

## **CRE's deliberation of 14 February 2008 on the assignment of an increased rate of return for projects aimed at the development of the Guyenne-Spain axis**

In its proposal submitted on 10 November 2006 concerning tariffs for use of natural gas transmission systems, the CRE adopted a real rate of return before tax of 7.25% for assets held on 1 January 2004. For investments cleared after this date a premium of 125 base points is applied.

In the preamble to this proposal, the CRE indicated that an additional increase of 300 base points *“could be assigned - after CRE deliberations, for a period of 5 to 10 years - to investments that are likely to make significant contributions to improving market operations, particularly by creating new entry points in the national network or by reducing network congestion, on the basis of requests sent upon the operator's own initiative”*.

The CRE was referred three such requests (two from TIGF dated 16 November 2007 and one from GRTgaz dated 25 October 2007), asking for a rate of return increase of 300 base points for a period of 10 years.

The requests were related to two separate projects:

- a TIGF request to revise the asset base eligible for an increased rate of return as part of the current reinforcement of the Guyenne pipeline (phase 1 of the project as well as phase 2, which has been moved forward);
- two requests to develop the Guyenne-Spain axis: phase 3 of the reinforcement of the Guyenne pipeline (by TIGF and GRTgaz), and the development of Lussagnet-Lacq pipeline (by TIGF).

### **1 Context**

#### ***1.1 CRE decision on 8 December 2005***

In 2005, TIGF and GRTgaz presented the CRE with a coordinated development plan for the Guyenne pipeline set out over 3 phases, and requested an increased rate of return for phase 1.

Phase 1, currently in progress, will increase the physical capacity of the Guyenne pipeline (in the TIGF-GRTgaz direction) to 180 GWh/day, including 150 GWh/day devoted to the evacuation of incoming LNG at the new Fos Cavaou LNG terminal and 30 GWh/day of marketable capacities.

The total amount of investment in phase 1 was estimated at €240 million - €175 million for TIGF and €65 million for GRTgaz.

In its decision delivered on 8 December 2005, the CRE considered that “*only the part of the initial phase of the project proposing a surplus capacity above that strictly required to evacuate gas from the LNG Fos Cavaou terminal, i.e. investments of €50 million for TIGF and €16 million for GRTgaz, can benefit from an increased rate of return of 3% for a period of 10 years, starting from the entry into service of the infrastructure*”.

### ***1.2 The South’s regional initiatives***

As part of the South Regional Initiative coordinated by ERGEG, the development of Franco-Spanish interconnections was identified as the leading priority to meet the objective of encouraging the emergence of a regional market in southern Europe, contributing to security of supply and improving market operations in Spain and the South of France.

A development plan for Franco-Spanish interconnections was jointly published by French (TIGF and GRTgaz) and Spanish (ENAGAS) TSOs on 6 February 2007. From a French perspective, the investment plan included provisions to strengthen the Guyenne (phase 3) and Lussagnet-Lacq pipelines.

## **2 Presentation of TIGF and GRTgaz requests**

### ***2.1 TIGF request concerning the revision of Guyenne phase 1 and anticipation of Guyenne phase 2***

Owing to the significant increase in costs and in anticipation of the work related to phase 2 of the Guyenne pipeline development project, TIGF revised the total amount of investment upwards from €175 million (initial estimation taken into account by the CRE in its deliberations on 8 December 2005) to €250 million.

Furthermore, TIGF has anticipated phase 2 of the Guyenne pipeline development, which will increase the capacity offered to the market to 80 GWh/day in the TIGF-GRTgaz direction, i.e. 50 GWh/day more than the 30 GWh/day initially forecast.

TIGF requests an upward revision of the asset base subject to the increased base rate granted in December 2005 by the CRE, with a view to providing for the increase in costs and the creation of supplementary capacities. According to TIGF assessments, the new base stands at 53% of the total amount of investments, estimated at €250 million, i.e. €132.5 million.

### ***2.2 TIGF and GRTgaz requests related to the development of the Guyenne-Spain axis***

Phase 3 of the Guyenne pipeline reinforcement, jointly conducted by TIGF and GRTgaz, will make it possible, by 2012, to increase the capacity of the Guyenne pipeline to 510 GWh/day in summer (375 GWh/day in winter) in the GRTgaz-TIGF direction, and to 255 GWh/day in summer (260 GWh/day in winter) in the TIGF-GRTgaz direction.

For TIGF, the work to be conducted during this phase is as follows:

- install two additional compressors, each with an 8 MW capacity, in the Sauveterre-de-Guyenne station;
- install two additional compressors, each with an 8 MW capacity, in the Lussagnet station;
- lay 60 km of piping with a nominal diameter of 800 mm connecting Lussagnet to Captieux.

For GRTgaz, planned work is as follows:

- create a 26 MW compression station and an interconnection station in Chazelles;
- adapt metering installations in Lamothe-Montravel.

The cost of phase 3 has risen to €308 million - €210 million for TIGF and €98 million for GRTgaz. The entry into service is scheduled for 2012.

