irish interconnectors have been accounted for and have been remunerated separately so that the costs associated with access to and use of the interconnectors are and will remain readily identifiable.

81. Amongst the important distinguishing characteristics of the interconnectors are these. They are used exclusively for the purpose of importing into Ireland the gas shipped from the United Kingdom and elsewhere and thus operate in one direction only. The onshore transmission system of BGE, on the other hand, is a ring main pipeline to which entry flows can be made at any point and from which gas can be taken by customers at any exit point. The submarine section of the interconnectors operates at pressures up to 140barg as high volume interstate delivery pipelines. The onshore transmission system, on the other hand, operates at pressures of 70barg. The interconnectors "provide swing and balancing services" which are not provided by the onshore transmission system. The applicants will provide these and other commercial services and thus be in competition with the interconnectors. The interconnectors are subject to a licence issued to BGE by OFGEM - the United Kingdom national regulator. The BGE interconnectors serve four separate jurisdictions, - the State, Northern Ireland, the Isle of Man and the mainland of Great Britain. The BGE transmission system serves only the State. There are exit points from the interconnectors for the Isle of Man and Northern Ireland, but all exit points from the onshore system are within the State. The interconnectors are treated separately by the CER for the purpose of assessing the State's security of supply as required by Regulation (EU) No. 994/2010. There are different (and undisclosed) price arrangements for the transmission of gas via part of the inter-connector to Northern Ireland and Scotland.

82. Furthermore, it is submitted that the legislation explicitly distinguishes between the national transmission systems and the interconnectors. Thus Article 2(17) of the Directive (see para. 21 above) defines an "interconnector" as a transmission line which spans and interstate border "for the sole purpose of connecting the national transmission systems" in question, thus distinguishing between a national transmission system on the one hand and the interconnector on the other. It is submitted that the power which the CER purports to exercise can only be based upon its competence under s. 10A(17) of the Gas Act 1976 to "give directions to an operator from time to time in respect of the basis for charges for third party access to, or connection to, a facility under the control of the operator". (See para 30 above) In subs. (1) of that section "Facility" is defined as meaning "a transmission or distribution pipeline, an LNG facility or a natural gas storage facility". In the same subsection "Third Party Access" means "in the case of a downstream natural gas pipeline, transportation of natural gas through a pipeline operators pipeline . . .".

83. It is also pointed out that under para. (e) of subs. (17) (above) it is provided that: "a charge for third party access to, or connection to, a facility under the control of the operator should be calculated in accordance with directions given by the Commission under this section so as to enable the operator to recover – (1) the appropriate proportion of the costs directly or indirectly incurred in carrying out any necessary works, and (2) a reasonable rate of return on the capital represented by such costs". The applicants argue that given the connection created between the charge for third party access and "a facility" ie. a transmission pipeline in this case, the power of the respondent is limited to setting a tariff for access by a third party to such a facility in order to use it and it could not, accordingly, extend to setting a tariff for not using a facility.

Findings of the Court.

84. In the judgment of the Court, the reliance placed upon the fact that Article 2(17) of the Directive contains the above definition of "interconnector" for this purpose is mistaken. The term "transmission" is defined in Article 2 as meaning "the transport of natural gas through a network, which mainly contains high pressure pipelines, other than an upstream pipeline network and other than the part of the high pressure pipelines primarily used in the context of local distribution of natural gas, with a view to its delivery to customers, but not including supply". While an interconnector is identified as a pipeline which has the sole purpose of spanning a border to connect two national transmission systems, it is still a "transmission pipeline" other than an upstream pipeline network or a pipeline primarily used for local distribution to customers. In the judgment of the Court, the term "interconnector" is not so defined in order to form part of the basis for the setting of tariffs. It merely identifies it as a particular type of transmission pipeline which has the specific purpose of connecting two national systems. That does not appear to preclude the particular transmission pipeline being used for part of its length for other functions as is the case with the first of these interconnectors. It is to be noted that in para. (4) of Article 2, the term "Transmission System Operator" is defined as meaning " a natural or legal person who carries out the function of transmission and is responsible for operating, ensuring the maintenance of, and if necessary, developing the transmission system in a given area and, where applicable, its interconnections with other systems . . . etc." (Emphasis added.) Thus the operation, maintenance etc of an interconnector is but one facet of the operator's function of operating its transmission system as a whole.

