

PREM 19/1290

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~~Confidential~~ Economic Co-operation between
Northern Ireland and the Republic of
Ireland.
Proposals for supply of Natural Gas to Northern
Ireland from the Irish Republic.

IRELAND

May 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
10.5.79		20.7.84					
16.5.79		8.8.84					
18.5.79		13.8.84					
1.6.79		15.8.84					
8.6.81		17.8.84					
7.9.81		23.8.84					
15.11.81		1.9.84					
18.11.81		5.7.84					
22.11.81							
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5.7.84							
13.7.84							
16.7.84							
18.7.84							
26.7.84							

From: THE PRIVATE SECRETARY

cc Press Office



NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

Charles Powell Esq
Private Secretary
10 Downing Street
LONDON SW1

5th September 1984

AT to see

NBM

CDP 579.

Dear Charles,

KINSALE GAS

The Prime Minister's message of 15 August to Dr FitzGerald made it plain that the Kinsale Gas project would not now go ahead. It is clear that the Irish accept that the project will not now go ahead - Mr Spring said as much at a news conference on Monday, and you told me that when Dr FitzGerald called on the Prime Minister on Monday he made only the briefest reference to Kinsale Gas, and had nothing of substance to say.

... We therefore propose to make a low key press announcement (on the lines of the attached draft) on 6 September to confirm publicly that the project is at an end, there will also be some additional material to correct the record with the Press on some of the points that the Irish have been making in public over the last few weeks.

Since the Irish do not wish to join us in a joint statement, the need for further consultation with them does not arise, but as a courtesy our Embassy in Dublin will be handing the Irish a copy of our statement shortly before it is released.

I am sending copies of this letter to the Private Secretaries to Members of E(A), to Colin Budd and to Richard Hatfield.

Yours Sincerely

Neil Ward.

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DRAFT STATEMENT BY ADAM BUTLER, MINISTER OF STATE

KINSALE GAS PROJECT

In my statement of 10 August I outlined the Government's position on the Kinsale Gas Project and indicated that we had discussed with the Irish Government the difficulties which we would face in carrying the project forward. In the light of the outcome of these discussions it is clear that it is not possible to reconcile the interests of both sides and that the project would not be economically viable for Northern Ireland. The project cannot therefore go ahead. I am bitterly disappointed that despite the intense efforts put into negotiations and discussion by both governments, the project to supply natural gas to Northern Ireland from Kinsale will not now go ahead.

IMMEDIATE

PS (6)
PS/LADY YOUNG
PS/MS WHITNEY

PS/S. G. S
PS/ MR R. ANDREW.
ORR 1/56

MR SPIDMAN

NIO

PS/PCS

MR ANGE

~~SIR R. ARMSTRONG~~

J. LYON

~~MR R. ARMSTRONG~~

MR JENNINGS

SIR R. ARMSTRONG

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FM DUBLIN 011225Z SEPT 84
TO IMMEDIATE FCO
TELEGRAM NUMBER 428 OF 1 SEPTEMBER 1984
INFO IMMEDIATE NIO (BELFAST) NIO (LONDON)

KINSALE GAS

SUMMARY

1. THE IRISH GOVERNMENT DO NOT WISH TO ISSUE A JOINT STATEMENT.

DETAIL

2. AFTER THE SECRETARY OF STATE FOR NORTHERN IRELAND'S DINNER WITH DR FITZGERALD AND MR BARRY ON 31 AUGUST, LILLIS, DORR AND I WITHDREW FOR HALF AN HOUR. I THEN SAID THAT I WAS DISAPPOINTED THAT KINSALE GAS HAD NOT BEEN DISCUSSED. WE HAD BEEN PROMISED AN ANSWER ON DR FITZGERALD'S RETURN. WE DID NOT WANT THIS TOPIC TO TAKE UP TIME BETWEEN DR FITZGERALD AND THE PRIME MINISTER ON 3 SEPTEMBER.

3. LILLIS IMMEDIATELY REPLIED THAT HE WAS AUTHORIZED TO GIVE ME THE IRISH GOVERNMENT'S ANSWER. IT WAS THAT THE IRISH GOVERNMENT WERE UNWILLING TO ISSUE ANY JOINT STATEMENT ON THE SUBJECT. AFTER MAKING QUITE SURE THAT HE WAS CONFIDENT OF HIS AUTHORITY, I REPLIED THAT IN THAT CASE I WOULD ADVISE HMG TO ISSUE A UNILATERAL STATEMENT AS SOON AS THEY WERE READY. LILLIS SAID THAT IT WOULD BE PREFERABLE FOR THERE TO BE NO STATEMENTS, BUT HE ACCEPTED THAT WE CONSIDERED ONE NECESSARY TO DISPEL UNCERTAINTY IN NORTHERN IRELAND.

COMMENT

14. I NOTE FROM THE PRESS ON 1 SEPTEMBER THAT IRISH TRADE UNION LEADERS HAVE WRITTEN TO HMG AND THE IRISH GOVERNMENT ON THIS TOPIC. THE IRISH GOVERNMENT WILL THEREFORE PROBABLY BE FORCED TO MAKE A STATEMENT IN REPLY, AND HMG MAY ALSO WISH TO DO SO. IN ANY CASE, I HOPE YOU WILL BE ABLE TO GIVE ME ADVANCE WARNING OF PUBLICATION OF ANY BRITISH STATEMENT AND IF POSSIBLE A TEXT WHICH I COULD HAND OVER TO THE IRISH IN ADVANCE AS A MATTER OF COURTESY.

5. I HAVE NOT YET MADE THE POINT TO THEM THAT TECHNICAL DISCUSSIONS AT WORKING LEVEL WILL BE NEEDED THEREAFTER, BUT I AM SURE THAT THEY REALISE THIS, AND I WOULD SEE NO OBJECTION TO DIRECT CONTACT WITHOUT FURTHER ADD BETWEEN THOSE RESPONSIBLE IN THE NORTH AND THE SOUTH AFTER PUBLICATION OF A BRITISH STATEMENT. I DO NOT THINK IT WOULD BE APPROPRIATE EARLIER.

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IRISH GAS DEAL OFF - REPORT

A DEAL TO SUPPLY NATURAL GAS FROM THE IRISH REPUBLIC TO NORTHERN IRELAND IS BELIEVED TO HAVE BEEN FORMALLY CALLED OFF BY MRS THATCHER. A LETTER FROM HER TO IRISH PREMIER DR GARRET FITZGERALD HAS BEEN DELIVERED IN DUBLIN AND WILL BE CONSIDERED BY THE REPUBLIC'S GOVERNMENT NEXT WEEK.

MRS THATCHER'S MESSAGE WAS HANDED OVER BY BRITISH AMBASSADOR IN DUBLIN, MR ALAN GOODISON, EARLIER THIS WEEK BUT OFFICIAL SPOKESMEN HAVE NOT DISCLOSED ITS CONTENTS.

IT IS THOUGHT CERTAIN THOUGH TO MARK REJECTION OF A MULTI-MILLION POUND AGREEMENT, WORKED OUT OVER THREE YEARS OF ANGLO-IRISH NEGOTIATING, TO PIPE GAS TO ULSTER FROM IRELAND'S KINSALE FIELD OFF THE COAST OF COUNTY CORK.

THE MOVE IS EXPECTED TO CONFIRM THE LOSS OF MORE THAN 1,000 JOBS IN NORTHERN IRELAND'S GAS SUPPLY INDUSTRY.

THE DEAL'S COLLAPSE WAS FORECAST EARLIER THIS MONTH BY DEPUTY IRISH PREMIER AND ENERGY MINISTER, MR DICK SPRING. HE CLAIMED BRITAIN WAS SEEKING A 50 PER CENT REDUCTION IN THE AGREED PRICE BECAUSE OF A CHANGE IN THE COST OF HEAVY FUEL OIL BUT STRESSED THERE WAS NO ROOM FOR MANOEUVRE ON THE PART OF HIS GOVERNMENT.

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PP DUBLIN

GRS 420

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FM FCO 17132UZ AUGUST 84

TO PRIORITY DUBLIN

TELEGRAM NUMBER 167 OF 17 AUGUST

MY IMMEDIATELY PRECEDING TELEGRAM: KINSALE GAS.

1. FOLLOWING IS PROPOSED TEXT FOR THE JOINT ANNOUNCEMENT.
BEGINS

2. OVER A PERIOD OF NEARLY THREE YEARS THE TWO GOVERNMENTS HAVE BEEN IN NEGOTIATION TO ESTABLISH THE BASIS OF A MUTUALLY BENEFICIAL PROJECT FOR THE SUPPLY OF NATURAL GAS FROM THE KINSALE FIELD TO NORTHERN IRELAND.

3. NEGOTIATIONS OF THIS NATURE IN THE ENERGY FIELD ARE OF NECESSITY DIFFICULT AND COMPLEX SINCE THE END PRODUCT MUST MEET THE INTEREST OF BOTH PARTIES IF THE AGREEMENT IS TO BE SUCCESSFUL. IN THIS CASE THE INTEREST OF THE IRISH GOVERNMENT HAS BEEN TO ENSURE THAT THE PRICE OBTAINED FOR ITS NATURAL GAS IS SUCH AS TO COMPENSATE FULLY FOR ITS REPLACEMENT FUEL. ON THE UK SIDE THE TERMS OF AGREEMENT HAD TO BE SUCH AS TO ALLOW THE DEVELOPMENT OF AN ECONOMICALLY VIABLE NATURAL GAS INDUSTRY IN NORTHERN IRELAND. A MEMORANDUM OF UNDERSTANDING WAS SIGNED IN OCTOBER 1983 PROVIDING THE MAIN TERMS ON WHICH A CONTRACT BETWEEN NORTHERN IRELAND GAS COMPANY AND BGE WOULD HAVE BEEN CONSTRUCTED. AT THAT TIME BOTH SIDES BELIEVED THAT THE TERMS AGREED WOULD ENABLE THEM TO MEET THEIR DECLARED OBJECTIVES.

4. FURTHER MONITORING OF KEY PROJECTIONS LED TO A REASSESSMENT OF THE PROJECT ON THE BRITISH SIDE, WHICH FORCED THE GOVERNMENT OF THE UK TO CONCLUDE THAT ON THE LATEST ASSESSMENTS OF PRICE AND MARKET DEMAND FOR GAS THE PROJECT WOULD NO LONGER BE ECONOMICALLY VIABLE. IN VIEW OF ITS FIRMLY DECLARED INTENT THAT THE PROJECT MUST NOT BE DEPENDENT ON SUBSIDY THE UK GOVERNMENT CONVEYED ITS DIFFICULTIES TO THE IRISH GOVERNMENT.

5. IN THE ENSUING EXCHANGES THE BRITISH SIDE MADE IT CLEAR THAT THEIR REASSESSMENT OF THE PROJECT DID NOT ALLOW IT TO BE VIABLE

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IN THE TERMS WHICH HAD ALWAYS BEEN INTENDED. THE IRISH GOVERNMENT COULD SEE NO JUSTIFICATION FOR ANY CHANGE IN THE TERMS OF THE MEMORANDUM WHICH WOULD HAVE PREVENTED IT MEETING IT CLEAR OBJECTIVE OF OBTAINING AN ECONOMIC PRICE FOR A VALUABLE NATURAL RESOURCE.

6. BOTH GOVERNMENTS DEEPLY REGRET THAT IN THE LIGHT OF THE SITUATION FACING THEM THE PROJECT CANNOT NOW PROCEED. IT IS PARTICULARLY REGRETTABLE THAT AFTER THE MAJOR EFFORT PUT INTO IT AND WITH BOTH SIDES ACTING REASONABLY AND IN GOOD FAITH A POSITION OF MUTUAL BENEFIT WAS NOT AVAILABLE. BOTH GOVERNMENTS HOWEVER, WISH TO MAKE CLEAR THAT THIS DISAPPOINTMENT OVER THE KINSALE PROJECT WILL NOT IN ANY WAY INFLUENCE ADVERSELY THEIR INTENTION TO CO-OPERATE IN PROJECTS WHICH ARE OF MUTUAL BENEFIT IN THE FUTURE.

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PP DUBLIN

GRS 360

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FM FCO 1713UOZ AUGUST 84

TO PRIORITY DUBLIN

TELEGRAM NUMBER 166 OF 17 AUGUST 1984

MY TELEGRAMS NOS 160-164 OF 15 AUGUST: KINSALE GAS.

1. THE PRIME MINISTER HAS AGREED THAT HER REPLY SHOULD BE HANDED OVER EARLY NEXT WEEK. WE UNDERSTAND THAT THE EARLIEST TIME THE IRISH CAN MANAGE IS 5PM ON TUESDAY 21 AUGUST. THAT DOES NOT PRESENT US WITH ANY DIFFICULTY. YOU SHOULD THEREFORE TAKE ACTION AS INSTRUCTED IN MY TELS UNDER REFERENCE.

2. MY TEL NO 161 PARA 6 PROMISED A FULL DRAFT TEXT OF A POSSIBLE JOINT ANNOUNCEMENT. THE TEXT IN MY IMMEDIATELY FOLLOWING TELEGRAM HAS BEEN AGREED INTERDEPARTMENTALLY. IT HAS BEEN SHOWN TO MR BUTLER WHO IS CONTENT WITH ITS GENERAL APPROACH.

3. OUR PRIME AIM IS TO PERSUADE THE IRISH TO AGREE TO A JOINT ANNOUNCEMENT. HOWEVER EVEN IF THEY DO WE SHALL NEED FOR INTERNAL POLITICAL REASONS IN NORTHERN IRELAND TO ISSUE A RATHER MORE DETAILED STATEMENT THERE ABOUT THE COURSE OF THE NEGOTIATIONS AND THE REASONS FOR THEIR FAILURE. WHAT WE HAVE IN MIND IS THAT AFTER A SUITABLE INTERVAL A PRESS NOTICE WILL ISSUE CONTAINING A STATEMENT ATTRIBUTED TO MR BUTLER, WHO WILL THEN BE AVAILABLE FOR INTERVIEW OR QUESTIONING BY THE MEDIA. THE TEXT OF THE PROPOSED PRESS BRIEFING IS BEING SENT TO YOU BY BAG AND SHOULD REACH YOU BEFORE YOUR APPOINTMENT ON 21 AUGUST. YOU SHOULD NOT SHOW IT TO THE IRISH, BUT IT WOULD BE COURTEOUS TO INDICATE TO THEM THAT

A) FOLLOWING THE JOINT ANNOUNCEMENT IT WILL BE NECESSARY FOR MR BUTLER TO INDICATE TO THE PUBLIC IN NORTHERN IRELAND HOW THE FUTURE OF THE GAS INDUSTRY WILL BE HANDLED, AND ALSO TO DRAW A LINE FOR THEM UNDER THE GAS PROJECT IN NORTHERN IRELAND. WE ARE CONSCIOUS OF THE NEED TO DO THIS IN WAYS WHICH WILL NOT CAUSE FURTHER PROBLEMS FOR THE IRISH GOVERNMENT.

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B) DEPARTMENT OF ECONOMIC DEVELOPMENT OFFICIALS WILL NEED AT A LATER STAGE TO CLEAR UP ANY OUTSTANDING DETAILS WITH THEIR OPPOSITE NUMBERS IN DUBLIN (MY TEL NO 164, PARA 4).

4. IF THE IRISH DO NOT AGREE TO A JOINT ANNOUNCEMENT WE SHALL WISH TO RECONSIDER THE FORM IN WHICH WE WOULD MAKE THE ANNOUNCEMENT UNILATERALLY, BUT THE SUBSTANCE WILL NOT DIFFER GREATLY FROM THE TEXTS WHICH WE HAVE SENT TO YOU.

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10 DOWNING STREET

From the Private Secretary

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16 August 1984

KINSALE GAS

Thank you for your letter of 15 August. I am grateful also for Stuart Eldon's letter of the same date.

I have consulted the Prime Minister about the timing of her reply to Dr. FitzGerald. She agrees that, subject to any intervening developments, this should issue on Monday, 20 August.

I should be grateful if Stuart Eldon could arrange accordingly.

I am sending copies of this letter to Stuart Eldon (Baroness Young's Office, FCO), to the Private Secretaries to the members of E(A) and to Richard Hatfield (Cabinet Office).

(DAVID BARCLAY)

N.D. Ward, Esq.,
Northern Ireland Office.

JS

PRIME MINISTER

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KINSALE GAS

WE HAVE NOW RECEIVED FCO AND NIO ADVICE ON THE TIMING OF YOUR
REPLY TO DR FITZGERALD.