In parallel with the reinforcement of the Guyenne pipeline, the development of the Lussagnet-Lacq pipeline will bring the interconnection capacities between France and Spain (Larrau interconnection point) to 165 GWh/day in both directions, the equivalent of 5 Gm<sup>3</sup> per year.

To increase the capacity of this pipeline, the following work is planned:

- installing additional compression power of 8 MW in the Mont station;
- installing 60 km of piping with a nominal diameter of 800 mm connecting Lussagnet to Lacq.

The cost of these works, which only concern TIGF, stands at €125 million. The entry into service is scheduled for the end of 2011.

GRTgaz and TIGF request that all these investments benefit from a rate of return increase of 300 base points, over a period of 10 years.

### **3 CRE observations**

#### ***3.1 TIGF request concerning the revision of phase 1 and anticipation of phase 2***

- a) The increase of TIGF investment costs linked to the roll-out of phase 1 of the Guyenne pipeline project is mainly a result of:
- significant increases in project unit costs, particularly with regards to engineering, material and civil engineering expenditures. This increase reflects current market tensions for the provision of services to oil and gas projects in Europe and throughout the rest of the world.
  - compliance with new statutory regulations, particularly with regards to safety (decree of 4 August 2006) and the environment (new emission standards).

Current tariffs for use of natural gas transmission systems call for the inclusion of assets into the Regulated Asset Base according to real investment costs. In this way, capital costs actually incurred by the operator are covered. However, these tariff rules do not provide for a retroactive application of the 300 base point premium to actual costs.

As a result, extra costs related to the implementation of phase 1 of the Guyenne pipeline project cannot benefit from an increase of 300 base points.

- b) TIGF's anticipation of phase 2 of the Guyenne pipeline development project will lead to the creation of 50 GWh/day additional capacities in the TIGF-GRTgaz direction.

During marketing operations of the link and interface capacities between balancing zones, coordinated jointly by GRTgaz and TIGF between mid December 2007 and mid-January 2008, capacity requests in the TIGF-GRTgaz direction, were twice as high as the available capacity. Additional capacities, created in preparation for phase 2 as set out by TIGF, are therefore a response to a real requirement and will help improve market operations in the South of France.

As a result, investments corresponding to the creation of the additional 50 GWh/day capacities for market players, i.e. €35 million for TIGF, can benefit from a rate of return increase of 300 base points over a period of ten years.

### ***3.2 TIGF and GRTgaz requests related to the development of the Guyenne-Spain axis***

The reinforcement project for the Guyenne-Spain axis is essential if the interconnections between France and Spain are to be developed. The project is among the European priorities defined as part of the ERGEG's South Regional Initiative.

Furthermore, the development of interconnections with Spain will significantly improve competition in the southern region of France by making it possible to enter additional quantities of gas from Spain. This project provides shippers with new possibilities when choosing between different supply sources and, according to specific circumstances, the end-consumer will therefore enjoy more competitive sources. It will also increase market liquidity which is currently insufficient in the South of France.

The Guyenne-Spain axis reinforcement project meets the application criteria for an increased rate of return for the reasons listed above.

### ***3.3 Changes to the incentive mechanism for investment in natural gas transmission systems***

In mid 2008, the CRE will propose new transmission tariffs that are due to come into force on 1 January 2009. To mark this occasion, it is planning to put forward proposals to modify the incentive mechanism for investment in natural gas transmission systems.

The planned changes are as follows:

- the withdrawal of the 125 base points premium currently granted to all new investments on the transmission system;
- an increase of 300 base points, over a ten year period, for all investments on the main transmission system that create additional capacities.

Past decisions related to rate of return premiums will not be challenged.

These changes will make it possible to better target investment incentives, whilst continuing to offer improved visibility to transmission system operators. They will be submitted for public consultation, as part of the preparatory work for the next transport tariffs.

In light of the forecasted entry into service dates (2011-2012) for the reinforced phase 3 Guyenne and Lussagnet-Lacq pipelines, and given that final investment decisions will only be taken after market consultations at the end of 2008 / beginning of 2009, these projects will be subject to the investment incentive mechanism that will be in force as part of the next tariff for the use of transmission systems.

## **4. CRE decision**

In light of all the above factors, the CRE has decided that:

*Decision concerning TIGF:*

- increased TIGF costs for phase 1 of the Guyenne pipeline development project, cannot benefit from an increased rate of return of 300 base points;
- investments belonging to phase 2 of Guyenne project - corresponding to the creation of 50 GWh/day of additional marketable capacities and to costs of €35 million for TIGF - will enjoy an increased rate of return of 300 base points, over a ten year period;
- investments related to the reinforcement of the Guyenne (phase 3) and Lussagnet-Lacq pipelines, as described in the interconnection development plan approved within ERGEG's Regional Initiative South, are eligible for the investment incentive mechanism that will be in force in the next tariff for the use of transmission systems.

*Decision concerning GRTgaz:*

Investments related to phase 3 of the reinforcement of the Guyenne pipeline, as described in the interconnection development plan approved within ERGEG's Regional Initiative South, are eligible for the investment incentive mechanism that will be in force in the next tariff for the use of transmission systems.

Paris, 14 February 2008

For the Commission de regulation de l'énergie  
The Chairman

Philippe de Ladoucette