85. It seems to the Court that the applicants' view of these interconnectors as a distinct and significant infrastructure may be unduly influenced by the historical circumstances in which they came about and by the fact that until now, 95% of natural gas supply in the State has been supplied through them with their associated costs having been allocated to the Moffat entry point and paid for the shippers using that entry point. That historical arrangement, however, has not been based upon any express requirement of the legislation in question. It happens that the two interconnectors are a major piece of distinguishable infrastructure in that they are 200km in length and laid under the Irish Sea. The provisions of the Directive, however, apply to all inter-state interconnectors and make no distinction between submarine interconnectors and onshore interconnectors. Indeed, the majority of interconnectors between Member States are onshore transmission pipelines and in the more densely populated areas of continental Europe are presumably comparatively short in length. (There are apparently only two other submarine interconnectors between Member States namely, English Channel pipelines between the United Kingdom and Belgium and the Netherlands.) It can also be surmised that had the two BGE interconnectors not been laid first, the interconnection between the Irish network and the United Kingdom national transmission system might have taken the form of a relatively short cross-border onshore transmission pipeline from the transmission system in Northern Ireland supplied from what is now the third sub-sea pipeline from South West Scotland to Belfast.

86. If the applicants were correct in their proposition that the legislation means and requires that interconnectors, irrespective of their length or location onshore or sub-sea must be separately accounted for and tariffed, it would seem to be disproportionate and inefficient that an inter-connector of only a few kilometres in length joining two major national networks each comprising many hundreds of kilometres of pipelines should require to be so costed and tariffed when its associated costs may be miniscule in the

context of the operating costs of the operator concerned.

87. As mentioned above, the first of the interconnectors does not have as its "sole purpose" the connection of the Irish and United Kingdom national transmission systems. It operates as an extension to the UK national transmission system for the supply of gas to the Isle of Man and, via South-West Scotland, to Northern Ireland.

88. In the judgment of the Court, therefore, while the term "interconnector" has its own definition in the Directive it does not constitute the basis for any separate, substantive treatment of such a transmission pipeline for tariff-setting purposes. As is clear from the definitions of "Transmission" and "Transmission System Operator" above, the functions for which such an operator is responsible include the transmission of gas through interconnections. Recital (32) to the Directive explains: "National regulatory authorities should be able to fix or approve tariffs or the methodologies underlying the calculation of the tariffs, on the basis of a proposal by the transmission system operator . . ." and requires that in approving such tariffs the regulator is to ensure that they are "non discriminatory and cost-reflective". In other words, the tariffs are to be reflective of the costs of the operator as a "transmission system operator" as defined in Article 2(4) and those operations include the operation, maintenance and development of the system's interconnections with other systems as mentioned above.

89. That the legislation treats a transmission system operator as having responsibility for the system in a way which includes interconnectors is also evident from the provisions of Article 13(2) and Article 41(6) of the Directive. Article 13(2) obliges a transmission system operator to build sufficient cross border capacity to integrate the European transmission infrastructure and Article 13(4) provides that regulatory authorities may require such operators to comply with minimum standards for the maintenance and development of the transmission system including its interconnection capacity. Article 41 of the Directive sets out the duties and powers of the regulators and provides in para. (6) that they are to be responsible for fixing and approving in advance of entry into force the methodologies used to calculate or establish the terms and conditions for, *inter alia*, connection and access to national networks and access to cross border infrastructures.

90. For theses reasons, the Court is satisfied that there is no express or implied provision to be found in the legislation whether the Regulation, the Directive or s. 10A of the Gas Act 1976 (as amended) which requires an interconnector as such to be treated as a distinct or stand-alone infrastructure which must always be separately costed and tariffed.

The Second Limb: the Article 13 arguments.
91. Turning to the second limb of the grounds summarised at para. 78 above, the applicant submits that even if there is no explicit statutory requirement to treat the interconnectors separately for tariff setting purposes it is nevertheless incompatible with the requirements and conditions of the legislation and therefore outside the terms of the power upon which the CER relies, to set a tariff for third party access to the transmission network on a basis which integrates the onshore and offshore assets thereby eliminating the existing separate recovery of the costs associated with the interconnectors. It is, it is submitted, ultra vires the relevant provisions to adopt the proposed two-part tariff described in paras. 43, 44 and 51 above (Option 5) based upon a) the application of the forward looking LRMC methodology to set a tariff for transport of gas from each entry point, thereby treating the entry point at Moffatt as a point of entry to the onshore transmission network in Ireland; and b) recouping any shortfall in the revenue requirement from that entry tariff by means of a common charge on all entry points.