MR PRIOR'S VIEW, WITH WHICH OUR AMBASSADOR AGREES, IS THAT
THE REPLY SHOULD NOT BE LONG DELAYED. IN ORDER TO ALLOW A
LITTLE TIME FOR THE PRESENT ANGLO-IRISH DIFFICULTIES TO SUBSIDE,
5-THEY SUGGEST MONDAY 20 AUGUST - BUT NO LATER.

CONTENT FOR YOUR REPLY TO ISSUE ON THAT DAYN SUBJECT TO ANY
INTERVENING DEVELOPMENTS?

DAVID BARCLAY
15 AUGUST 1938

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From: THE PRIVATE SECRETARY



28/8/84
NORTHERN IRELAND OFFICE

WHITEHALL

LONDON SW1A 2AZ

Timothy Flesher Esq
Private Secretary
10 Downing Street
SW1

15th August 1984

Dear Tim,

KINSALE GAS *attached*

Your letter of 14 August conveyed the Prime Minister's agreement to the draft message to Dr FitzGerald, subject to some minor amendments and sought advice on when the reply should be sent bearing in mind current influences on Anglo/Irish relations.

As Mr Prior indicated before Sunday's events there is everything to be said for an early reply. There are already signs that Dublin may be misreading our likely response. Delay of more than a few days runs the risk that the Irish will be encouraged to think their tactics have succeeded and that we are searching afresh for some way of proceeding with the project. If this gained ground the eventual delivery of our message would cause added difficulty.

It is also essential that this piece of business should be concluded before Mr Prior meets Mr Barry on 31 August and to ensure that there is no residue for the Prime Minister's meeting with Dr FitzGerald on 3 September.

Our judgement therefore is that a reply should be given no later than Monday 20 August and if the remainder of the week is quiescent Friday 17 August should not be ruled out. The Foreign and Commonwealth Office, having consulted the Ambassador, agree this advice.

I am sending copies to the Private Secretaries to Members of E(A), to Colin Budd (Foreign and Commonwealth Office), Stuart Eldon (Baroness Young's Office FCO) and Richard Hatfield (Cabinet Office).

Yours Sincerely
Neil Ward.

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Foreign and Commonwealth Office

London SW1A 2AH

15 August 1984

Dear Tim

KINSALE GAS

You sent me a copy of your letter of 14 August to Graham Sandiford about the Prime Minister's reply to Dr Fitzgerald's message on Kinsale Gas.

It seems desirable to us, and to HM Ambassador in Dublin, that the Prime Minister's reply should be handed over not later than Monday 20 August in order to put an end to the current uncertainty about the project. This would meet the Prime Minister's wish that we should not give such an unpalatable message when tempers are inflamed by last Sunday's events in Belfast, while leaving a reasonable interval before the two leaders meet on 3 September. The necessary arrangements have been made to do this once we know that you are content.

I am sending copies of this letter to Graham Sandiford, the other Private Secretaries to members of E(A) and to Richard Hatfield (Cabinet Office).

yours ever

Stanley Eldon

S G Eldon
PS/Lady Young

Tim Flesher Esq
10 Downing Street
Whitehall

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Foreign and Commonwealth Office

LONDON SW1A 2AA



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PP DUBLIN
GRS 530
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FM FCO 151300Z AUG 44
TO PRIORITY DUBLIN
TELEGRAM NUMBER 163 OF 15 AUGUST
MY TEL NO 161
KINSALE GAS.

1. THE FINAL PARAGRAPH OF THE PRIME MINISTER'S MESSAGE TO THE TAOISEACH INDICATES THAT YOU WILL BE INSTRUCTED TO SEEK IMMEDIATE DISCUSSIONS WITH IRISH OFFICIALS AS TO THE BEST WAY OF ANNOUNCING THE END OF THE PROJECT.

2. HMG'S OVERALL OBJECTIVE IS TO MINIMISE ANY DAMAGE TO THE WIDER ANGLO/IRISH RELATIONSHIP BY DEMONSTRATING, BOTH TO THE IRISH AUTHORITIES AND TO THE PUBLIC, THAT THE DECISION HAS BEEN FORCED ON US BY ECONOMIC FACTORS ALONE, AND THAT IT DOES NOT IN ANY WAY DIMINISH OUR DESIRE FOR PROGRESS ON THE WIDE RANGE OF OTHER BUSINESS BETWEEN OUR TWO GOVERNMENTS.

3. IDEALLY WE WOULD LIKE THE IRISH TO JOIN US IN THE DECISION NOT TO PROCEED. BUT IT SEEMS VERY UNLIKELY THAT THEY WOULD BE WILLING PUBLICLY TO DO SO. WE EXPECT THEM TO INSIST THAT THE UK ALONE IS RESPONSIBLE FOR THE PROJECT'S COLLAPSE. APART FROM ANYTHING ELSE, IT HAS A BEARING ON THE CAPITAL CONTRIBUTION (SEE MY TEL NO 164). HOWEVER WE HOPE THAT THEY WOULD BE PREPARED TO SUBSCRIBE TO A JOINT STATEMENT, WHICH WOULD DEMONSTRATE PUBLICLY THE DESIRE OF BOTH GOVERNMENTS TO LIMIT THE IMPACT UPON ANGLO/IRISH RELATIONS OF OUR WITHDRAWAL FROM THE PROJECT. IT SHOULD NOT ONLY DRAW A LINE UNDER THE KINSALE PROJECT BUT RE-AFFIRM THE INTENTION TO PURSUE ECONOMIC CO-OPERATION.

4. IN SPEAKING TO DONLON OR LILLIS YOU SHOULD THEREFORE FIRST PROPOSE TO THEM THAT THE MOST SATISFACTORY WAY OF PUTTING AN END TO THE PRESENT UNCERTAINTY AND ACRIMONY WOULD BE A FORMAL JOINT ANNOUNCEMENT WHICH WOULD:-

(A) ACKNOWLEDGE THAT THE GAS PROJECT CANNOT PROCEED AND, AS FAR AS IT IS POSSIBLE TO DO SO, RECOGNISE THE REASONS WHY NOT: AND

IT THE LEVEL OF SUBSIDY THAT WOULD BE NEEDED:

- C) THESE ARE GENUINE ECONOMIC CONSIDERATIONS: AND THEY HAVE COME TO A HEAD ONLY AFTER THE MOU WAS SIGNED.
 - D) IN THE MATURING RELATIONSHIP BETWEEN THE TWO COUNTRIES, IT IS IMPORTANT THAT WE SHOULD BE WILLING TO FACE UP TO THESE ECONOMIC REALITIES. FOR THE TWO GOVERNMENTS TO HAVE PRETENDED THAT THE PROJECT WAS STILL VIABLE WHEN ALL OUR CALCUALTIONS SHOW THAT IT IS NOT SO WOULD ONLY HAVE STORED UP TROUBLE FOR BOTH GOVERNMENTS IN FUTURE. APART FROM ALL OTHER CONSIDERATIONS WE WOULD NOT WISH TO BURDEN FUTURE ANGLO-IRISH RELATIONS WITH A PROBLEM OF THIS SORT.
3. THE IRISH RESPONSE TO MANY OF THESE POINTS HAS BEEN MADE PLAIN IN DR FITZGERALD'S TWO MESSAGES: AND IN MR SPRING'S PRESS CONFERENCE ON 8 AUGUST. YOU MAY, IN RESPONSE TO IRISH COMMENT, NEED TO DRAW ON THE FOLLOWING POINTS:
- I) WHILST THE PROVISION IN THE MOU FOR OUR CALLING ON LOWER QUANTITIES OF GAS WOULD HAVE THE EFFECT OF REDUCING OUR LOSSES SLIGHTLY WERE THE PROJECT TO FAIL DISASTROUSLY AFTER THE SIGNING OF AN AGREEMENT, THERE WAS NEVER ANY SUGGESTION THAT A PROJECT HANDLING ONLY THESE VOLUMES OF GAS COULD BE FINANCIALLY VIABLE. IF THESE HAD BEEN THE PROJECTED SALES LEVELS WE WOULD NOT HAVE REACHED EVEN THE MOU STAGE:
 - II) WHIEE THE MOU PROVIDES FOR POSSIBLE RENEGOTIATION OF GAS PRICES, THE GAS PRICE FORMULA CAN ONLY BE CHANGED BY AGREEMENT BETWEEN BOTH GOVERNMENTS. IT WOULD BE UNREALISTIC TO EXPECT AGREEMENT TO A RENEGOTIATION ON THE SCALE THAT WE THINK WILL BE NEEDED IN 5 YEARS TIME IF THE IRISH ARE NOT WILLING TO CONTEMPLATE SUCH A RENEGOTIATION NOW:
 - III) THE IRISH HAVE ARGUED THAT THE ECONOMIC PROSPECTS OF THE PROJECT CANNOT POSSIBLY HAVE CHANGED SO SIGNIFICANTLY SINCE LAST AUTUMN: UNFORTUNATELY, THE IRISH ARE WRONG AND THE SHARP INCREASES IN HEAVY FUEL OIL PRICES IN THE LAST NINE MONTHS TOGETHER WITH THE LARGE DETERIORATION IN THE STERLING/DOLLAR EXCHANGE RATE HAVE ALREADY PRODUCED A GAS PRICE WHICH IS FAR IN EXCESS OF ANYTHING THAT WE

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(B) ISOLATE, AND LEAVE BEHIND, ANY DISAPPOINTMENT ABOUT CANCELLATION OF THE GAS PROJECT, MAKING CLEAR THAT THE FAILURE WILL NOT OBSTRUCT PROGRESS ON THE WIDE RANGE OF OTHER BUSINESS BETWEEN OUR TWO GOVERNMENTS.

5. IF THE IRISH ARE DISPOSED IN PRINCIPLE TO AGREE TO THIS YOU SHOULD SAY THAT WE SEE IT AS CONTAINING THE FOLLOWING POINTS:

(A) DISAPPOINTMENT THAT THE PROJECT COULD NOT PROCEED AFTER ALL THE EFFORT THAT WENT INTO IT FROM BOTH SIDES:

(B) RECOGNITION THAT BOTH SIDES HAVE ACTED REASONABLY AND IN GOOD FAITH: LEADING TO

(C) SOME DESCRIPTION OF THE FINAL POSITIONS OF BOTH SIDES TO THE DEAL. THE UK ENCOUNTERED ADVERSE FACTORS AS TO PRICE AND DEMAND WHICH IN ITS VIEW MADE THE PROJECT NON-VIABLE. THE REPUBLIC COULD NOT, AND DID NOT, DEPART FROM THE ECONOMIC CRITERION IT HAS SET ITSELF THAT THE PRICE OF THE GAS HAD TO RELATE TO THE PRICE OF REPLACEMENT FUEL TO THEM.

(D) AN AFFIRMATION THAT DISAPPOINTMENT OVER KINSALE WILL NOT HAVE ADVERSE REPERCUSSIONS ON OTHER MUTUALLY BENEFICIAL PROJECTS INCLUDING FUTURE COOPERATION IN ENERGY MATTERS.

6. A FULL DRAFT TEXT WILL BE TELEGRAPHED TO YOU SHORTLY. AS WE BELIEVE THAT AN EARLY PUBLIC ANNOUNCEMENT IS REQUIRED, WE HOPE IT WILL BE POSSIBLE TO AGREE A JOINT TEXT WITHOUT PROTRACTED DISCUSSIONS. YOU SHOULD MAKE IT PLAIN THAT IF THE IRISH DO NOT WISH TO SUBSCRIBE TO A JOINT STATEMENT WE SHALL MAKE A UNILATERAL ANNOUNCEMENT ON THE LINES OF PARA 5 ABOVE IN THE VERY NEAR FUTURE

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GRS 1301

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FM FCO 151700Z AUG 84

TO PRIORITY DUBLIN

TELEGRAM NUMBER 162 OF 15 AUGUST

MY TELNO 160

KINSALE GAS

1. DR FITZGERALD'S MESSAGE TO THE PRIME MINISTER MEANS THAT THE KINSALE GAS PROJECT WILL NOW HAVE TO BE CANCELLED. THE PRIME MINISTER'S REPLY TO DR FITZGERALD, DRAWING THIS CONCLUSION, IS IN MY IMMEDIATELY PRECEDING TEL. 160.

2. THE DISCUSSION BETWEEN THE TWO GOVERNMENTS ON KINSALE GAS HAS BEEN COMPARATIVELY TERSE: WE ARE ACUTELY CONSCIOUS OF THE DANGER THAT THE IRISH GOVERNMENT WILL ALLOW THEMSELVES TO ASSUME THAT OUR UNWILLINGNESS TO GO AHEAD WITH THE GAS PROJECT SIGNALS SOME LESSENING OF OUR GENERAL INTEREST IN IMPROVING ANGLO-IRISH RELATIONS. IT IS IMPORTANT THAT THE IRISH SHOULD NOT BE ALLOWED TO DRAW THIS CONCLUSION, AND YOU SHOULD THEREFORE MAKE THE FOLLOWING POINTS TO THE IRISH AT A VERY SENIOR LEVEL:

- A) WE ARE RELUCTANT AND UNHAPPY TO HAVE TO BRING THE KINSALE GAS PROJECT TO AN END. WE APPRECIATE THE STRENGTH OF THE POLITICAL CONSIDERATIONS POINTING IN FAVOUR OF CONTINUING WITH THE PROJECT IF AT ALL POSSIBLE - THOUGH THERE ARE ALSO CONTRARY POLITICAL ARGUMENTS:
- B) WE HAVE BEEN FORCED TO CANCEL THE PROJECT SOLELY BECAUSE ECONOMIC CONSIDERATIONS NOW WEIGH SO STRONGLY AGAINST IT. THE 15P PER THERM PRICE GAP QUOTED IN THE PRIME MINISTER'S LETTER OF 31 JULY DEMONSTRATES JUST HOW LARGE THE GAP BETWEEN THIS PROJECT AND ECONOMIC VIABILITY HAS BECOME. IT IS AN ENORMOUS GAP, AND WE CAN UNDERSTAND WHY THE IRISH ARE UNABLE TO OFFER TO FILL IT. BUT PRECISELY BECAUSE IT IS SUCH AN ENORMOUS GAP IT IS UNREALISTIC FOR US ALONE TO FILL IT. THE OVERWHELMING ECONOMIC REALITY IS THAT THE PROJECT IS UNECONOMIC AND THAT NEITHER COUNTRY CAN AFFORD TO GIVE

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CONTEMPLATED LAST WINTER:

- IV) THE IRISH MAY ARGUE THAT WE HAVE ALWAYS SOUGHT AN ARTIFICIALLY HIGH RATE OF RETURN ON THE PROJECT. IN FACT THE REVERSE IS TRUE - IN CALCULATING OUR RATE OF RETURN WE TOOK ON TRUST THE AVAILABILITY OF GAS OVER THE LIFE OF THE FIXED ASSETS (32 YEARS) ALTHOUGH THE CONTRACT WOULD HAVE RUN FOR ONLY ABOUT 20 YEARS. IF WE HAD CONFINED OUR CALCULATIONS TO THE 20 YEAR PERIOD THERE WOULD NEVER HAVE BEEN ANY PROSPECT OF ECONOMIC VIABILITY.
- V) THE IRISH HAVE IN THE PAST ASSERTED THAT WE SHOULD COUNT AGAINST THE PROJECT THE PDS STG 140M OR SO THAT WOULD BE INVOLVED IF WE HAD TO WIND UP THE EXISTING TOWN GAS INDUSTRY IN NORTHERN IRELAND - ON THE GROUNDS THAT WE FACED EXPENDITURE ON THIS LEVEL ANYWAY AND SHOULD NOT THEREFORE ALLOW IT TO INFLUENCE OUR CALCULATION OF THE RATE OF RETURN. IF THIS IS RAISED AGAIN, YOU SHOULD POINT OUT THAT THE CALCULATION OF THE RATE OF RETURN MUST BY DEFINITION BE A RATE OF RETURN ON THE EXPENDITURE ACTUALLY INVOLVED: TO EXCLUDE PART OF THE EXPENDITURE FALSIFIES THE CALCULATION. THE SAVING OF EXPENDITURE ON CLOSING THE GAS INDUSTRY IS RELEVANT NOT TO THE CALCULATION OF THE RATE OF RETURN BUT TO THE CALCULATION OF HOW MUCH PUBLIC EXPENDITURE IS REQUIRED. OUR CALCULATIONS OF THE LATTER AT THE GAS PRICES NOW PROJECTED SHOW THAT AFTER DEDUCTING THE SAVING ON CLOSING THE EXISTING GAS INDUSTRY THE KINSALE GAS PROJECT WOULD HAVE CREATED AN ADDITIONAL BURDEN ON PUBLIC EXPENDITURE RUNNING INTO SEVERAL HUNDREDS OF MILLIONS OF POUNDS, INCLUDING THAT ARISING FROM ITS ADVERSE EFFECT ON THE ELECTRICITY INDUSTRY.
- VI) THE IRISH HAVE CHOSEN TO PRESENT THE PRIME MINISTER'S LETTER OF 31 JULY AS REQUIRING A PRICE CUT OF SOME 50 PERCENT, THAT LETTER WAS IN FACT VERY CAREFUL TO SAY THAT THIS SIZE OF PRICE CUT WAS THE SIZE OF THE GAP BETWEEN THE PROJECT AND ECONOMIC VIABILITY: THE PRIME MINISTER'S PENULTIMATE PARAGRAPH SPECIFICALLY RAISED THE POSSIBILITY OF THE IRISH GOING ONLY 'A VERY SUBSTANTIAL WAY TOWARDS BRIDGING THE