92. In particular, the applicants argue that the basis for such a two-part entry point tariff fails to comply with the requirements of Article 13 of the Directive namely that tariffs set by the CER must:-

- Be transparent;

- Reflect actual costs incurred;

- Be applied in a non discriminatory manner;

- Be set separately for every entry point into the transmission system;

- Avoid cross subsidies and

- Provide incentives for investment.

93. The applicants submit that the requirement of Article 13(1), that tariffs be set separately for each entry point on a non-discriminatory basis means that the tariff at each given entry point must reflect the actual costs incurred at that entry point. At the moment that is what is done at Moffatt and Inch.

94. The expression "actual costs incurred" necessarily requires that historic costs be the basis of the tariff and this will not be so if an explicitly "forward-looking" methodology is employed. The shippers of gas who use the interconnectors are not asked to underwrite the costs of the applicants' pipeline to Foynes or the Mayo/Galway pipeline. Thus there will be discriminatory treatment of the applicants as compared with the treatment of the shippers using the interconnectors.

95. The Contested Decision will have the effect of requiring the applicants to cross-subsidise the users of the interconnectors by forcing them to contribute to the costs of an infrastructure facility they do not and cannot use. Because the applicants will be competing with the shippers from the United Kingdom through the interconnectors, they will be placed at a competitive disadvantage. This will also act as a deterrent to future investment in competing infrastructure contrary to one of the objectives defined in Article 13(1) of the Regulation.

96. The use of a revenue shortfall or "common charging" element will have the effect of imposing an additional charge upon the three entry points (i.e. Foynes, Inch and Bellanaboy,) that will compete with BGE's interconnectors, in order to compensate BGE for any shortfall that results from the application of the LRMC tariff. This will create a cross subsidy in violation of a strict requirement of Article 13(1).

97. Furthermore, the application of the proposed tariff regime to the applicants' business on the same basis as other shippers will be discriminatory. The operations of the second-named applicant are tied to the use of the importation terminal and the entry point at Foynes which the applicants have paid to build. It cannot use any other entry point, but will nevertheless be compelled to contribute to the costs associated with the interconnectors. There is thus discrimination in favour of shippers importing from the UK to the detriment of the applicants and the producers on the Corrib pipeline.

98. The Contested Decision involves imposing on the applicants a mandatory cross-subsidisation of the users of the interconnectors in violation of Article 13(1). Article 13(1) requires that non discriminatory tariffs must be set separately for every entry point into and exit point from the transmission system and reflect actual costs incurred in so doing. The CER explicitly proposes to maintain a premium or "differential" in the entry tariff level which is clearly inconsistent with the requirement that the tariff be set separately at each entry point to reflect the actual costs incurred.

99. The expert report furnished by Mr. Lapuerta for the applicants dated the 10th December, 2012, articulates the essential basis of the challenge advanced on foot of non-compliance with the requirements of Article 13.1 of the Regulation. In the opinion of Mr. Lapuerta the use of the LRMC methodology when applied to the merged costs of the interconnectors and the onshore network to set the tariffs for each entry point will:

> "Ensure that the differences in entry tariffs for the various entry points would reflect nothing more than projections of the hypothetical future costs of expanding entry points in the event of congestion. Any projected future costs will then be ignored as soon as they are actually incurred and the LRMC system will then look past the relevant costs into the more distant future, to a new day when a new wave of congestion might occur."

100. He points out that new entry tariffs for the interconnectors will necessarily recover less than their actual costs incurred so that the deficit will be made up in part by raising entry points tariffs elsewhere and thus involve an exercise in cross subsidy.

Findings of the Court.
101. It is convenient to address first the applicants' argument in relation to "actual costs" as this is at the heart of the submission that the proposed tariff regime infringes Article 13 by adopting a forward looking LRMC methodology which cannot, per se, take into account or reflect the actual costs incurred by BGE in the operation and maintenance of the interconnectors. There is, accordingly, a dispute as to what is meant by "actual costs" in Article 13(1) of the Regulation.

102. In considering this issue it must be borne in mind that the process of setting tariffs to be applied as charges imposed upon shippers for access to the entry and exit points on the network is one which involves a number of steps. Broadly speaking it involves first ascertaining the overall "revenue requirement" which the operator needs in order to cover the costs of maintaining, operating and developing the transmission system. Next, a methodology must be devised which allocates the costs in order to determine how, from which sources and in what proportions the operator will recover that revenue requirement. Thirdly, the process involves calculating and fixing the various tariffs which will be charged to the users of the individual entry points and the exit points which will constitute the sources. It is important to note that the applicants' challenge to the proposed use of the LRMC methodology for the purpose of allocating costs between the entry points is concerned only with the second stage of that process. The revenue requirement is based upon the operator's actual incurred costs subject only to adjustment for inefficiencies and appropriate return on investment.