GAP'. WE CAN UNDERSTAND WHY THE IRISH FELT IT WAS TOO MUCH OF A BURDEN TO MAKE SUCH A 'VERY SUBSTANTIAL' RESPONSE, BUT THEY ARE MISREPRESENTING OUR POSITION IF THEY CONTINUE TO CLAIM THAT OUR POSITION WAS SIMPLY TO DEMAND A 50 PERCENT PRICE CUT: THIS MISREPRESENTATION IS UNDOUBTEDLY POLITICALLY HELPFUL TO IRISH MINISTERS, BUT IT DOES NOT HELP ANGLO-IRISH RELATIONS:

- VII) IN ANSWER TO THE COMMENT OF MR ALBERT REYNOLDS (FIANNA FAIL) THAT THE BRITISH GOVERNMENT HAS A PRACTICE OF BREAKING AGREEMENTS WITH THE IRISH: YOU SHOULD POINT OUT THAT THE PRESENT IRISH GOVERNMENT THEMSELVES SOUGHT RENEGOTIATION OF THE DEAL WHICH WE BELIEVED WE HAD AGREED WITH MR REYNOLDS IN MAY 1982. THE IRISH APPARENTLY FOUND THE DEAL ORIGINALLY AGREED TO BE ECONOMICALLY UNACCEPTABLE AND SUBSEQUENTLY SOUGHT MAJOR CHANGES IN THE WAY THE PRICE OF GAS IS CALCULATED:
- VIII) EARLIER IN THE SUMMER THE IRISH MADE SOMETHING OF THE ARGUMENT THAT WE WERE MORALLY BOUND BY THE MOU, THEY CLEARLY ACCEPT NOW THAT WE WERE NOT LEGALLY BOUND BY IT. WE DO, HOWEVER, ACCEPT THAT THE MEMORANDUM MARKED A REAL EXPECTATION BY BOTH GOVERNMENTS THAT A FIRM AGREEMENT WOULD BE SIGNED. WE ARE SORRY THAT CHANGES IN ECONOMIC CIRCUMSTANCES HAVE COMPELLED A DIFFERENT CONCLUSION:
- IX) DR FITZGERALD DREW ATTENTION TO POSSIBLE (NATIONALIST) DISMAY IN NORTHERN IRELAND IF THE PROJECT IS CANCELLED. BUT THERE WILL BE A MUCH STRONGER (UNIONIST) REACTION IF WE GO AHEAD WITH A PROJECT THAT IS PATENTLY UNECONOMIC. UNIONISTS WILL CLAIM THAT IF HMG PRESSES ON WITH A PROJECT THAT NO LONGER HAS ECONOMIC VALIDITY, THEN THE MOTIVE FOR PRESSING ON MUST BE POLITICAL: THE POLITICAL MOTIVE WOULD BE SEEN AS VERY STRONG (AND IN THEIR EYES VERY SINISTER) IF IT JUSTIFIED EXPENDITURE OF SEVERAL HUNDREDS OF PDS STG M.

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PS/PUS

MR DEREK THOMAS
SIR W HARDING
MR GOODALL
MR BARRINGTON
MR O'NEILL
MR JENKINS
MR D C THOMAS
BUCKINGHAM PALACE

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Subject cc master
of 1

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Seen at 1450 on 16/8/84.
Told FCO to ensure that
reply does not issue before
Monday 20 August.

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39162 - 1

Sub
16/8

PP DUBLIN

GRS 530

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FM FCO 151015Z AUG 84

TO PRIORITY DUBLIN

TELEGRAM NUMBER 161 OF 15 AUGUST

MIPT

KINSALE GAS.

1. FOLLOWING IS TEXT OF MESSAGE FROM THE PM TO THE TAOISEACH.
AS MRS THATCHER IS AWAY UNTIL 28 AUGUST WE DO NOT PROPOSE TO SEND
A SIGNED LETTER.

BEGINS

THANK YOU FOR YOUR LETTER OF 8 AUGUST. I AM SORRY THAT YOU HAVE
BEEN UNABLE TO OFFER ANY SUGGESTIONS THAT MIGHT ENABLE US BOTH TO
CONTINUE WITH THE KINSALE GAS PROJECT. IN MY LETTER OF 31 JULY
I EXPRESSED MY DISAPPOINTMENT THAT CHANGES IN ECONOMIC CIRCUM-
STANCES HAD PUT THE PROJECT AT RISK. HOWEVER, I FULLY ACCEPT
THAT PRICE CHANGES OF THE ORDER REQUIRED TO SAVE THE PROJECT WOULD
BE VERY DIFFICULT FROM YOUR POINT OF VIEW. I HOPE THAT YOU IN
YOUR TURN WILL UNDERSTAND THAT THE BURDEN WE IN THE UNITED KINGDOM
WOULD FACE IF WE WENT AHEAD ON THE BASIS OF THE EXISTING FORMULA
WOULD BE AT LEAST AS HEAVY, AND WE ARE NOT PREPARED TO BEAR IT
ALONE.

IN CASE THERE SHOULD BE ANY MISUNDERSTANDING I WOULD MAKE CLEAR
THAT WHILE I DREW ATTENTION IN MY LETTER TO THE EXTENT OF THE
DETERIORATION IN THE ECONOMIC PROSPECTS FOR THE PROJECT, I DID NOT
SUGGEST A PRICE REDUCTION OF ALMOST HALF. THE FACT IS THAT OUR
CALCULATIONS SHOWED THAT A REDUCTION OF THIS MAGNITUDE WOULD BE
NEEDED FOR THE PROJECT TO YIELD THE SAME RETURN AS ORIGINALLY
ENVISAGED AT THE TIME THE MOU WAS SIGNED: IN MY LETTER I SOUGHT
AN INDICATION AS TO WHETHER YOU AND YOUR COLLEAGUES WERE ABLE TO
GO A VERY SUBSTANTIAL WAY TOWARDS BRIDGING THE GAP.

IT WAS ALWAYS CENTRAL TO THE PROJECT THAT ANY DEAL MUST BE TO THE
ECONOMIC ADVANTAGE OF BOTH SIDES. THIS VIEW WAS REPEATED ON
SEVERAL OCCASIONS BY MINISTERS AND WAS REGARDED AS SUFFICIENTLY

1

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PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T145/84

CONFIDENTIAL

39162 - 1

IMPORTANT TO BE INCLUDED IN THE PREAMBLE TO THE MEMORANDUM OF UNDERSTANDING. IN THE LIGHT OF THAT, YOU WILL APPRECIATE THAT YOUR DECISION EFFECTIVELY MEANS THAT THE PROJECT CANNOT PROCEED.

YOU ARE RIGHT TO POINT OUT THAT THERE WILL BE DEEP DISAPPOINTMENT IN NORTHERN IRELAND THAT THE GAS INDUSTRY IS NOT TO BE PRESERVED BY IMPORTING NATURAL GAS: BUT I THINK THERE WOULD HAVE BEEN EVEN MORE WIDESPREAD DISMAY IF THE UNITED KINGDOM GOVERNMENT HAD DECIDED TO PROCEED WITH THE PROJECT IN THE KNOWLEDGE THAT FROM ITS OUTSET IT WAS UNECONOMIC. APART FROM THE CRITICISM THAT WOULD JUSTLY BE MADE OF SUCH AN ECONOMIC POLICY, YOU AND I WOULD BOTH HAVE TO FACE THE POLITICAL DIFFICULTIES CREATED BY THE INEVITABLE WIDESPREAD SUSPICION THAT ECONOMIC CONSIDERATIONS WERE BEING OVERRIDEN, AT CONSIDERABLE COST, BY OTHER FACTORS. THESE COULD EASILY HAVE LED TO OTHER MISUNDERSTANDINGS IN THE FUTURE. THE TANAISTE'S PRESS CONFERENCE ON 8 AUGUST HAS AROUSED CONSIDERABLE PRESS SPECULATION ON THE FUTURE OF THE PROJECT AND ON THE IMPLICATIONS FOR ANGLO-IRISH RELATIONS. THAT THE PROJECT CANNOT PROCEED SHOULD THEREFORE BE ANNOUNCED FAIRLY SOON. I AM ASKING OUR AMBASSADOR IN DUBLIN TO SEEK IMMEDIATE DISCUSSIONS WITH YOUR OFFICIALS AS TO THE BEST WAY OF DOING THIS. ON OUR SIDE WE SHALL WISH TO CONTINUE TO LAY THE STRONGEST EMPHASIS ON THE FACT THAT THIS IS A DECISION FORCED UPON US BOTH BY ECONOMIC REALITIES AND THAT IT DOES NOT IN ANY WAY DIMINISH OUR DESIRE FOR CONTINUED PROGRESS ON THE WIDE RANGE OF OTHER BUSINESS BETWEEN OUR TWO GOVERNMENTS.

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10 DOWNING STREET

From the Private Secretary

14 August 1984

The Prime Minister has now had a chance to consider David Coleman's letter of 10 August and the draft reply to Dr. Garret FitzGerald which was enclosed. Mrs. Thatcher has agreed to the draft subject to a number of relatively minor amendments and I attach the final version. On timing, however, the Prime Minister considers that it is an unpropitious moment in Anglo-Irish relations to send the message and she would prefer to wait until the present furore has died down. Nevertheless she understands the argument for an early reply and I should be grateful therefore if, together with the Foreign and Commonwealth Office, you could consider when the reply should be sent and provide advice on that point. Since the Prime Minister is away until 28 August the reply will need to be transmitted in the form of a message rather than a letter and I should be grateful if Stuart Eldon to whom I am copying this letter could make the necessary arrangements.

I am sending copies of this letter to the Private Secretaries to members of E(A), to Colin Budd (Foreign and Commonwealth Office), Stuart Eldon (Baroness Young's Office, FCO) and Richard Hatfield (Cabinet Office).

Timothy Flesher

Graham Sandiford, Esq.,
Northern Ireland Office.

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SLH

JAAES

MESSAGE FROM THE PRIME MINISTER TO DR. FITZGERALD

Thank you for your letter of 8 August. I am sorry that you have been unable to offer any suggestions that might enable us both to continue with the Kinsale Gas project. In my letter of 31 July I expressed my disappointment that changes in economic circumstances had put the project at risk. However, I fully accept that price changes of the order required to save the project would be very difficult from your point of view. I hope that you in your turn will understand that the burden we in the United Kingdom would face if we went ahead on the basis of the existing formula would be at least as heavy, and we are not prepared to bear it alone.

In case there should be any misunderstanding I would make clear that while I drew attention in my letter to the extent of the deterioration in the economic prospects for the project, I did not suggest a price reduction of almost half. The fact is that our calculations showed that a reduction of this magnitude would be needed for the project to yield the same return as originally envisaged at the time the MOU was signed; in my letter I sought an indication as to whether you and your colleagues were able to go a very substantial way towards bridging the gap.

It was always central to the project that any deal must be to the economic advantage of both sides. This view was repeated on several occasions by Ministers and was regarded as sufficiently important to be included in the preamble to the Memorandum of Understanding. In the light of that, you will appreciate that your decision effectively means that the project cannot proceed.

You are right to point out that there will be deep disappointment in Northern Ireland that the gas industry is

not to be preserved by importing natural gas; but I think there would have been even more widespread dismay if the United Kingdom Government had decided to proceed with the project in the knowledge that from its outset it was uneconomic. Apart from the criticism that would justly be made of such an economic policy, you and I would both have to face the political difficulties created by the inevitable widespread suspicion that economic considerations were being overridden, at considerable cost, by other factors. These could easily have led to other misunderstandings in the future.

The Tanaiste's press conference on 8 August has aroused considerable press speculation on the future of the project and on the implications for Anglo-Irish relations. That the project cannot proceed should therefore be announced fairly soon. I am asking our Ambassador in Dublin to seek immediate discussions with your officials as to the best way of doing this. On our side we shall wish to continue to lay the strongest emphasis on the fact that this is a decision forced upon us both by economic realities, and that it does not in any way diminish our desire for continued progress on the wide range of other business between our two governments.

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CCNO



Treasury Chambers, Parliament Street, SW1P 3AG

Tim Flesher Esq
10 Downing Street
LONDON SW1

14 August 1984

Dear Tim,

KINSALE GAS

This is to confirm that the Minister of State is content with the draft letter for the Prime Minister to send to Dr Garrett Fitzgerald enclosed in David Coleman's letter to you of 10 August.

I am copying this to recipients of David Coleman's letter.

Yours sincerely,

Debbie McCambridge

P.P. M E CORCORAN
Private Secretary

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**The following
image type has
poor quality
text due to the
nature of the
material.**

**Image quality is
best available.**

MLAEE

MESSAGE TO THE PRIME MINISTER

FROM TIM FLESHER

C O N F I D E N T I A L

KINSALE GAS:

EVERYONE NOW AGREES THAT FOLLOWING DR FITZGERALD'S MESSAGE WHICH YOU SAW LAST WEEK THERE IS NO OPTION BUT TO CANCEL THE PROJECT. THE ADVICE IS THAT YOU SHOULD REPLY TO DR FITZGERALD AS SOON AS POSSIBLE CONFIRMING THIS. THIS WILL COME AS NO SURPRISE TO THE IRISH SINCE MR SPRING GAVE A PRESS CONFERENCE LAST WEEK WHICH WAS CLEARLY BASED ON THE ASSUMPTION THAT THE PROJECT WOULD BE CANCELLED.

2. NIO ALSO ADVISES THAT YOU SHOULD TAKE THE OPPORTUNITY OF YOUR REPLY TO SET THE RECORD STRAIGHT ABOUT DR FITZGERALD'S CLAIM IN HIS MESSAGE THAT WE HAD SUGGESTED A PRICE REDUCTION OF 50%.

3. AS SOON AS YOUR REPLY IS DELIVERED TO THE IRISH GOVERNMENT NIO AND THE FCO ADVISE HMHUT THE AMBASSADOR IN DUBLIN SHOULD SEEK DISCUSSIONS WITH THE IRISH ON THE BEST WAY OF MAKING THE ANNOUNCEMENT. FOLLOWING IS THE TEXT OF DR FITZGERALD'S MESSAGE FOR REFERENCE:

"THANK YOU FOR YOUR LETTER OF 31 JULY, IN CONNECTION WITH THE SUPPLY OF KINSALE GAS TO NORTHERN IRELAND. MY GOVERNMENT HAVE CONSIDERED YOUR ARGUMENTS CAREFULLY AND I MUST SAY TO YOU THAT WE DO NOT FIND IN THEM GROUNDS FOR CHANGING THE TERMS OF WHAT WAS AGREED BETWEEN OUR MINISTERS. I REGRET VERY MUCH THAT YOUR GOVERNMENT ARE NOW PROPOSING TO ABANDON THE PROJECT DESPITE THE INTENTION TO IMPLEMENT IT FULLY WHICH WAS RECORDED IN THE MEMORANDUM OF UNDERSTANDING CONCLUDED BY BOTH GOVERNMENTS. WE WELCOMED THIS ACHIEVEMENT IN OUR JOINT COMMUNIQUE ON 7 NOVEMBER 1983.

"THE TERMS OF THE UNDERSTANDING WERE DRAWN UP IN SUCH A WAY AS TO BE FAIR TO BOTH PARTIES AND TOOK FULL ACCOUNT OF UNCERTAINTIES ABOUT FUTURE ENERGY PRICES EXCHANGE RATES AND DEMAND.

"YOU HAVE SUGGESTED A PRICE REDUCTION OF ALMOST HALF AS BEING NECESSARY TO ENSURE A VIABLE PROJECT. THIS WOULD INVOLVE SUPPLYING THE GAS AT A PRICE SO FAR BELOW ITS ECONOMIC VALUE AS TO BE UTTERLY UNREASONABLE.