103. The process was described in more detail in a document published by the Agency for the Cooperation of Energy Regulators ("ACER") dated the 17th September, 2012, entitled "(Initial) Impact Assessment for the Framework Guidelines on Harmonised Transmission Tariff Structures" which relied *inter alia* on a report prepared by the Brattle Group (whose principal Mr. Carlos Lapuerta provided the applicants' expert report in the present case): "While in general terms most national regulatory authorities and transmission system operators in the EU use a similar mechanism for setting tariffs, the details of the mechanisms vary widely. The typical steps for setting tariffs are:-

> 1. First, the NRA determines the TSO's [transmission system operator's] allowed revenue. This is usually determined by a combination of depreciation, return on capital and operating costs;
>
> 2. A forecast is made for capacity/throughput demand for each entry and exit point over the regulatory period and also in some cases the distance that the gas will travel;
>
> 3. The cost that must be recovered from each entry and exit point is then determined. We refer to the process of allocating costs that must be recovered from groups of entry and exit points as cost allocation;
>
> 4. Finally, the reference price at each entry and exit point is determined. Often this is done simply by dividing the costs allocated to that point by the expected demand at the point (or group of points)."

104. That Impact Assessment also commented upon the policy objectives for transmission tariffs in Article 13 of the Regulation namely, facilitating trade and competition; avoiding cross subsidies and undue discrimination between users; costs reflectivity; the promotion of efficient investments; and transparency. It points out that there are tensions and trade offs between those objectives and then observes:

> "Discrimination is closely linked to the idea of cost-reflectivity. If tariffs are broadly cost reflective, then discrimination is not possible, since all users will be paying roughly in proportion to the cost they create. Moreover, cross-subsidy occurs only in the absence of cost-reflectivity. If tariffs were perfectly cost reflective there would be no cross subsidy. If tariffs are not cross reflective, so the price user pays for a service is not closely related to its underlying cost, then the difference between the price of the transport service and the cost of providing it can be regarded as a penalty or burden that it borne by transport customers. Hence tariffs that are not cost reflective are discriminatory, since some market participants will tend to bear a higher burden than others. Accordingly, there is a strong relationship between the objective of non-discrimination and the objective of cost-reflectivity. However, it is also important to understand that full cost reflectivity is not possible in an entry/exit system where tariffs are based on the average cost of the system. The objective should therefore be interpreted as therefore broad cost reflectivity rather than absolute cost-reflectivity for every capacity contract. Similarly a certain amount of cross-subsidy is inevitable if tariffs cannot always be perfectly cost reflective."

105. In the judgment of the Court, the applicants' arguments in this regard are flawed. In the first place, it is clear from the scheme and objective of the Regulation and the Directive and from the nature of the tariff-setting process that the essential objective sought to be achieved is an overall correspondence between the aggregate remuneration or income the operator is allowed to exact from the sale to users of access to the transmission system on the one hand and the revenue it needs to cover the costs incurred or estimated as proper to be incurred during the period for which the tariffs are fixed in efficiently maintaining, operating and developing the system, on the other. Although Article 13.1 (fourth paragraph) refers to "costs allocation mechanisms" implying that it is the costs that are apportioned as if they are incurred in respect of identifiable and distinguishable parts of the network infrastructure, what is really required and what is in fact done is that the total estimated income required to cover the actual costs is apportioned first as between the exit and entry points and then as between the individual entry points. It is the aggregate end result of that

apportionment exercise that is required to correspond to the operator's allowable incurred costs. It is the tariffs that are to be set separately for entry as opposed to exit points. Thus the allowable costs included in the total revenue requirement form the basis of the tariffs and are reflected in their estimated overall income.

106. The applicants' contention as to the mandatory reflecting of incurred costs at each separate entry point is, in the view of the Court inconsistent with the basic innovative objective of the 2009 reform. As explained in Recital (19) of the Regulation, the new measures required a move away from tariffs based on usage and distance by abolishing "contract path" tariffs so as to enable users to book entry and exit capacity independently thereby enhancing competition in the wholesale gas markets: "Tariffs should not be dependent on the transport route. The tariff set for one or more entry points should not therefore be related to the tariff set for one or more exit points, and vice versa." Article 13(1), fourth paragraph, of the Regulation specifically prohibits the use of network charges calculated on the basis of contract paths. If, as the applicants argue, the costs of each entry point are to be reflected (in the sense of equating to) the revenue to be derived from the tariff for that entry point, the process would cut across the achievement of that objective.