"I SHARE YOUR ANXIETY TO MAKE SURE THAT A SETBACK ON THIS MATTER DOES NOT DAMAGE OUR ABILITY TO MAKE PROGRESS ON OTHER BUSINESS. I WOULD, HOWEVER, BE CONCERNED THAT THE PERCEPTION, PARTICULARLY IN NORTHERN IRELAND, OF A FAILURE BY YOUR GOVERNMENT TO IMPLEMENT THIS IMPORTANT ANGLO-IRISH AGREEMENT WOULD BE VERY NEGATIVE.

"I REMAIN CONVINCED THAT A POSITIVE APPROACH TOWARD IMPLEMENTING THE PROJECT WOULD BE SUCCESSFUL AND ACCORDINGLY MY GOVERNMENT WISHES TO PROCEED AS WAS AGREED."

4. FOLLOWING IS THE DRAFT MESSAGE TO DR FITZGERALD:

"THANK YOU FOR YOUR LETTER OF 8 AUGUST. I AM SORRY THAT YOU HAVE BEEN UNABLE TO OFFER ANY SUGGESTIONS THAT MIGHT ENABLE US BOTH TO CONTINUE WITH THE KINSALE GAS PROJECT. IN MY LETTER OF 31 JULY I EXPRESSED MY DISAPPOINTMENT THAT CHANGES IN ECONOMIC CIRCUMSTANCES HAD PUT THE PROJECT AT RISK. HOWEVER, I FULLY ACCEPT THAT PRICE CHANGES OF THE ORDER REQUIRED TO SAVE THE PROJECT WOULD BE VERY DIFFICULT FROM YOUR POINT OF VIEW. I HOPE THAT YOU IN YOUR TURN WILL UNDERSTAND THAT THE BURDEN WE IN THE UNITED KINGDOM WOULD FACE IF WE WENT AHEAD ON THE BASIS OF THE EXISTING FORMULA WOULD BE AT LEAST AS HEAVY, AND WE ARE NOT PREPARED TO BEAR IT ALONE.

"IN CASE THERE SHOULD BE ANY MISUNDERSTANDING I WOULD MAKE CLEAR THAT WHILE I DREW ATTENTION IN MY LETTER TO THE EXTENT OF THE DETERIORATION IN THE ECONOMIC PROSPECTS FOR THE PROJECT, I DID NOT SUGGEST A PRICE REDUCTION OF ALMOST HALF. THE FACT IS THAT OUR CALCULATIONS SHOWED THAT A REDUCTION OF THIS MAGNITUDE WOULD BE NEEDED FOR THE PROJECT TO YIELD THE SAME RETURN AS ORIGINALLY ENVISAGED AT THE TIME THE MOU WAS SIGNED: IN MY LETTER I SOUGHT AN INDICATION AS TO WHETHER YOU AND YOUR COLLEAGUES WERE ABLE TO GO A VERY SUBSTANTIAL WAY TOWARDS BRIDGING THE GAP.

"IT WAS ALWAYS CENTRAL TO THE PROJECT THAT ANY DEAL MUST BE TO THE ECONOMIC ADVANTAGE OF BOTH SIDES. THIS VIEW WAS REPEATED ON SEVERAL OCCASIONS BY MINISTERS AND WAS REGARDED AS SUFFICIENTLY IMPORTANT TO BE INCLUDED IN THE PREAMBLE TO THE MEMORANDUM OF UNDERSTANDING. IN THE LIGHT OF THAT, YOU WILL APPRECIATE THAT YOUR DECISION EFFECTIVELY MEANS THAT THE PROJECT CANNOT PROCEED.

"YOU ARE RIGHT TO POINT OUT THAT THERE WILL BE DEEP DISAPPOINTMENT IN NORTHERN IRELAND THAT THE GAS INDUSTRY IS NOT TO BE PRESERVED BY IMPORTING NATURAL GAS: BUT I THINK THERE WOULD HAVE BEEN EVEN MORE WIDESPREAD DISMAY IF THE UNITED KINGDOM GOVERNMENT HAD DECIDED TO PROCEED WITH THE PROJECT IN THE KNOWLEDGE THAT FROM ITS OUTSET IT WAS UNECONOMIC. APART FROM THE CRITICISM THAT WOULD JUSTLY BE MADE OF SUCH AN ECONOMIC POLICY, YOU AND I WOULD BOTH HAVE TO FACE THE POLITICAL DIFFICULTIES CREATED BY THE INEVITABLE WIDESPREAD SUSPICION THAT ECONOMIC CONSIDERATIONS WERE BEING OVERRIDDEN, AT CONSIDERABLE COST, BY OTHER FACTORS. THESE COULD EASILY HAVE LED TO OTHER MISUNDERSTANDINGS IN THE FUTURE.

"THE TANAISTE'S PRESS CONFERENCE ON 8 AUGUST HAS AROUSED CONSIDERABLE PRESS SPECULATION ON THE FUTURE OF THE PROJECT AND ON THE IMPLICATIONS FOR ANGLO-IRISH RELATIONS. THE FACT THAT THE PROJECT CANNOT PROCEED WILL THEREFORE HAVE TO BE ANNOUNCED VERY SHORTLY, AND I AM ASKING OUR AMBASSADOR IN DUBLIN TO SEEK IMMEDIATE DISCUSSIONS WITH YOUR OFFICIALS AS TO THE BEST WAY OF ARRANGING THIS, WITH A VIEW TO MINIMISING ANY DAMAGE TO OUR CONTINUING RELATIONSHIPS. ON OUR SIDE ~~WE SHALL WISH TO CONTINUE~~ WE SHALL WISH TO CONTINUE TO LAY THE STRONGEST EMPHASIS ON THE FACT THAT THIS IS A DECISION FORCED UPON US BOTH BY ECONOMIC REALITIES, AND THAT IT DOES NOT IN ANY WAY DIMINISH OUR DESIRE FOR CONTINUED PROGRESS ON THE WIDE RANGE OF OTHER BUSINESS BETWEEN OUR TWO GOVERNMENTS."



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NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

Tim Flesher Esq
10 Downing Street
London
SW1

10 August 1984

Dear Mr Flesher,

KINSALE GAS

Your letter of 8 August sought advice on whether, and in what form, any reply should be made to Dr FitzGerald's message of 8 August.

Dr FitzGerald's message indicates clearly that the Irish are unwilling to agree to the significant reduction in the price of gas that we would need to continue with the project on any of the bases discussed by E(A) on 24 July. In these circumstances, my Secretary of State believes there is no option but to cancel the project forthwith. He understands that the Prime Minister takes a similar view.

In the light of the Prime Minister's own letter to him of 31 July, Dr FitzGerald will not be expecting any other decision from us; and Mr Spring, the Tanaiste, would not have held his press conference on 8 August (you will have seen Dublin telegram No 380 containing the text of his prepared statement) unless he too assumed that the project was about to be cancelled.

Mr Prior suggests, therefore, that the Prime Minister should reply to Dr FitzGerald at once to tell him that in the light of his reply the project is being cancelled. Courtesy alone requires that we should tell Dr FitzGerald this; but there are also some points made in Dr FitzGerald's own message of 8 August which require correction. He is, for instance, wrong to claim that the Prime Minister suggested a price reduction of almost half; and since Mr Spring has subsequently made great play in the press of the unreasonableness of the United Kingdom's proposal that the Irish should cut their selling price by almost 50%, Mr Prior thinks it important that the Prime Minister's reply to Dr FitzGerald should seek to set the record straight. The enclosed draft does this.

The draft also picks up Dr FitzGerald's remark (in his penultimate paragraph) about perceptions in Northern Ireland. He is right to point out that some (mainly nationalists) will decry our decision, but should not be allowed to forget that others (mainly unionists) would be even more critical of the government if we were seen to be going ahead for purely political reasons with a project which

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was, on our own admission, manifestly uneconomic.

Mr Prior proposes that a formal announcement about the cancellation of the project should be made very soon after the Prime Minister's reply has been delivered to the Irish Government. He suggests that at the same time as delivering the letter, the Ambassador in Dublin should be instructed to speak to the Irish Government (at the most senior level available) to make it plain that the failure of the project stems solely from the scale of economic difficulty now posed by the project; that the economic unattractiveness of the project results from changes which are, contrary to apparent Irish belief, genuine, severe, and of recent derivation; and above all to emphasise that HMG's commitment to making progress on all other areas of business between the two governments remains as firm as ever. The Ambassador should also seek immediate discussions with Irish Officials about the way of announcing that the project cannot proceed.

On timing, Mr Prior suggests that the Prime Minister should write to Dr FitzGerald as soon as possible. The issue has already been thrown wide open to the public by Mr Spring's press conference on 8 August, and it is essential that the United Kingdom government should announce a firm decision within the next few days. Delay would allow unwelcome room for speculation both in Northern Ireland and within the Irish Government that Dr FitzGerald's letter (or Mr Spring's press conference) was causing us to rethink our attitude. There also seems to be some advantage to Anglo Irish relations in getting this awkward business settled during the holiday period, so that it does not have to be picked up again during September.

This advice has been agreed with the Foreign and Commonwealth Office.

I am copying this letter, and enclosures, to the Private Secretaries of members of E(A), to the Private Secretary to the Foreign and Commonwealth Secretary, and to the Private Secretary to Sir Robert Armstrong.

*yours sincerely,
Aid Coleman*

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DRAFT LETTER

FROM THE PRIME MINISTER TO DR. FITZGERALD

Thank you for your letter of 8 August. I am sorry that you have been unable to offer any suggestions that might enable us both to continue with the Kinsale Gas project. In my letter of 31 July I expressed my disappointment that changes in economic circumstances had put the project at risk. However, I fully accept that price changes of the order required to save the project would be very difficult from your point of view. I hope that you in your turn will understand that the burden we in the United Kingdom would face if we went ahead on the basis of the existing formula would be at least as heavy, and we are not prepared to bear it alone.

In case there should be any misunderstanding I would make clear that while I drew attention in my letter to the extent of the deterioration in the economic prospects for the project, I did not suggest a price reduction of almost half. The fact is that our calculations showed that a reduction of this magnitude would be needed for the project to yield the same return as originally envisaged at the time the MOU was signed; in my letter I sought an indication as to whether you and your colleagues were able to go a very substantial way towards bridging the gap.

It was always central ~~to the discussions on~~ the project that any deal must be to the economic advantage of both sides. This view was repeated on several occasions by Ministers ~~over the years of negotiation~~ and was regarded as sufficiently important to be included in the preamble to the Memorandum of Understanding. In the light of that, you will appreciate that your decision effectively means that the project cannot proceed.

You are right to point out that there will be deep disappointment in Northern Ireland that the gas industry is not to be preserved by importing natural gas; but I think there would have been even more widespread dismay if the United Kingdom Government had decided to proceed with the project in the knowledge that from its outset it was uneconomic. Apart from the criticism that would



justly be made of such an economic policy, you and I would both have to face the political difficulties created by the inevitable widespread suspicion that economic considerations were being overridden, at considerable cost, by other factors. These could easily have led to other misunderstandings in the future.

The Tanaiste's press conference on 8 August has aroused considerable press speculation on the future of the project and on the implications for Anglo-Irish relations. ^{That} ~~The fact that the project cannot proceed will therefore have to be announced very shortly,~~ ^{should} ~~and I am asking our Ambassador in Dublin to seek immediate discussions with your officials as to the best way of arranging this, with a view to minimising any damage to our continuing relationships.~~ ^{fairly soon} ~~with a view to minimising any damage to our continuing relationships.~~ ^{doing} On our side we shall wish to continue to lay the strongest emphasis on the fact that this is a decision forced upon us both by economic realities, and that it does not in any way diminish our desire for continued progress on the wide range of other business between our two governments.



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10 DOWNING STREET

From the Private Secretary

8 August, 1984

The Prime Minister has now received the attached message from Dr. Garret FitzGerald about Kinsale Gas in reply to hers of 30 July. No doubt you will be advising on whether and in what form we should respond further.

I am sending a copy of this letter and its enclosure to the Private Secretaries to members of E(A) and to Colin Budd (Foreign and Commonwealth Office) and Richard Hatfield (Cabinet Office).

(Timothy Flesher)

G. Sandiford, Esq.,
Northern Ireland Office

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ECC

PS
PS/LADY YOUNG
PS/VR WHITNEY

PS/S. O' S
PS/MR R. ANDREW
OAG 1/56

PS/PCS

MR. BERNAN

~~SIR J. BURNED~~

~~MR. ANGE~~

MR. JENAINS

J. LYON
~~MR. BOTS SWAN~~

NIO

N. I.O. LONDON * DB 081330Z

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Prime Minister

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TO IMMEDIATE FCO

TELEGRAM NUMBER 380 OF 8 AUGUST 1984

AND TO IMMEDIATE NIO (BELFAST) AND NIO (LONDON)(FOR BURNS)

ADVANCE COPY
IMMEDIATE

TELECON BARRIE/STIMSON:KINSALE GAS

FOLLOWING IS STATEMENT BY TANAISTE EMBARGOED FOR 1330Z.

BEGINS

" I WAS VERY CONCERNED TO LEARN OF A STATEMENT TO THE MEDIA ON 6TH AUGUST BY THE MINISTER OF STATE AT THE NORTHERN IRELAND OFFICE, MR ADAM BUTLER, MP, WHEN HE SAID, REGARDING THE SALE OF KINSALE GAS TO NORTHERN IRELAND, THAT "ON PRESENT CALCULATIONS THE EXISTING DEAL CAN NO LONGER BE VIABLE"

THE "EXISTING DEAL" REFERS TO THE MEMORANDUM OF UNDERSTANDING SIGNED ON BEHALF OF BOTH GOVERNMENTS IN OCTOBER, 1983, FOLLOWING TWO YEARS OF DETAILED NEGOTIATIONS. THE SATISFACTORY CONCLUSION OF NEGOTIATIONS WAS SUBSEQUENTLY WELCOMED BY THE TAOISEACH AND THE PRIME MINISTER IN THEIR JOINT COMMUNIQUE ON 7TH NOVEMBER, 1983.

THE BRITISH GOVERNMENT HAVE NOW CHANGED THEIR ATTITUDE AND HAVE SUGGESTED THAT THE IRISH GOVERNMENT ACCEPT A REDUCTION OF ALMOST 50 PERCENT IN THE AGREED PRICE PER THERM OF GAS. THE MEMORANDUM PROVIDES THAT THE FIRST REVIEW OF THE TERMS OF THE DEAL TAKES PLACE ONLY AFTER FIVE YEARS AND ANY CHANGE COULD THEN BE MADE ONLY BY THE AGREEMENT OF BOTH PARTIES. THIS PROVISION WAS INSERTED AT THE INSISTENCE OF THE BRITISH AUTHORITIES WHO WISHED TO SECURE FINALITY AND CERTAINTY IN THE TERMS.

FINALITY AND CERTAINTY IN THE TERMS.

THE REASONS ADVANCED BY THE BRITISH SIDE FOR THEIR CHANGE OF ATTITUDE RELATE TO RECENT PRICE AND MARKET DEVELOPMENTS. THE IRISH GOVERNMENT FIRMLY BELIEVE THAT THESE CONSIDERATIONS DO NOT JUSTIFY ANY CHANGE IN THE TERMS OF THE OCTOBER 1983 AGREEMENT FOR THE FOLLOWING REASONS:

- FIRST, THE MEMORANDUM OF UNDERSTANDING LINKED THE PRICE OF KINSALE GAS TO THE PRICE OF HEAVY FUEL OIL WHICH, OF COURSE, VARIES UPWARDS AND DOWNWARDS IN RESPONSE TO MARKET FORCES. BECAUSE OF SOME CURRENT EVENTS THE PRICE OF OIL HAS ESCALATED AND, ACCORDINGLY, THE PRICE OF GAS WILL BE HIGHER SO LONG AS THESE EVENTS CONTINUE. THE REPUBLIC WILL NOT BENEFIT FROM THIS PRICE INCREASE BECAUSE IT HAS IN TURN TO PAY A HIGHER PRICE FOR IMPORTED OIL TO REPLACE EXPORTED GAS.

- SECOND, BECAUSE OF UNCERTAINTY ABOUT THE ULTIMATE SIZE OF THE MARKET, THE MEMORANDUM OF UNDERSTANDING DELIBERATELY ALLOWED SUFFICIENT FLEXIBILITY TO CATER FOR A WIDE VARIATION IN THE DEMAND FOR GAS IN THE NORTH. A RECENT CONSULTANTS' ESTIMATE OF MARKET DEMAND IS WELL ABOVE THE MINIMUM QUANTITY OF GAS WHICH THE BRITISH AUTHORITIES ARE COMMITTED TO TAKE.

ONE CAN ONLY CONCLUDE, THEREFORE, THAT THE RANGE OF VARIABLES REGARDING FUTURE PRICES AND VOLUME DEMAND IS WITHIN THE RANGE ALLOWED FOR LAST OCTOBER WHEN BOTH GOVERNMENTS AGREED TO PROCEED WITH THE GAS DEAL. FURTHERMORE, THE COST PER THERM AGREED IN OCTOBER, FOLLOWING PROTRACTED NEGOTIATIONS, WAS AND REMAINS THE BEST COMMERCIAL OFFER THAT THE IRISH GOVERNMENT CAN MAKE.

WE HAVE CONFIRMED TO THE BRITISH GOVERNMENT OUR READINESS AND DESIRE TO PROCEED ON THE TERMS THAT WERE AGREED. '' ENDS

GOODISON

NNNN

PC

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IRISH EMBASSY, LONDON.

8 August 1984

Prime Minister

**PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T 143/84**

a MASTER
OPS

JA
8/8

Dear Private Secretary

I am instructed to forward to you the attached message from An Taoiseach, Dr Garret FitzGerald TD, for transmission to the Prime Minister.

Yours faithfully

Richard Ryan

Richard Ryan
Chargé d'Affaires a.i.

We can't go on it

the present price.

It seems cheaper

that we shall

Mr Charles Powell
Private Secretary to the Prime Minister
10 Downing Street
London SW1

have to abandon

the project. Please consult
with M. L. K.

mb

Message from An Taoiseach, Dr Garret FitzGerald T.D.,
to the Rt Hon Margaret Thatcher M.P.

Thank you for your letter of 31st July, in connection with the supply of Kinsale Gas to Northern Ireland. My Government have considered your arguments carefully and I must say to you that we do not find in them grounds for changing the terms of what was agreed between our Ministers. I regret very much that your Government are now proposing to abandon the project despite the intention to implement it fully which was recorded in the Memorandum of Understanding concluded by both Governments. We welcomed this achievement in our Joint Communique on 7th November, 1983.

The terms of the understanding were drawn up in such a way as to be fair to both parties and took full account of uncertainties about future energy prices, exchange rates and demand.

You have suggested a price reduction of almost half as being necessary to ensure a viable project. This would involve supplying the gas at a price so far below its economic value as to be utterly unreasonable.

I share your anxiety to make sure that a setback on this matter does not damage our ability to make progress on other business. I would, however, be concerned that the perception, particularly in Northern Ireland, of a failure by your Government to implement this important Anglo-Irish agreement would be very negative.

I remain convinced that a positive approach toward implementing the project would be successful and accordingly my Government wishes to proceed as was agreed.

8 August, 1984



10 DOWNING STREET

THE PRIME MINISTER

**PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T 137/84**

30 July 1984

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NIO
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CO*

*cc MASTER
OPS*

Dear Garret.

Thank you for your letter of 10 July about the Kinsale Gas project. I have discussed the issue once more very thoroughly with my colleagues: hence the short delay in my replying.

I was very glad when the two Governments reached agreement on the project last autumn. This was not just because of its importance for Northern Ireland, but because it seemed to me a project which demonstrably served the interests of both North and South. We could thus present it as an important step in the improved Anglo-Irish relations which we both want. This only makes the keener my disappointment that its future has been put at risk by changes in circumstances since the agreement was reached.

As Adam Butler has explained to the Tanaiste, the price of gas to Northern Ireland as determined by the formula in the Memorandum of Understanding is already far above anything that was foreseen last year. This means that the future competitive position of gas against coal in the Northern Ireland market is being seriously and continuously eroded. Moreover forecasts of demand have also changed considerably. As you say, these relate to the later years of the project, but it is precisely in that period that the project was due to earn the surpluses necessary to balance the heavy losses in the early years.

[Handwritten signature]

Thus instead of there being economic benefits for both sides as we hoped last autumn, we now find that it would impose a considerable burden on us. The gap between the price for the gas that would be produced under last October's formula and the price that we should now need in order to ensure a viable project is equivalent to a price cut of the order of 15p per therm. We cannot fill that gap without creating a wholly unfair burden on our economy.

I am reluctant to have to think in terms of abandoning the project. But the wider interests we both have at heart would not be served, at any rate on this side, by our entering into it on such manifestly uneconomic terms as those which I have described above. If you and your colleagues were able to make suggestions that would go a very substantial way towards bridging the gap, we should of course be ready to discuss them with you. Otherwise, I am sure you will agree, we have no alternative, in the face of these economic realities, but to end the project.

Should that also be your conclusion, it would be important to end the present uncertainty as soon as possible. In that event, may I say how anxious I am to make sure that a setback on this matter does not damage our ability to make progress on other business.

Y
Lansdown

Raymond S. Shaker



KEEP

10 DOWNING STREET

THE PRIME MINISTER

Thank you for your letter of 10 July about the Kinsale Gas project. I have ^{discussed it with you more very thoroughly} thoroughly re-examined the issue with my colleagues: hence the short delay in my replying.

I was very glad when the two Governments reached agreement on the project last autumn, ^{this was not just} not only because of its importance for Northern Ireland, but also because ^{it seemed to be a project which demonstrated} of its significance as a major example of mutually beneficial economic co-operation between North and South, ^{and that we could see it as an important step in the process which we both want} and indeed its benefits for Anglo-Irish relations as a whole. ^{It only makes the keener my disappointment} So it is a corresponding disappointment to me that its future has been put at risk by changes in circumstances since the agreement was reached.

As Adam Butler has explained to the Tanaiste, the price of gas to Northern Ireland as determined by the formula in the Memorandum of Understanding is already far above anything that was foreseen last year, ^{this means that} and the future competitive position of gas against coal in the Northern Ireland market is being seriously and continuously eroded. ^{However, forecasts of demand have also changed considerably} There are also major changes in the demand forecasts. As you say, these relate to the later years of the project, but it is precisely in that

/period

period that the project was due to earn the surpluses necessary to balance the heavy losses in the early years.

This instead of a benefit for both sides which
100% being a benefit for both sides as we hoped last
to be autumn we now get 100% of it would impose a
considerable burden on us.
We went into the project last autumn in the belief that it offered economic benefits to both countries. On our side, the changes I have referred to have turned the benefit into a burden. The gap between the price for the gas that would be produced under last October's formula and the price that we should now need in order to ensure a viable project is very large: *equivalent to a price cut of 15p per therm* on the assumption that the final price in 1985-86 is 28.5p per therm, the gap is equivalent to a price cut of some 15p per therm. We cannot fill that gap. *without creating* If we were to do so we should create a wholly unfair burden on our economy.

I am reluctant to have to think in terms of abandoning the project. *as those which have discussed here* But the wider interests we both have at heart would not be served, at any rate on this side, by our entering into it on such manifestly uneconomic terms. If you and your colleagues were able to make suggestions that would go a very substantial way towards bridging the gap, we should of course be ready to discuss them with you. Otherwise I think that we had better both face up to the economic realities, and agree to terminate it. If that is also your conclusion, it will be important to end the present uncertainty as soon as possible; and of course we should want to discuss with you how the project could be brought to an end with least damage to the fabric of Anglo-Irish relations. I am anxious to make sure that a setback on this project does not damage our ability to make progress on other business.

Dr. Garret FitzGerald, TD.

FROM: JOHN GIEVE
 DATE: 26 July 1984



ANDREW TURNBULL

10 Downing Street
 SW1

Dear Andrew

KINSALE GAS

TPM
 The Chief Secretary has seen the draft letter for the Prime Minister to send Dr Fitzgerald that Graham Sandiford circulated on 25 July. He thinks that the passage marked B in the final paragraph is completely unacceptable; it would give a clear impression that we could accept a reduction in price of, say, 7 or 8p. More generally, he feels that neither Options A or B have quite the right flavour. As he understood it the intention was not to invite a further round of the negotiations but to seem to walk away from the deal without completely closing the door on further proposals. He would prefer, therefore, a draft on the following lines:

"I am very sorry that we should find ourselves in this position but I see no alternative to facing up to the realities confronting us and acknowledging that in view of the scale of economic difficulty involved in the project we should now agree to terminate it. If this is also your conclusion then it will be important to end the present uncertainty as soon as possible and our Government will need to be in touch urgently to discuss how the project should be brought to an end with least damage to the close & flourishing relationship between our two countries that is so important to both of us. Of course, ^{if} at some later stage, circumstances should alter and you should feel disposed to make a different proposal then we should be very happy to consider it".

2. Copies of this go to Graham Sandford, Colin Budd,
and Richard Hatfield.

Yours sincerely

John Gieve

JOHN GIEVE

IRELAND: Natural Gas in N. Ireland: May 79

26 JUL 1984

11 12 1 2 3
4 5 6 7 8 9

Prime Minister

Andrew T

RTA has prepared a redraft
of the letter to Mr Fitzgerald
Content?

Ref. A084/2159

MR POWELL

AT 26/7

Kinsale Gas

The Private Secretary to the Secretary of State for Northern Ireland sent me a copy of his letter of 25 July, with a draft reply to the Taoiseach.

2. The Prime Minister asked me to look carefully at the draft in relation to other business between her and the Taoiseach.

3. I have slightly recast the draft letter in that light, and I attach a revised draft herewith. You will see that, in the last paragraph of the draft, I have adopted the version preferred by the Foreign and Commonwealth Secretary and the Secretary of State for Northern Ireland which talks about "suggestions which would go a substantial way towards bridging the gap", but I have strengthened that by talking about "a very substantial way".

RTA

ROBERT ARMSTRONG

26 July 1984

It is just not clear in
simple enough. Some of
the language on the point
was put very well

mb



DRAFT LETTER FROM THE PRIME MINISTER TO

Dr Garret FitzGerald
An Taoiseach
Dublin

Thank you for your letter of 10 July about the Kinsale Gas project. I have thoroughly reexamined the issue with my colleagues: hence the short delay in my replying.

I was very glad when the two Governments reached agreement on the project last autumn, not only because of its importance for Northern Ireland, but also because of its significance as a major example of mutually beneficial economic co-operation between North and South, and indeed its benefits for Anglo-Irish relations as a whole. So it is a corresponding disappointment to me that its future has been put at risk by changes in circumstances since the agreement was reached.

As Adam Butler has explained to the Tanaiste, the price of gas to Northern Ireland as determined by the formula in the Memorandum of Understanding is already far above anything that was foreseen last year; and the future competitive position of gas against coal in the Northern Ireland market is being seriously and continuously eroded. There are also major changes in the demand forecasts. As you say, these relate to the later years of the project, but it is precisely in that period that the project was due to earn the surpluses necessary to balance the heavy losses in the early years.



We went into the project last autumn in the belief that it offered economic benefits to both countries. On our side, the changes I have referred to have turned the benefit into a burden. The gap between the price for the gas that would be produced under last October's formula and the price that we should now need in order to ensure a viable project is very large: on the assumption that the final price in 1985-86 is 28.5p per therm, the gap is equivalent to a price cut of some 15p per therm. We cannot fill that gap. If we were to do so we should create a wholly unfair burden on our economy.

I am reluctant to have to think in terms of abandoning the project; but the wider interests we both have at heart would not be served, at any rate on this side, by our entering into it on such manifestly uneconomic terms. If you and your colleagues were able to make suggestions that would go a very substantial way towards bridging the gap, we should of course be ready to discuss them with you; otherwise I think that we had better both face up to the economic realities, and agree to terminate it. If that is also your conclusion, it will be important to end the present uncertainty as soon as possible; and of course we should want to discuss with you how the project could be brought to an end with least damage to the fabric of Anglo-Irish relations. I am anxious to make sure that a setback on this project does not damage our ability to make progress on other business.



10 DOWNING STREET

Prime Minister ①

RTA has not yet seen this, but subject to any comments he may have, are you content?

If so do you prefer A or B?

AT

25/7

Wants

rechecked

- c) it is too woolly
 - v) not clear.
- mt

From: THE PRIVATE SECRETARY

CEPC



NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

Charles Powell Esq
10 Downing Street
LONDON SW1

AT
For you I think
CDP

25 July 1984

Dear Charles

KINSALE GAS

I enclose a draft reply to Dr Garrett FitzGerald's letter of 10 July to the Prime Minister. The draft is based on the conclusions of yesterday's meeting of E(A) and has been drawn up in consultation with the Treasury and with the Foreign and Commonwealth Office.

In the final paragraph of the draft the Treasury think that the passage marked 'A' and shown in square brackets should be included; the Foreign and Commonwealth Office think that the passage marked 'B' and shown in square brackets would be more appropriate. Either passage would be consistent with the minutes of E(A), but my Secretary of State, who has approved the draft, is inclined to think that the text proposed by the FCO would reduce the dangers of Anglo-Irish relations while retaining the firmness of approach on which E(A) are agreed.

I am copying this letter and enclosure to the Private Secretaries to Members of E(A), to the Private Secretary to Sir Geoffrey Howe and to Richard Hatfield.

Your sincerely,

Graham Sandys



DRAFT LETTER TO DR. GARRET FITZGERALD

Thank you for your letter of 10 July about the Kinsale Gas project. Although time is very short, I thought it important thoroughly to re-examine the issues with my ^{Celmer} colleagues before replying.

We are acutely conscious of the importance of the Kinsale Gas project for Northern Ireland, for economic co-operation between North and South, and for Anglp-Irish relations as a whole. You know already how very glad I was when the two governments reached agreement on the project last Autumn. It was therefore very distressing for us to find that circumstances had undermined the economic viability of the project which we had seen as being a major example of mutually beneficial economic co-operation.

As Adam Butler explained to Mr. Spring, the price of gas to Northern Ireland as determined by the formula in the Memorandum of Understanding is already far above anything that was foreseen last year; and the future competitive position of gas against coal in the Northern Ireland market is being seriously and continuously eroded. There are also major changes in the demand forecasts; as you point out, these relate to the later years of the project - but it is precisely in that period that the project was to earn the surpluses necessary to balance the heavy losses in the early years. The combination of price changes and market shrinkage has destroyed the project's viability.

I believe I attach as much importance to this project as you - but it is precisely because of its importance in the development of Anglo Irish relations that it seems to us crucial that we should not go ahead with the project on a false prospectus. Both governments were united last Autumn in their belief that the project offered economic benefits to both countries. On our side the benefit has now turned into a burden. The gap between the price for the gas that would be produced under last October's formula and the price that we would now need in order to ensure a viable project is very large - on the assumption that the formal price in 1985/86 is 28.5p per therm the gap is equivalent to a price cut of some 15p. I appreciate the enormity for you of any suggestion that your government should fill that gap; but I hope that you will also understand that it is impossible for us to



fill it. If we were to do so we would create a wholly unfair burden on our economy; and the project itself would suffer from the perception that it was being pursued solely for political reasons.

I am very sorry that we should find ourselves in this position.

A [However, unless you have any proposal for yourselves bridging the gap]

B [However, unless you can make suggestions which would go a substantial way towards bridging the gap] that lies between the project and economic viability (and I can see that this might be unacceptably difficult for you and your colleagues), then I see no alternative but to face up to the realities confronting us, and to acknowledge that in view of the scale of economic difficulty involved in the project, we should now agree to terminate it. If this is also your conclusion, then it will be important to end the present uncertainty as soon as possible, and our governments will need to be in touch urgently to discuss how the project should be brought to an end with least damage to the close and flourishing relationship between our two countries that is so important to both of us.

IRELAND: Natural Gas : May 79



20 JUL 1984



10 DOWNING STREET

Prime Minister

Foreign Secretary has minuted supporting an attempt at renegotiating a cut in the price to cover operating costs only.

The Cabinet Office brief, however, challenges the argument that the capital cost of the new project is matched by the cost of closing the existing industry. The saving on keeping open the existing industry is more than swallowed up by higher electricity subsidies.

AT

23/7

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by landress.

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No infrastructure.

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CONFIDENTIAL

P.01351

PRIME MINISTER

Kinsale Gas:

E(A)(84)46

Flag A

At their meeting last week the Sub-Committee agreed that they needed more information before they could take a decision on whether to proceed with negotiations for the supply to Northern Ireland of natural gas from the Kinsale field (E(A)(84)19th Meeting, Item 4). The memorandum by the Secretary of State for Northern Ireland (E(A)(84)46) sets out the information requested by the Sub-Committee.

Flag B

Proposed pricing formula

The pricing formula is set out in Annex A to the memorandum. It links the price of gas in each quarter to the average prices of heavy fuel oil and gas oil in the preceding quarter. It is forecast that the price in 1985-86 would be 28.5 pence a therm.

Required reduction in price

To return the project to the level of viability projected in the Autumn of 1983 would require a reduction in price of about 15 pence a therm. To cover the operating costs only would require a reduction of about 5 pence a therm.

Currency

Although payment is in sterling, pricing is effectively in US \$.