107. It is also to be noted that it is by no means clear that the Regulation requires that a distinct tariff be set separately in respect of each entry point on a system. The essential purpose or objective of the entry/exit approach and the elimination of contract paths as explained in Recital (19) is to give users the freedom to book entry capacity independently of booking exit capacity. The final sentence of the paragraph refers to "the tariff set for one or more entry points" (emphasis added) suggesting that it is the separation of entry tariffs from exit tariffs that is crucial and not necessarily the separation of entry tariffs *inter se* as well. A single tariff may be set for several entry points. In the Contested Decision of course the CER proposes to set entry tariffs on that basis using the LRMC methodology to set a reserve for the auctions to be conducted for access to each entry point in order to provide a premium or differential available to reward developers of efficient new sources of supply.

108. In the judgment of the Court what the legislation envisages and requires is that there should be a broad correspondence between the total revenue exacted by the operator from access tariffs and the amount of revenue it requires for the maintenance, operation and development of the transmission system when operated efficiently. The actual costs are confined to those incurred in the operation, maintenance etc of the transmissions system as defined in Article 13.1 and exclude costs incurred in other activities or costs attributable to inefficiencies. They are the costs of the transmission system as a whole and there is nothing in the scheme of the legislation which can be construed as requiring those costs to be calculated or estimated by reference to specific parts of the infrastructure. Again, the approach of the applicants is clearly based on the fact that the costs of the interconnectors have in fact been separately identifiable and used as the basis for the Moffat entry point until now. It must be questionable whether when applied to transmissions systems generally including those without that particular history, it is reasonably feasible to achieve cost reflectivity in respect of distinct parts of the infrastructure with multiple entry points given that important parts may have multiple functions not necessarily attributable to a single entry point. Furthermore, as is pointed out in the NERA Report, individual parts of the system may have "externalities" on other parts. While the applicants complain that they will not use the interconnectors, it does not follow that they derive no benefit from their existence. The interconnectors provide an important supply security which benefits all users so that setting cost reflective tariffs for each entry point as the applicants contend would involve allocating such system benefits across all entry point users.

109. So far as the terms of the legislation are concerned there are a variety of possible ways in which a national regulator can approach the exercise of cost allocation in the third step of the tariff setting process including, as heretofore in this case, the allocation of ascertained historical costs of the interconnectors to their users. The selection amongst the available solutions in that regard is however a matter for the expert appraisal of the national regulator subject to compliance with the relevant criteria and conditions of the legislation. There can therefore be no necessary or *per se* illegality in the choice of an LRMC methodology as the basis of the cost allocation mechanism between entry points.

110. It is recognised by the European Commission and by ACER and the other agencies such as the European Network of Transmission System Operators for Gas (ENTSO) that have been involved in advising on the liberalisation programme and in the drawing up of Guidelines, Working Papers and studies which have informed much of the consultation process leading to the Contested Decision, that the very use of an entry/exit approach is incapable of achieving a one hundred per cent cost reflectivity and may possibly give rise to some element of cross-subsidy as between entry points (which would constitute a form of discrimination). The point is made in the ACER document of 17 September 2012 referred to at paragraph 103 above: "Cost reflectivity is a key principle of tariff setting, as stated in [the Regulation] and fully reflective tariffs can be considered non-discriminatory when eliminating cross-subsidies. There is a debate on the interpretation of this principle, whether the cost reflectivity principle should be applied on an aggregated or individual level. …. The principle of entry/exit tariffs consists in finding a balance between the cost reflectivity principles being applied on an aggregated or individual level." (Original emphasis.)

111. The choice of methodology and the striking of that balance in application of the costs reflectivity principles is essentially one for the expert appraisal of the CER as described in paragraph 62-63 of this judgment. What defines the boundary between a lawful and an unlawful tariff resulting from those policy choices is whether or not the end result embodies or causes a degree of cross-subsidy or discrimination which is excessive, disproportionate and avoidable. That determination can only be made, in the judgment of the Court, when the terms of the actual methodology have been settled and published and the entry point tariffs have been fixed. It is only then that it will be possible to measure any discrepancies that are caused in the relative treatment of the individual entry points.

112. Both the Regulation and the Directive effectively recognise that the complex process of opening up the transmission networks to competitive inter-state trade in this way can create risks of cross-subsidisation and discrimination in the markets and bring about abusive conduct and distortions to competition. That is why throughout the Regulation and the Directive the need to avoid such outcomes is reiterated – see for example, Article 13.1, second and third paragraphs of the Regulation; and Articles 13(1) (b), 31(3), 41(1) (f) and 41(13) of the Directive.

113. That the CER is also conscious of these imperatives is also evident in its determination to finalise the terms of the LRMC methodology and the definitive tariffs only after further deliberation and consultation in the Network Tariffs Liaison Group. As already cited at paragraphs 72-74 of this judgment, at paragraph 66 of the Contested Decision the CER undertakes that the Group will meet regularly throughout the tariff determination process and will have as its function to provide:

> "a forum to communicate and discuss ongoing network tariffs issues of interest to the industry, for example the form of the LRMC locational signals, the treatment of future investment in this context, dealing with under/over recoveries etc."

In paragraphs 69-72 the CER acknowledges the possibility that adopting Option 5 is capable of giving rise to questions of compatibility with EU law (including State aid) and accepts its duty to comply at all times with applicable laws. Furthermore, it expressly confirms that "the precise detailed methodologies for setting tariffs will also have to be fair and non-discriminatory."

114. In the judgment of the Court the proposed adoption of an LRMC methodology as the basis, in part, for the separate setting of entry point tariffs cannot be said to be *per se* or in principle incompatible with the requirements and criteria laid down for that process in the legislation. As such, a ground for quashing the Contested Decision on that basis has not been made out. Whether those criteria are ultimately satisfied in the tariffs as fixed will depend on the degree to which the resulting differentials between the entry point charges can then be shown to exceed what is reasonable, proportionate and avoidable by way of cross-subsidy, discriminatory treatment or other distorting or anti-competitive effects.

Competition Rule Grounds
115. There remain, accordingly, the grounds advanced upon the basis of alleged infringements of the competition rules namely, first, that the effect of the Contested Decision will be to enable or compel BGE to abuse the dominant position it occupies in the market in the State for the transmission of natural gas contrary to Article 4(3) TEU, Article 102 TFEU and Article 41.3 of the Directive; and secondly, that it will involve the grant of an unlawful State aid contrary to Articles 107 – 108 TFEU.

Abuse of Dominant Position
116. The applicants submit that BGE holds a position of dominance in the market for the transmission of natural gas in Ireland and, as that geographic market covers the entire territory of a Member State, it constitutes a substantial part of the common internal market. In effect, BGE has a monopoly both in law and in fact as operator of the national transmission system.

117. The applicants argue that this dominant position will be abused in a number of respects by the implementation of the tariff regime proposed in the Contested Decision. First, it is submitted that charges for access to the onshore transmission system must be based exclusively on the costs of operating and maintaining that system and should not include the costs of the interconnectors which the applicants will not use. Because the proposed regime will include in the entry and exit charges imposed on the applicant the costs incurred in the operation of the interconnectors, the charges imposed upon the applicants will be unfair and in excess of the value of the service actually used by the applicants.

118. Secondly, the effect of the new regime will be to impose unfair terms in the form of supplementary obligations upon users of the transmission systems such as the applicants by requiring them to bear part of the costs actually incurred by the operator on infrastructure which the applicants do not use. Thirdly, there will be abuse in the form of "margin squeeze" because the tariffs will have the effect of reducing the costs of using the interconnectors while increasing access costs at the other entry points, thereby making it economically more attractive for importers to use the interconnectors. BGE has a monopoly on the market for transmission services onshore within the State, but at the same time is present on the market for the transportation of gas to the onshore network by providing services for the use of the interconnectors. The example is given of a shipper of LNG by tanker which has the choice of off loading at the applicants' Shannon facility to enter the onshore transmission system at Foynes or alternatively of off loading at a UK terminal in order to transport the gas via the UK network and the interconnectors to the Irish onshore network.

State Aid
119. According to the applicants, the proposals in the Contested Decision also result in a grant of aid contrary to Article 107(1) TFEU which has not been notified to the European Commission as required by Article 108(3) TFEU. In the absence of such notification and the receipt of a determination from the Commission that what is proposed is compatible with the State aid rules, the State, including the CER as a public authority, is prohibited from implementing the aid.