CONFIDENTIAL

Risk-sharing

Mr Prior implies that it may be possible to negotiate arrangements to share the risks arising from changes in the relative prices of heavy fuel oil and crude oil, but rules out any prospect of being able to negotiate sharing of the risks arising from movements in the exchange rate between the pound and the US dollar.

- Flag C
2. The brief I submitted for the last meeting of the Sub-Committee remains valid: for convenience I attach a copy. The present minute comments briefly on how the information in E(A)(84)46 affects the issues.

Basis for re-negotiation

3. The only basis for negotiation which would restore the project genuinely to the level of viability assumed last autumn would be a reduction of 15 pence a therm, ie a reduction of more than half in the price of 28.5 pence a therm assumed for 1985-86. It seems inconceivable that the Irish would agree to this. Embarking on a renegotiation on this basis might indeed cause more ill-will than withdrawal from the project.

4. Mr Prior's preferred proposal is to seek a reduction of 5 pence a therm. This would enable the project to cover its operating costs. It would not however restore the project to the viability assumed last September. He justifies this proposal on the grounds that we need not look for a return on the capital costs of the investment since we should avoid the cost of closing down the Northern Ireland town gas industry. But the benefit of the latter was included in the economic assessment last autumn and has to be offset by the extra costs of subsidising the Northern Ireland electricity industry. We cannot count that benefit twice. A price reduction of 5 pence a therm therefore requires in practice a United Kingdom Government subsidy to this project.

CONFIDENTIAL

CONFIDENTIAL

5. We cannot be sure that the Irish would accept even this proposal. They would argue that they were being expected to accept what is, internationally, a low price for their gas. Our reply would be that we were making a major concession in subsidising the capital costs of the project; they should be prepared to make a sacrifice also.

6. If Ministers think that a 5 pence reduction is worth pursuing, they will need to consider whether it is essential also to secure satisfactory risk-sharing arrangements. Trying to do so would no doubt increase the difficulty of negotiating a reduction in price.

Issues to be decided

7. The options are as follows:

- i. Renegotiation:
 - a. on a basis that would restore viability to the project ie a reduction of 15 pence a therm;
 - b. on a basis which would involve a UK subsidy but which might just be acceptable to the Irish, ie a reduction of 5 pence a therm.
- ii. Withdrawal.

8. If it is decided to withdraw, how should this be done? Should we, for example, suggest that there should be studies of possible ways of collaborating on other energy projects?

PLG

P L GREGSON

23 July 1984



PM/84/128

PRIME MINISTER

Renegotiation of the deal to supply Kinsale Gas from the
Republic of Ireland to Northern Ireland

1. I understand that the proposed sale of gas from the Kinsale field, which was discussed in E(A) on 18 July, is to be considered again at a meeting of E(A) on 24 July. As I may not be able to attend, I thought it would be useful if I were to put my views in writing.
2. We are all agreed that the project cannot go ahead on the basis of the existing Memorandum of Understanding. It must be seen to be commercially viable if it is to be regarded as a genuine example of North/South cooperation. It will be bitterly condemned by unionist opinion if it appears to be motivated by political rather than economic calculations.
3. But as I pointed out in my minute to you of 28 June, simple cancellation of the project without any attempt to improve the terms, would lay us open to serious charges of bad faith and would represent a set-back to Anglo-Irish relations at a particularly delicate time.
4. I therefore believe that if we can come up with a new financial formula which has a prospect of being accepted by the Irish and which would render the project commercially viable, we should press the Irish to renegotiate the deal. In doing so, we should be prepared to take into account the

/cost



cost of closing down the existing Northern Ireland gas industry and should, if necessary, be prepared to make a contribution to the capital costs of the project.

5. The Irish probably see it as being in their interests to stall for as long as they can. They may even be prepared to dig in their heels and force us to cancel, in which case they would certainly try to put the blame on us. But there are domestic political factors which may encourage them to agree to renegotiate:

- (a) they cannot afford to abandon such an important project without making every effort to save it. They would stand to lose possibly Irish £500 million in foreign exchange over a period of 20 years;
- (b) cancellation would play into the hands of Mr Haughey and would tend to undermine the basis of Dr FitzGerald's conciliatory approach to Anglo-Irish relations;
- (c) Mr Spring's standing would be further damaged by the overthrow of a major project for which his Ministry is responsible.

6. Provided that we can devise a reasonable financial formula, I think that we should make it clear to the Irish that if they are not prepared to renegotiate, we will be forced, most reluctantly, to revoke the Memorandum of Understanding. In these circumstances, I believe that there is a chance that the Irish may be prepared to make concessions.

CONFIDENTIAL



7. I am sending copies of this minute to our E(A) colleagues, to James Prior and to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be 'G. Howe', written in a cursive style.

(GEOFFREY HOWE)

Foreign and Commonwealth Office
23 July 1984

CONFIDENTIAL

IRELAND: Supply of Natural Gas
May 79

23 JUL 1979

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P.01345

PRIME MINISTERKinsale Gas

BACKGROUND

In October 1983 a Memorandum of Understanding was signed with the Republic of Ireland for the supply of natural gas from the Kinsale field to Northern Ireland. Ministers approved the signing of the Memorandum on the basis that, although the appraisal had indicated that the project would show a rate of return only marginally above the minimum Required Rate of Return, there were wider social, economic and political advantages which outweighed the undoubted commercial risks (E(A)(83)4th meeting).

FLAG A

2. A draft contract is now ready for signature. But the outlook on two of the key factors determining the project's rate of return has changed markedly since the Autumn. First the prospective market in Northern Ireland is now thought to be about one-third lower than estimated then. Secondly, the prospective price at which the Irish Government would sell the gas has risen, because of movements in the price of heavy fuel oil (to which the gas price is linked) and the exchange rate. Their combined impact is to make the projected rate of return on the project strongly negative: the net present value of the project has been revised downwards from £+4 million to £-107 million. To restore the marginal rate of return on the project expected when the Memorandum was signed, the price at which the gas is obtained from the Irish Government would have to be more than halved.

FLAG B

3. The Secretary of State for Northern Ireland reported the revised assessment to you in his minute of 22 June 1984. He argued that the Government should renegotiate the terms



and conditions of the contract; he proposed that the Government might pay the capital cost of the project (£140 million) on the grounds that if the project went ahead, it would avoid expenditure of the same order otherwise necessary to close the existing Northern Ireland gas industry. He suggested that the Irish Government would look to the United Kingdom (UK) Government to make a contribution of at least this size, in view of the political importance attached to the project. If the capital costs were met in this way, then providing a reduction of 4-5 pence per therm in the selling price of the gas could be negotiated with the Irish Government, the project would cover its operating costs.

FLAG C

4. In his minute of 28 June the Secretary of State for Foreign and Commonwealth Affairs supported renegotiation.

FLAG D

The Chief Secretary, Treasury, however, in his minute of 29 June suggested that unless the 15 pence per therm reduction in the selling price necessary to restore commercial viability could be secured, the Government should withdraw from the project. Your Private Secretary's minute of 3 July agreed that an attempt should be made to renegotiate the terms of the contract; but you also pointed out that it might ultimately be necessary to withdraw from the project.

FLAG E

5. On 4 July the Minister of State, Northern Ireland Office (Mr Butler) discussed the contract with the Irish Minister of Energy, Mr Spring. Mr Butler indicated that renegotiation of the contract would be necessary if the UK were to go ahead; Mr Spring professed to be surprised and no real negotiations took place. On 10 July the Irish Prime Minister wrote to you and proposed that the project should proceed on the basis of the original Memorandum of Understanding.

FLAG F

FLAG G



6. In his minute to you of 13 July Mr Prior sets out the options as follows:

- a. to accept the terms and conditions now on offer and sign the contract;
- b. to withdraw, without any attempt to negotiate concessions, on the grounds that the project is now too far from viability;
- c. to negotiate with a view to achieving a major concession on price.

He attaches a draft letter for you to send to Dr Fitzgerald on the basis of option c. He suggests however that it would not be desirable to float a compromise until Ministers have reached a clear view on the extent to which we are willing to renegotiate.

MAIN ISSUES

7. It is not disputed that the project is now totally uneconomic: no one favours accepting the contract on the basis of the original Memorandum of Understanding. The choice therefore lies between withdrawal and renegotiation.

The case for withdrawal

8. We understand that the Chief Secretary, Treasury will argue that, since there is now no realistic prospect of an economic rate of return (because the Irish Government will not bridge the price gap) the UK should withdraw. He will point out that Ministers have not previously agreed to overt subsidy for the project; that to offer subsidy on gas would be expensive in itself; and that it makes no sense to subsidise gas in Northern Ireland, when electricity is heavily subsidised. The subsidies necessary on electricity, because of a likely decline in demand once gas becomes available could indeed have to be increased.

The case for renegotiation

9. The case for renegotiation is primarily political. Abandonment of the project will undoubtedly have a bad effect on relations with Dr Fitzgerald's Government. On the other hand, as Mr Prior has pointed out, a joint project which was demonstrably uneconomic would attract political criticism and harm the cause of Anglo-Irish cooperation.

The basis of renegotiation

10. If it is agreed that renegotiation should be attempted, it should be borne in mind first that a reduction of 15 pence per therm in the price of gas would be necessary to restore the level of viability assumed in September 1983, and secondly that the Irish Government has so far shown no disposition to accept any reduction in price. The options are therefore:

- to seek a price reduction of 4 or 5 pence per therm and meet capital costs of around £140 million as Mr Prior envisaged in his minute of 22 June
- to seek a larger price reduction (say of 7 or 8 pence per therm) and make a smaller contribution to capital costs.

11. If however it is concluded that there is no basis for renegotiation which would be acceptable both to ourselves and to the Irish, withdrawal may be the more straightforward course. Ministers would then need to consider further how withdrawal might be handled in the way least likely to damage Anglo-Irish relations.

HANDLING

12. You will wish to invite the Secretary of State for Northern Ireland to open the discussion. The Chief Secretary, Treasury will wish to argue the case for withdrawal and the Secretary of State for Foreign and Commonwealth Affairs the case for renegotiation. The Secretaries of State for Energy and Trade and Industry and the Chancellor of the Duchy of Lancaster will wish to contribute to the discussion.



CONCLUSIONS

13. You will wish the Sub-Committee to reach conclusions on the following:

- i. whether to seek an orderly withdrawal from the project; or
- ii. whether to seek renegotiation of the terms and conditions of the contract; and if so on what basis.

PLG

P L GREGSON

17 July 1984

MR TURNBULL17 July 1984KINSALE GASWhat has gone wrong

We are placed in an extremely difficult position over this contract. When E(A) gave the go-ahead last September, wider social and political considerations tilted the balance in favour of what was a very marginal economic project.

Since then market assessments have dropped by a third; the purchase price has risen by 17% (based on revised higher fuel oil prices which are the predominant element in the price formula); and the exchange rate has moved adversely. The result is a hopelessly uneconomic project.

It is reasonable to ask why the underlying assumptions of a project with a 32 year life should have changed so fundamentally in the course of 9 months. The answers are unconvincing.

The original market surveys were carried out in 1981. The desk revisions which took place in 1983 significantly underestimated the extent to which gas was losing the central heating market. This fact only emerged in market surveys carried out since. Similarly, recent sharp rises in fuel oil prices caused by the miners' strike do not fully explain why the underlying trend in fuel oil prices forecast for the next 30 years should have changed so significantly.

The simple answer is that we underestimated the degree of risk. It is not surprising that the Irish Government are now surprised that we wish to renegotiate the contract.

The Irish did in fact come very well out of the earlier negotiations. The price formula represented an extremely good deal for the seller but a very exposed position for the purchaser. The formula was based on 90% of the prevailing heavy fuel oil price and 10% of the gas oil price subject to 3 monthly adjustments. This was in line with the Irish Government's policy of selling the gas at a price which would enable them to replace it eventually with oil. The result however, as far as the purchaser is concerned, is that any rises in the fuel oil price which would normally improve the competitive position of gas will be nullified.

What to do now

Nevertheless, this is all water under the bridge. We now have no alternative but to renegotiate the terms of the contract or to withdraw.

DAVABD

There is no chance of renegotiating a price cut of up to 15p per therm needed to restore the original marginal real rate of return. The best we can hope for is to reduce the price by about the 5p needed to ensure that revenues match operating costs. This assumes that we subsidise the £122 million capital costs of the project, on the basis that we would otherwise be liable for expenditure of the order of £140 million to secure the orderly closure of the existing gas industry. This latter figure includes conversion of appliances, and appropriate redundancies.

In the circumstances, this is probably the best we can hope to achieve. However, it is by no means certain that the Irish Government will accept and unless we can achieve this minimum position, we should withdraw. Even on this basis this remains an extremely risky project.

There is also the further point that the Kinsale project will increase electricity subsidies in Northern Ireland as gas sales reduce electricity revenues. These subsidies are currently running at £89 million per year. At the time of the original decision, E(A) commissioned an NIES generating strategy study with the aim of reducing electricity subsidies. This study is still outstanding and should be brought forward as soon as possible.

Conclusion

This project demonstrates once again the pitfalls when governments attempt to forecast supply and demand in the energy industries. It is difficult to place any credibility on the figures being put to E(A).

Given the special circumstances of Northern Ireland and the history of this project, we recommend that the terms of the contract should be renegotiated in order to ensure financial viability after capital costs of £122 million have been written off. If the Irish Government do not accept this position, which is a long way from a viable project in its own right, we recommend that the project should be cancelled.

DLP.

DAVID PASCALL

DAVABD

CONFIDENTIAL



Chancellor of the Duchy of Lancaster

Cenro

CABINET OFFICE,
WHITEHALL, LONDON SW1A 2AS

16 July 1984

NBPM

DB

1677

Dear Derek,

KINSALE GAS

Thank you for your letter of 13 July to Alex Galloway.

The Chancellor of the Duchy has commented that the pattern of prices that emerges from the correspondence looks very odd:

	<u>Pence per Therm</u>
Original figure	24.1
April 1983 revise	27.1
Q2 1984	31.9
Q3 1984	33.7
Q4 1985	28.5

Lord Cockfield wonders whether such figures do not suggest that there may be something peculiar about the formula which gives rise to them. It might well be helpful if some further light could be shed on this before the discussion in E(A) on Wednesday.

I am copying this letter to the Private Secretaries to the members of E(A), to Roger Bone (FCO) and to Richard Hatfield.

James
Sebastian Birch

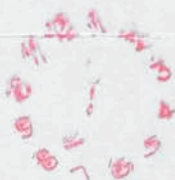
SEBASTIAN BIRCH

D A Hill
Private Secretary to the Secretary
of State for Northern Ireland
Northern Ireland Office
Old Admiralty Building
London SW1

Natural Gas to NI.

Ireland May 79

16 JUL 1979



For E(A) a Wednesday AT 16/7

CONFIDENTIAL

Prime Minister

This will be on the agenda for E(A) on Wednesday. No action required at present

AT 13/7

Prime Minister

1. You have received Garret FitzGerald's letter of 10 July in which he asks whether the Government is prepared to proceed with the project on the basis of the Understanding agreed in October 1983. Receipt of Dr FitzGerald's letter does not change the options open to us which are -

- (a) to accept the terms and conditions now on offer and sign the contract because it is politically too late and too dangerous for Anglo-Irish relations to let the project fall; (Dr FitzGerald's case)
- (b) to accept that the project is so far from viability in the circumstances which now face us, particularly as to purchase price, that we should seek an orderly withdrawal from our commitment without an attempt to negotiate concessions which would still leave us with a project unable to meet the conventional tests; or
- (c) in line with the proposals made in my letter to colleagues of 22 June and the acceptance by you that we should seek to re-negotiate, we should urge the Republic to discuss with us a major concession on price.

2. Dr FitzGerald gives no indication that his government is willing to make concessions on the purchase price of gas and indeed his final paragraph is seeking to establish whether we are prepared to go forward without re-negotiation. I still feel that this is not an option which is tenable for reasons which are spelled out in the draft reply. Dr FitzGerald's final

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question leaves it open to us to accept the implication of his letter that no price abatement is likely and to begin the formal withdrawal process at this stage. I assume, however, that you will be reluctant to authorise this drastic step without further collective discussion.

If however we are to pursue course (c), I think we must first form a clear and collective judgement as to whether any concession the Irish are likely to contemplate could bring the project within the bounds of acceptability, having regard to its wider political significance. The Chief Secretary clearly thinks not, and although I believe his reaction to the note of Adam Butler's meeting with Mr Spring did not do justice to the skill with which Adam played a most difficult part, I do not believe it would be in our interest, in replying to the Taoiseach, to float the idea of a compromise unless and until we have decided that we could live with the result (and there is no present ground for believing that the Irish would be prepared to contemplate a price concession of 4 or 5 pence per therm).