120. The applicants contend that the new tariff regime will bring about the grant of aid because charges currently borne and budgeted for by the shippers using the interconnectors from the United Kingdom will be reduced at the expense of suppliers joining the onshore transmission system within the State. The purpose of the new tariff structure is to reduce the charges imposed upon the UK suppliers although the costs of the interconnectors will remain unchanged. The reduced revenue otherwise applicable to discharge those costs will be recouped from the users of the onshore entry points although the latter continue to bear the cost of transportation of their supplies to the onshore entry points. In other words, the Contested Decision constitutes an intervention by a public authority in this market which will have the effect of reducing charges otherwise borne by one particular category of undertakings (the UK shippers), in order to make it financially attractive for them to continue using the interconnectors. Furthermore, the tariff regime will have the effect of granting a subsidy to BGE and its subsidiaries in the operation of the interconnectors. They will receive a guaranteed income to cover the costs of operation of the interconnectors regardless of the extent to which the interconnectors are actually used.

Findings of the Court.
121. It is possible to deal together with the arguments advanced under these headings but by way of preliminary observation, it is to be noted that these grounds based on infringements of the competition rules are raised in the context of a market that is the subject of regulation and are advanced both against the national regulator for the sector and the incumbent operator of the transmission system. At first sight it might seem strange that anti-competitive conduct could arise as a consequence of compliance with a direction issued by the regulator of the sector under measures adopted within the framework of the legislative programme for the establishment of the competitive internal market for the sector.

122. There is, however, no doubt but that the competition rules of the Treaty apply to undertakings in the energy sector and there are no special competition rules for these markets such as apply, for example, in the agricultural and transport sectors other than the rules governing nuclear energy which is covered by its own treaty. In common with other sectors based upon networks such as the telecommunications sector, it is well recognised that anti-trust rules alone cannot guarantee effective competition. Hence the need for the series of measures referred to above (the Third Energy Package) directed at the gradual liberalisation of the gas and electricity sectors culminating in the 2009 Regulation and Directive which seek to unbundle the long established vertically integrated monopolies across the Union.

123. While the principle of the hierarchy of norms means that the legislative measures considered in this judgment cannot be regarded as curtailing the inherent scope of the primary competition rules of the Treaty, it is nevertheless the practical reality that a party to litigation who seeks to assert that a commercial practice authorised or directed under the legislation infringes Article 102 TFEU or the State aid rules, faces a difficult onus of proof.

124. It is also clear however that infringement of those rules can occur even within the framework of a package of liberalisation measures. For example, a refusal of access to a network by a transmission system operator on grounds which are inadequate, discriminatory or unsubstantiated for the purposes of Article 35.1 of the Directive, could in principle infringe Article 102 TFEU although it would primarily constitute a decision which is invalid under the Directive.

125. It is also evident that questions of possible State aid can and have arisen in these sectors and particularly in relation to national measures adopted to assist incumbent undertakings with "stranded costs" resulting from investment in pre-liberalisation plant which

becomes inefficient and uncompetitive as a result of price reduction brought about by the liberalisation process.

126. Where a network operator is accused of abusive conduct contrary to Article 102 TFEU, when acting within the framework of a regulatory regime, the essential question to be asked is whether the conduct in question and its effects are attributable to the commercial choice of the operator or to its compliance with a binding direction on the part of the regulator. An example of that issue is to be found in the judgment of the Court of Justice of the European Union in case C-280/08P *Deutsche Telekom v Commission* [2010] I-ECR 3555. There the German network operator had been accused of abusive margin squeeze between its wholesale and retail prices but sought to rely by way of defence upon the fact that network access prices were regulated by the national telecom regulator. It was held, however, that Deutsche Telekom was entitled to adjust its end-user prices by applying to the regulator for authorisation to increase them and, as a dominant undertaking, had a special responsibility to do so in order to avoid distorting competition. The Court accordingly held that the pricing practice which was impugned was attributable to the commercial conduct of the operator and not to the binding direction of the Regulator. It was not an instance in which the operator was precluded from facilitating competitive activity by a binding requirement of the regulatory regime. (See paras. 80 – 85 of the judgment).