Indeed, until we have reached a collective view on the extent to which we are willing to renegotiate, I do not think that any useful reply can be sent to Dr FitzGerald. Any holding reply would run the risk of allowing him to think that we might be willing to do as he says, and to proceed on the basis of the October 1983 understanding.

I am acutely conscious of the time constraints upon the project. If we are to have any hope of bringing natural gas into Belfast by the autumn of next year (which was our original intention) we cannot contemplate delaying the decision beyond early August at the latest. To miss this date will not only set back the programme by a year, but will also effectively destroy the public

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confidence and the consumer base upon which the new industry
is to be built.

I hope therefore that we can meet urgently to discuss the approach
we should take; if we decide to follow course (c), you could then
reply to Dr FitzGerald on the lines of the attached draft.

I am sending copies of this minute (with a copy of Dr FitzGerald's
letter to you) to our EA colleagues, Sir Geoffrey Howe and to
Sir Robert Armstrong.



JP

13 July 1984

DRAFT LETTER

FILE NUMBER.....

ADDRESSEE'S REFERENCE.....

<p>To</p> <p>Dr FitzGerald</p> <p>(Full Postal Address)</p>	<p>Enclosures</p>	<p>Copies to be sent to</p> <p>(Full Address, if Necessary)</p>
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LETTER DRAFTED FOR SIGNATURE BY PRIME MINISTER
(Name of Signatory)

Thank you for your letter of 10 July. I do appreciate your concern about the proposals for the supply of natural gas to Northern Ireland. We found it very distressing that Adam Butler had to tell Mr Spring of the difficulties which had become clear so late in the day.

While the deteriorating market situation has a major impact upon the project, the price of gas to Northern Ireland as determined by the formula in the Memorandum of Understanding is already very significantly above anything which was foreseen last year - and all our advice is that this is not simply a short-term aberration in the market but a trend that is likely to continue. The competitive position of gas against coal in the Northern Ireland market is being seriously and continuously eroded.

/...

CONFIDENTIAL

It is true that the major changes in the demand forecasts relate to the latter part of the project but it is precisely in that period that the project was to earn significant surpluses to balance the heavy losses in its early years. Indeed, to help the project meet the test of financial viability, we have been prepared to evaluate it over a period well beyond the 22 years of the intended gas supply contract - thus taking on trust our ability to contract further supplies on reasonable terms. On any reasonable assessment, the latest projections of market and gas price would not allow the project to be viable even on such generous treatment. Indeed on present perceptions it could have a serious negative impact upon the Northern Ireland public expenditure provision over the total period.

Like you I am extremely unhappy faced with the prospect that the Memorandum of Understanding might not be capable of being developed into the mutually beneficial project which we all believed to be within sight at that time. We were careful always (on both sides) to point to our intention that the supply of natural gas from Kinsale to Northern Ireland would be undertaken as a sound economic project which was financially viable in its own right. We made clear that it was not being undertaken for political reasons and on that basis it demonstrated the value of co-operation in appropriate economic areas. There is no doubt that if we were to go forward on a basis which could be easily shown to be non-economic for Northern Ireland the credibility of further economic co-operation between the two governments in relation to Northern Ireland would be seriously undermined.

CONFIDENTIAL

CONFIDENTIAL

The changes which Adam Butler explained to Mr Spring therefore pose a real dilemma. The economic justification for the gas project has been transformed into an economic burden. It would be irresponsible to continue with the project as it stood in the October 1983 understanding. But the project has the same high political importance for the United Kingdom as it does for the Republic of Ireland, and it was in recognition of this, and in the hope that it might still be possible, by major moves on both sides, to save the project from cancellation, that Adam Butler asked Mr Spring whether your Government would be willing to make such a move. I appreciate that the difficulties for you are great, but we would not have broached the matter with your Government if the difficulties for us were not so great as to compel us to face the prospect of cancellation. Because of the wider importance of the project we are ready, if you are, to take on a major extra burden in financing it; I hope very much that you will be able to say the same.

CONFIDENTIAL

AMBASÁID NA hÉIREANN, LONDAIN



IRISH EMBASSY, LONDON.

17 Grosvenor Place

SW1X 7HR

1 AT
2 CDP
14/7.

3. CF to BIF
with draft
replies from NIO

AF
1217

12th July 1984

Dear Private Secretary,

With reference to my letter of 10th July in which I enclosed the text of a letter from the Taoiseach, Dr Garret FitzGerald TD to the Prime Minister, The Rt Hon Mrs Margaret Thatcher, I now enclose herewith the Taoiseach's original letter. I should be grateful if you would kindly bring it to the attention of the Prime Minister.

*Yours sincerely
Noel Dorr*

Noel Dorr
Ambassador

Mr Charles Powell
Private Secretary to
The Rt Hon Mrs Margaret Thatcher MP
10 Downing Street
London SW1

Encl.

BIC with E(A) papers
11/13
CO NO
MS

From: THE PRIVATE SECRETARY



NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

A K Galloway Esq
PS/Chancellor of the Duchy of Lancaster
Cabinet Office
Whitehall
London SW1

13 July 1984

Dear Alex

Lord Cockfield has asked what is the present price of the gas from which the 5p reduction is being sought.

If Kinsale gas was now available it would have cost 31.9p/therm for the period April-June 1984. For the third quarter of 1984 it would be about 33.7p/therm. Using the economic assumptions provided by the Department of Energy earlier this year and applying them to the purchase price formula agreed with the ROI, the gas price at the end of 1985 (when the first gas should arrive) would be 28½p/therm. It is from this price that we would require a reduction of 5p/therm to ensure that, if all fixed capital costs were paid, the project would be able to cover its total operating deficit. On present assumptions the reduction would have to remain over the life of the project (32 years) and the figure of 5p be appropriately escalated year by year.

I am copying this letter to the Private Secretaries to the members of E(A), Roger Bone FCO and Richard Hatfield.

Yours ever

Dave

D A HILL

Ireland: Economic Co-operation

5/79

CONFIDENTIAL



B/P with
draft re: D Fitzgerald
and DOD are supplying

AT
11/2

Treasury Chambers, Parliament Street, SW1P 3AG

A J Turnbull Esq
PS/Prime Minister
10 Downing Street
LONDON
SW1

11 July 1984

Dear Andrew

KINSALE GAS

with AT?

The Chief Secretary was alarmed to read, in a letter of 4 July, the account of Mr Butler's meeting with the Irish Minister of Energy in Dublin.

He appreciates that Mr Butler did not quote a specific figure in pence per therm for the price at which he would be prepared to settle. But Mr Butler's hint to Mr Spring, that we might be able to consider disregarding the capital costs of the project, must surely point the Irish towards a reduction of around 5p per therm as the kind of level we could accept. Yet the Chief Secretary pointed out, in his minute to the Prime Minister of 29 June, that even a 15p reduction would not be enough to make the project commercially attractive.

He hopes that the commercial realities of this deal can be kept firmly in mind during the negotiations and that Ministers will have an opportunity to discuss the matter collectively before any understanding is reached with the Irish Government.

Copies of this go to Derek Hill, Peter Ricketts, Alex Galloway & Richard Hatfield.

Yours sincerely

J.S. Gieve



British Library, 96 Euston Road, London NW1 2DB

11 JUL 1984



BRITISH LIBRARY



**PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T122AA/84**

**a MASTER
OPS**

10 July, 1984.

Oifig an Taoisigh
Office of the Taoiseach

The Rt. Hon. Mrs. Margaret Thatcher, M.P.,
Prime Minister.

Dear Margaret,

I was concerned and indeed taken aback to hear from the Tanaiste that the Minister of State at the Northern Ireland Office Mr. Butler has indicated to him that the British side now want a radical change in the terms of the Memorandum of Understanding signed on behalf of both Governments in October 1983 providing for the supply of Kinsale Gas to Northern Ireland.

You will recall that the negotiation of this important project was heralded in our joint communique of 5 November, 1981 and that on 7 November, 1983, we jointly welcomed the satisfactory conclusion of negotiations.

The reasons given by Mr. Butler for this change of attitude include recent changes in the sterling/dollar exchange rate and in the price of heavy fuel oil, which under the agreement determine the price of gas. But the central factor is a downward revision in projected market size.

But the more pessimistic forecast now being put forward relates only to the year 1990 and beyond, and involves a level of demand which is two-thirds of the maximum figure stipulated in the agreement, while the agreement itself allows that the quantity of gas to be taken may be reduced to one-third of the maximum.

The agreement between our two Governments on this project was seen in our two countries as the most important economic initiative between North and South in Ireland ever undertaken. A withdrawal from its terms at the initiative of either side would, I feel sure, adversely affect the public perception of our relations and of our capacity to work together.

/.....



Oifig an Taoisigh
Office of the Taoiseach

-2-

I feel that I have no option but to ask you whether your Government is prepared to proceed on the basis of the understanding agreed in October, 1983.

Best Wishes.

Yours,

Ireland: Economic Co-operation
5779

file

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10 DOWNING STREET

From the Private Secretary

10 July 1984

KINSALE GAS

The Prime Minister has been sent the attached note from the Irish Government on Kinsale gas. She will be speaking to Dr. FitzGerald on the telephone tomorrow morning on another subject but it is possible that he will use the opportunity to raise the question of Kinsale gas. I would be grateful if you could advise, by close of play tonight, on the line which the Prime Minister should take if this happens.

I am copying this letter to John Gieve (Chief Secretary's Office), Peter Ricketts (Foreign and Commonwealth Office), Alex Galloway (Chancellor of the Duchy of Lancaster's Office) and Richard Hatfield (Cabinet Office).

(Andrew Turnbull)

Derek Hill, Esq.,
Northern Ireland Office

From: THE PRIVATE SECRETARY

CONFIDENTIAL

NORTHERN IRELAND OFFICE

WHITEHALL

LONDON SW1A 2AZ



Dear Andrew

Kinsale Gas

I attach as requested
a line to take for use by
the Prime Minister if Dr
FitzGerald raises the topic of
Kinsale gas, about which he
has written.

I am copying this letter to
John Gieve, Peter Richetts, Alex
Galloway and Richard Hatfield

Yours ever

Derek

CONFIDENTIAL

KINSALE GASLine to Take:

We do regard the understanding reached last year as very important but it is essential that the project at least covers its operating costs. We do have a serious difficulty about future demand given the current price. I therefore hope it will be possible to reach a mutually satisfactory accommodation on price. Mr Butler is ready to discuss this further with Mr Spring.

Background Note:

On 4 July Mr Butler, Minister of State for Northern Ireland met the Irish Minister of Energy in Dublin. He explained that the combination of oil price changes, exchange rate changes and new market assessments had shown that the project, hitherto marginally viable, would now offer no return on the Government's investment. If HMG were to proceed with the project on the present basis it would have to invest heavily to cover the capital costs without real prospect of repayment or return. It could not contemplate moving forward with a project which did not even cover its operating costs.

2. HMG's view is that the only way forward is for the Irish to offer a reduction in the price per therm. However the meeting did not discuss the level of price reduction needed (nor is one contemplated in Dr FitzGerald's letter) but unless this is reduced by at least 5 p per therm the project is unlikely to be able to recover its operating costs. (let alone full costs)

3. The Irish Cabinet met on 10 July to discuss the gas issue. Dr FitzGerald may seek an understanding from the Prime Minister that HMG would be willing to make a significant contribution to the project - perhaps disregarding some or all of the £140m capital costs. This issue would have to be agreed collectively.

Prime Minister
Andrew and I both
feel it would be a
mistake to get into the
substance during the
telephone call. A procedural
reply - received the message,

will look into it & let
you have an answer soon -
would be better.
CDP 10/7.

AMBASÁID NA HÉIREANN, LONDAIN.



IRISH EMBASSY, LONDON.

17 Grosvenor Place

SW1X 7HR

10th July 1984

Dear Mr Powell

I should be most grateful if you would be kind
enough to convey to the Prime Minister the
enclosed ^{text of a} letter from the Taoiseach, Dr Garret
FitzGerald TD.

Yours sincerely

Noel Dorr
Ambassador

Mr Charles Powell
Private Secretary to the Prime Minister
10 Downing Street
London SW1

10th July 1984

The Rt Hon Mrs Margaret Thatcher MP
Prime Minister

Dear Margaret

I was concerned and indeed taken aback to hear from the Tanaiste that the Minister of State at the Northern Ireland Office Mr Butler has indicated to him that the British side now want a radical change in the terms of the Memorandum of Understanding signed on behalf of both Governments in October 1983 providing for the supply of Kinsale Gas to Northern Ireland.

You will recall that the negotiation of this important project was heralded in our Joint Communiqué of 5th November 1981 and that on 7th November 1983 we jointly welcomed the satisfactory conclusion of negotiations.

The reasons given by Mr Butler for this change of attitude include recent changes in the sterling/dollar exchange rate and in the price of heavy fuel oil, which under the agreement, determine the price of gas. But the central factor is a downward revision in projected market size.

But the more pessimistic forecast now being put forward relates only to the year 1990 and beyond, and involves a level of demand which is two-thirds of the maximum figure stipulated in the agreement, while the agreement itself allows that the quantity of gas to be taken may be reduced to one-third of the maximum.

The agreement between our two Governments on this project was seen in our two countries as the most important economic initiative between North and South in Ireland ever undertaken. A withdrawal from its terms at the initiative of either side would, I feel sure, adversely affect the public perception of our relations and of our capacity to work together.

I feel that I have no option but to ask you whether your Government is prepared to proceed on the basis of the understanding agreed in October 1983.

Best wishes,

Yours,

Garret FitzGerald

CONFIDENTIAL



Chancellor of the Duchy of Lancaster

FCNO

MSM
11/9/84

CABINET OFFICE,
WHITEHALL, LONDON SW1A 2AS

6 July 1984

Dear Graham,

KINSALE GAS

The Chancellor of the Duchy has seen your letter of 4 July to Andrew Turnbull recording Mr Butler's meeting with Mr Spring.

Lord Cockfield has asked what the present price of the gas is, from which the 5p reduction is being sought.

I am copying this letter to the Private Secretaries to members of E(A), Roger Bone (FCO) and Richard Hatfield.

Yours sincerely,

Alex Galloway

A K GALLOWAY
Private Secretary

G Sandiford Esq
Private Secretary
Northern Ireland Office
Whitehall
London SW1A 2AZ

CONFIDENTIAL

CONFIDENTIAL



be Policy Unit

file

10 DOWNING STREET

From the Private Secretary

5 July, 1984.

Kinsale Gas

The Prime Minister has seen and noted your letter to me of 4 July reporting on Mr. Butler's discussions with Mr. Spring on the Kinsale Gas project. She awaits a further report when the Irish have reacted.

I am sending copies of this letter to the Private Secretaries to the members of E(A), to Len Appleyard (Foreign and Commonwealth Office) and to Richard Hatfield (Cabinet Office).

Andrew Turnbull

G.K. Sandiford, Esq.,
Northern Ireland Office.

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NO

CONFIDENTIAL

From: THE PRIVATE SECRETARY



Prime Minister ②

To note and await further Irish reaction.

AT
4/7

NORTHERN IRELAND OFFICE

WHITEHALL

LONDON SW1A 2AZ

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

4th July 1984

Dear Andrew,

KINSALE GAS

Mr Butler met Mr Spring, the Irish Minister of Energy in Dublin earlier today. Mr Butler explained that the combination of oil price changes, exchange rate changes and new market assessments had shown that the project, hitherto considered marginally viable, would now offer no return at all on the Government's investment. The magnitude of the change was illustrated by the fact that a price cut of 13-15p per therm would be needed to restore the original, marginal, real rate of return. We were naturally embarrassed at this development, for we had hoped that a viable agreement had been reached last autumn. Like the Irish, we attached great importance to the project, which both sides had seen as a unique example of economic co-operation with mutual benefits. But the latest information could not be ignored, and it showed that the project was no longer the economically advantageous proposition anticipated last autumn.

Mr Spring said he was astounded. The public perception, north and south, was that a deal had been concluded last autumn, and that (irrespective of the present legal position - Mr Spring seemed aware that the Memorandum of Understanding (MOU) is not, strictly, binding) the public would expect it to go ahead - particularly after its endorsement at the Chequers Summit. Mr Spring and his officials said they could not understand that the current problems were not foreseen in the protracted and detailed negotiations that preceded the MOU. There was in any case a review clause in the MOU - why not wait until the first review in 5 years time? And was our market assessment to be relied upon: vigorous marketing was surely the key? Moreover, they added, we should understand that any cut in the price of gas would break the Irish Government's firm policy of selling the gas at a price that would enable them to replace it eventually with oil.