127. In the judgment of the Court there are several reasons why neither of these competition rule grounds can be considered to have been made out in the circumstances in which this application for judicial review has been brought. As matters stand, no actual tariffs have yet been set and no entry or exit charges have been calculated by BGE. As already pointed out above, whether or not there will ultimately exist any of the elements of discrimination in the charges, cross-subsidy effects or the conferring of anticompetitive benefits or advantages on other undertakings, necessarily depends upon the precise terms of the methodology yet to be formulated, because it is only when that has been applied to specific access charges that it will be possible to examine the mechanisms by which the revenue requirement will be allocated as between the entry and exit point charges on the one hand and as between the different entry point charges themselves on the other. It is not seriously doubted that the exercise of apportioning the operating costs of the network (or their revenue requirement) as between the different entry points is not one which can be carried out with total accuracy or precision. One hundred percent cost reflectivity at each entry point is unlikely to be achieved. Similarly, it is inevitable that there may be some element of cross-subsidisation as between users across the network. What will be crucial will be the avoidance of unnecessary or excessive cross-subsidies or avoidable discrimination in the treatment of the entry points. Whether that exists and the extent which it can be measured as avoidable or unavoidable is, in the view of the Court, entirely dependent upon the outcome of the methodology and the application of the allocation mechanisms. That being so it cannot, in the judgment of the Court, be said that the decisions of principle contained in the Contested Decision as regards the choice of a particular methodology and the integration of the interconnectors with the onshore network must necessarily bring about abusive conduct on the part of BGE or the creation of a distorting benefit or advantage in favour of the applicants' competitors such as might constitute unlawful State aid.

128. It follows, accordingly, that insofar as the argument is made that the standstill prohibition of Article 108.3 TFEU is relevant, there is as yet no identifiable or quantifiable aid about to be granted which might be capable of notification.

129. It must also be pointed out that the decision as to whether or not the interconnectors are integrated with the onshore transmission network is exclusively one taken by the CER and not a commercial choice attributable to BGE. As a consequence, the aggregation of the costs of the entire infrastructure is not attributable to any autonomous commercial choice on the part of BGE, but is something imposed upon it as an essential part of the regulatory framework for the sector devised by the CER.

130. For these reasons, in the particular circumstances of this case it does not appear to the Court to be necessary to examine in any detail many of the assertions that are relied upon by the applicants as the basis for the alleged infringements of these articles, including, for example, the basis upon which the applicants define the relevant product and geographic markets or seek to identify particular forms of abuse of conduct such as unfair pricing or the imposition of unfair or discriminatory terms to charges for the transmission services provided. These assertions are to a large degree predicated upon an acceptance of the applicants' central propositions namely that the interconnectors constitute a separate infrastructure to be treated distinctly from the onshore transmission system and are to be tariffed exclusively by reference to the costs incurred on the operation of the interconnectors.

131. The Court would, however, comment in passing that the proposition that BGE will infringe Article 102 TFEU by conduct which amounts to "margins squeeze" would appear to be clearly unfounded. Indeed, it is difficult to understand how such a case can be made out in the circumstances of the gas sector in the State. Typically, margin squeeze occurs where a vertically integrated dominant undertaking itself engages in the supply of an input which is used on the downstream market while at the same time supplying the input product to third parties active on the market and competing with the dominant firm. The dominant undertaking can by means of a variety of tactics (raising its input prices, below cost selling on the downstream market for example,) seek to bring about a drop in its competitors' profits with a view to rendering their presence on the downstream market uneconomic.

132. The applicants' assertion that there exists such a downstream market here in the provision of services for transport of gas to Ireland is in the view of the Court contrived and unsubstantiated. It is, as mentioned, predicated on the assumption that the interconnectors are providing a service on a distinct market, which, as the Court has held, is an unfounded assumption. It must also be pointed out that it is the second-named applicant that is concerned by the proposed tariffs and it is not at all clear that that undertaking is engaged in a distinct market for the transportation of gas to Ireland.

133. It must be borne in mind that in any event a national Court has no function in deciding whether an alleged State aid is compatible or incompatible with the internal market: that is an exclusive competence of the European Commission. It is true that were there is *prima facie* evidence of the proposed grant of an aid which has not been notified to the European Commission as required by Article 108(3), a national court has jurisdiction based upon paragraph 4 of that Article to injunct its implementation. In the present case, however, quite apart from the fact that no actual aid has been identified as about to be granted and that the new regime will not in any event be introduced until at least October 2014, (see para. 51 above), the Court has evidence before it that the applicants' contentions under this heading are the subject of a complaint (case No. SA 33518) made to the Commission in 2011, which is currently under consideration by it. It would therefore be unnecessary and possibly improper for this Court to make any determination in respect of these contentions given that if there is any substance to them, the applicants' position will be fully protected by appropriate decision of the European Commission.

134. For all of these reasons the Court finds that the grounds advanced have not been made out and the reliefs claimed are refused.