/...

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Mr Butler stressed that we were as unhappy as the Irish at the turn of events. We were satisfied that the market assessment was realistic (it had been confirmed by a separate assessment by the prospective private sector investor), and it was in any case only one of three adverse changes we had to face. The assessment took account of Northern Ireland's recent vigorous promotion campaign for natural gas, and there was no reason to believe that future marketing efforts would improve the expected sales. We could not rely on the 5 year review because the MOU required the agreement of both parties to any change. Neither Mr Spring nor Mr Butler could bind their successors on the decision to be taken in 5 years time. We realised that concessions now by the Irish would conflict with their policy on replacement by oil, but that was a measure of the seriousness of the situation - further contribution by HMG to the financing of the project would be equally painful.

We had, he said, to face up to the facts now before us. Was the Irish Government willing to make a move to save the project? If so, HMG would consider what moves it could make - although it would be a major departure from our normal practice, and would represent a considerable cost, we might be able to consider disregarding the capital costs of the project if the Irish could make a similarly generous move. Mr Butler made it clear that a major movement of price would be necessary, but did not quote a specific figure in pence per therm (thus avoiding any implication that HMG would be likely to settle for that amount). But Mr Butler emphasised that it would be essential for HMG, if the project continued, that it should be in the reasonable expectation that it would recover all its operating costs. He suggested to Mr Spring that it should be possible to devise some arrangement whereby the benefit of any movement more favourable than those currently anticipated by HMG should not accrue solely to us.

Mr Spring said that his Government had not had occasion to consider Kinsale Gas in Cabinet since last autumn. He could not therefore respond to Mr Butler today, but would report to Dr Fitzgerald, and the Government would no doubt discuss the issue at its meeting tomorrow, after which Dr Fitzgerald might well want to raise it with the Prime Minister.

In response to a question from Mr Spring, Mr Butler confirmed that the Prime Minister and senior colleagues were aware of the difficulties that had arisen, and had authorised the approach he was making to Mr Spring.

The Irish clearly appreciate now the urgency of coming to a conclusion on this: and they should now understand that the magnitude of the changes in circumstances requires a major movement on their part if there is to be a chance of the project going ahead. In view of the replies to my Secretary of State's minute of 22 June we have not discussed with the Irish the size of the movement we want from them: but if the Irish will not agree to something equivalent to at least 5p off the present price of the gas, the project is unlikely to be able to recover its operating costs.

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CONFIDENTIAL

CONFIDENTIAL



The next move is for the Irish. Mr Spring has promised to keep in touch with Mr Butler, but the next contact may be from Dr Fitzgerald to the Prime Minister. If so, Dr Fitzgerald seems likely to argue that it is politically too late, and too dangerous for Anglo-Irish relations, to let the project fail. The key question is then whether Dr Fitzgerald is willing to agree that the Irish should make a major concession on the price of gas (not less than 5p per therm); he will not agree to this if he believes the Irish are being asked to carry the whole burden of the changed circumstances. He may therefore seek an understanding from the Prime Minister that HMG would be willing to make a significant contribution - perhaps on the lines of disregarding some or all of the £140m capital expenditure on the project.

I am copying this letter to the Private Secretaries to members of E(A), the Foreign and Commonwealth Secretary, and to Sir Robert Armstrong.

Yours sincerely,

Graham Sandiford

G K Sandiford

CONFIDENTIAL

CONFIDENTIAL

E(A)

289

file



Ant DTI
D/En. CDHO
SO D/Eng.
WO MAFF
DOE CSO, ANT
LPSO DTTrans.

bc: Nick
Owen
+ Fco
CO.

10 DOWNING STREET

From the Private Secretary

3 July 1984

KINSALE GAS

The Prime Minister has seen your Secretary of State's minute of 22 June and subsequent minutes from the Chancellor of the Duchy of Lancaster, the Foreign Secretary and the Chief Secretary. She has noted the substantial deterioration in the economics of the project but believes the right course is to seek to renegotiate the terms. This should be done, however, in the knowledge that there is a point beyond which the UK cannot go and that it may ultimately be necessary to withdraw from the project. When revised terms have been renegotiated, the Prime Minister would like them to be put back to colleagues for decision on whether to proceed or to cancel.

I am copying this letter to the Private Secretaries to the members of E(A), to Len Appleyard (Foreign and Commonwealth Office) and Richard Hatfield (Cabinet Office).

Andrew Turnbull

Derek Hill,
Northern Ireland Office.

CONFIDENTIAL

289AAU

ECL

PRIME MINISTER

KINSALE GAS

Mr Prior's minute of 22 June reported the deterioration in the economics of the Kinsale Gas project. He set out three options - cancellation, perseverance and renegotiation. The Foreign Secretary recommends renegotiation though acknowledges that it might be necessary ultimately to cancel the project. To cancel the project without attempting further negotiation would have serious political disadvantages. The Chief Secretary believes that there is no genuine prospect that the economics of the project can be restored by further negotiations and recommends cancellation now.

Mr Prior's paper implies that renegotiation and cancellation are alternatives. In practice, these could be two stages in the same process. It would be important to enter further negotiations with a minimum objective which, if not achieved, would lead to cancellation. To enter negotiations knowing that the project would be retained come what may would be very dangerous particularly if this were ever known by the Opposition.

(i) Agree that the negotiations be attempted but in the knowledge that there is a price beyond which we cannot go?

Yes no

(ii) Agree that after renegotiation the terms be put to colleagues for approval?

Yes no

AT

2 July 1984

cc NO

CONFIDENTIAL



FROM: CHIEF SECRETARY
DATE: 29 June 1984

PRIME MINISTER

KINSALE GAS

I have seen a copy of Jim Prior's minute of 22 June to you.

When we discussed Kinsale Gas last September, we made a finely balanced judgement - that social and political factors were sufficient to justify proceeding with what was, at best, a project of marginal viability. Since then, the scales have been tipped decisively against the project. As an illustration of the scale of the shift, I understand that the price to be paid for Kinsale gas is now 35p - 39p a therm and that this would have to be reduced by 15p, even to regain the marginal viability we thought we had last September.

Jim Prior argues that if the £14m that would have to be spent closing the gas industry (in the event of our dropping the Kinsale gas project) is deducted from the cost of Kinsale gas, then he has only to reduce the price by 4p a therm to achieve a positive return.

But we cannot accept this analysis. An appraisal of the project on its own shows it to have a negative return. If we are to take account of the project's associated public expenditure savings (from avoiding closure), as Jim argues, then we should also take account of its associated public expenditure costs - namely the increased electricity subsidies that will be necessary because gas will reduce electricity sale revenue. A full public expenditure analysis (as was carried out before) would have been helpful - and would almost certainly show that closure is the cheaper option.

CONFIDENTIAL

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If we accepted the objective of a 4p per therm reduction in negotiation, therefore we would be:

- i) Accepting that Kinsale gas would never be viable;
- ii) Setting up a second subsidised energy undertaking in Northern Ireland, which would compete with electricity in a way which will increase the subsidies to both;
- iii) Accepting a gas price which was well above recent international agreements, including our own hard fought negotiations with Norway over the Sleipner Field; and
- iv) Weakening our negotiating position over future gas deals.

If Jim were able to argue that there was a chance of achieving a 15p reduction in the price of Kinsale gas, (ie. enough to restore it to, at least marginal viability) I could see that social and political considerations might justify making the attempt.

But if there is no realistic chance of this, then I think it would be wrong to prolong the uncertainty by attempting renegotiation. The project cannot be viable under the most optimistic outcome of such negotiations and we should drop it now.

I am copying this minute to other members of E(LA), Geoffrey Howe, and Sir Robert Armstrong.



PETER REES

CONFIDENTIAL



D/F with Treasury
response

CE/NO
AT 28/6

PM/84/109

PRIME MINISTER

Kinsale Gas

1. I am responding to Jim Prior's minute of 22 June setting out the three options we have open to us. As Jim demonstrates, all have drawbacks.
2. Simple cancellation would lay us open to serious charges of bad faith, and would damage Anglo-Irish relations at a particularly delicate time.
3. I also agree that we cannot accept the pricing structure as at present negotiated. We have consistently held - and the Irish know this - that the viability of the project must be decided on its commercial merits. If the project goes ahead on the present basis it will require continuous subsidy from British public funds and lack all credibility as an example of North/South economic cooperation. This would antagonise the moderate unionists who originally gave the project cautious support (Ian Paisley has always opposed it) and prove to be a source of continuing friction in Anglo/Irish relations.
4. To attempt re-negotiation on the lines suggested in Jim Prior's minute is the only possible course. But we must consider its chances of success coolly. Although Garret FitzGerald's coalition government will unite with its Fianna Fail opposition to condemn us if we cancel the project Fianna Fail are unlikely to miss the opportunity of attacking the Irish Government for mishandling the affair. The Irish Minister with direct responsibility for Kinsale, Mr Spring, is particularly vulnerable following his party's debacle at last week's European elections. It is just possible that at the end of the day the Irish would be willing to give way on price per therm if they could point to the £141 m British capital contribution. But we cannot be sure. Kinsale Gas's survival does not depend on it



being able to sell to the North, and Mr Spring and the rest of the Irish Government may see political advantage in standing firm and blaming the British if the negotiations fail.

5. We should obviously make great efforts to avoid such an outcome, but not to the extent of accepting manifestly uncommercial terms. If we are in the end obliged to cancel we should attempt to soothe the Irish by offering to join them in exploring other possibilities for economic cooperation in the energy and other fields.

GEOFFREY HOWE

Foreign and Commonwealth Office

28 June, 1984



Chancellor of the Duchy of Lancaster

CJP
 BP with Treasury response
 AT 26/2

PRIME MINISTER

KINSALE GAS

still
 with AT?

1. I refer to the Northern Ireland Secretary's minute to you of 22 June.
2. Part of the "fresh price proposals" which "met our requirements" as reported by the Northern Ireland Secretary in his earlier Memorandum of 7 September 1983 to E(A) was an increase in price on an April 1983 basis from 24.1 pence/therm to 27.1 pence.
3. It is not at all clear from the Northern Ireland Secretary's present memorandum what price we are now being asked to pay. But I suspect it is even more than the 27.1 pence. If it is, I would think that our minimum requirement for going ahead should either be the 4 to 5 pence reduction the Northern Ireland Secretary suggests or a roll back to the 27.1 pence. Perhaps it might also be interesting to compare the current Kinsale price with Sleipner.
4. It would need to be made clear to the Irish that if they were not prepared to agree, the deal was definitely off. Otherwise "renegotiation" would, as always, simply lead to an unsatisfactory outcome.
5. I am copying this to the other members of E(A), to Geoffrey Howe and to Sir Robert Armstrong.

A.C.

A C

25 June 1984

NO



Prime Minister:

Prime Minister

KINSALE GAS

I agree with the
conclusion that the
pursue Option (C)
not

Mr Prior proposes
renegotiating the Kinsale
gas contract. This may have
to go to E(A) but, in any
event, await Treasury response?

It
22/6

Following my minute of 7/June (not copied to all), I am writing to seek colleagues' agreement to modifying our approach to the Kinsale Gas project and to pursuing further negotiations with the Republic of Ireland.

Colleagues will recall that, with their agreement, a Memorandum of Understanding was signed in October 1983 for a supply of natural gas from Kinsale in the Republic of Ireland to Northern Ireland; it was expected that over a 32 year life the project would show a rate of return marginally above the 5 per cent minimum. We accepted at that time that the wider social economic and political advantages outweighed the undoubted risks of the project.

The Northern Ireland Gas Company Limited has been negotiating with its Irish opposite number about the detailed terms of the contract; a draft contract is now ready for signature. Since October, however, the prospects for the project have deteriorated significantly. Recent market surveys have shown a decrease in the potential sales of one-third (reflecting, inter alia, the rapid recent penetration of the domestic central heating market in Northern Ireland by solid fuel); the price of heavy fuel oil - which is the predominant element in the price formula - has risen substantially in relation to crude oil and is expected to remain at a higher level; and the exchange rate has moved adversely.

We have reassessed the project on the basis of this latest information; this reassessment demonstrates that there is now a real possibility of an outcome which would leave us with a substantial deficit at the end of 32 years as against the positive rate of return which we



accepted last year. Indeed, on the new market and price assumptions the project would not meet its operating costs even if we were to contribute, without expectation of return, the total capital cost.

Adam Butler has outlined these developments to Mr Spring, the Irish Minister of Energy, who expressed surprise and shock. Officials have had further discussions with the Irish, who have responded that we should not take a short term view of a long term project, having regard in particular to the notorious unreliability of energy forecasts. Their clear view is that we should put our current doubts to one side and proceed. Irish officials have also taken the firm line that there can be no question of any re-negotiation of price. The Memorandum of Understanding was of course neither an international Treaty nor a legal contract. Nevertheless, it is already clear from their public and private reactions that the Irish regard us as being strongly morally and politically bound by the terms of the Understanding, agreed as it was by both Governments.

Options

There is no realistic prospect that the Irish would make concessions of the magnitude required to restore the project to the degree of viability expected last year. This being so, the following options appear to be open to us:-

- a. Decide that we cannot proceed with the project because the forecast economic results are unacceptable.
- b. Conclude that the moral commitment is so great and that the political cost of failure to implement the project on the basis of the Memorandum of Understanding would be so high that we must proceed to sign the contract in spite of the adverse economics.
- c. Set out to close the gap in the viability of the



project as we now see it by attempting to renegotiate improved price terms from the Irish as well as displaying on our side a readiness to accept substantial costs as a direct charge on public funds.

Option (a) Cancel

There are strong reasons for not going ahead with the project. The latest assessment shows that the project does not meet the criteria for viability on which we based our decision last year and on which we have set such public store. If the projections now made prove to be an accurate forecast of the development of demand and the movement of oil prices over the next three decades, then the project would, at a 5% discount rate, have a net present value of - £107m. The project would not run into annual surplus for the first time until 1999/2000, after reaching a peak funding requirement of £170m in the previous year. On the other hand, if we decide to withdraw from the deal on the basis of these results we will be exposed to charges of extreme bad faith. We have of course been careful to avoid any legal obligation. If we did cancel the project we should seek ways of easing the resentment on the Irish side by offering wide-ranging discussion on energy issues.

Option (b) Proceed

The case for proceeding has to be based on an acceptance that we have some moral obligation to follow on from the Memorandum of Understanding. Additionally, this course has the advantage that some jobs in the gas industry will be secured and consumers will retain an additional fuel option. On the other hand, we have always stated that this project was going forward on the basis that it was viable and in the genuine interests of both parties. The latest assessment shows we can no longer be confident that this is the case for Northern Ireland.

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Option (c) - Re-negotiate

There is of course a possibility that the Irish might agree to abate the purchase price of the gas. If we made an irrecoverable contribution of £152m (or £122m - net of assumed EC aid) which would be equivalent to the capital costs of the project we would require an abatement of 4.5p per therm from the Irish to cover operating costs. If the UK Government were willing to make a contribution to the project equivalent to the amount (£141m) which we would have to pay to secure the orderly closure of the existing gas industry, a 4p abatement from the Irish would be needed.

There is no indication yet that the Irish would be willing to make such concessions - but I believe we would be wrong not to approach them. If they refuse, it is difficult to see any rational basis upon which we could continue with the project - but we would have made a major effort to preserve it and this would help us in handling the strong criticism we will face (in the Republic, from the Nationalist community in Northern Ireland and from the Opposition) if the project is cancelled.

It is of course arguable whether we should even be willing to meet capital costs in this way. It conflicts with our normal approach to investment analysis. On the other hand, it is widely known that the Government estimates the costs of closing the existing industry at around £140m and most observers, as well as those in Northern Ireland and the Republic who have an interest, take it for granted that in our assessment of the project we will disregard this £140m which we would have to spend in any case. To our critics, and I think to our supporters, it will seem better to spend the £140m to assure the establishment of a new energy industry with the social, economic and political benefits accruing from that decision, and in the process to maintain the goodwill of the Irish at a sensitive and difficult time, rather than to spend such a sum for the negative purpose of closure. It is on this basis that we would publicly defend a decision to meet the capital costs.

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/.... Conclusion



25 JULY 1894

Conclusion

Time is against us. There is predictable pressure from the Irish to sign the supply contract; but more important, there is a tight timetable within Northern Ireland for bringing the first gas deliveries to the Province by end 1985, and if this work is delayed, the first deliveries will slip badly, further affecting the economics of the project if we do not take a firm decision soon. There is therefore no time for lengthy renegotiations.

There are major political sensitivities whatever decision we take; but on balance I believe our best course is on the lines of option (c). If colleagues agree with this, Adam Butler will seek an immediate meeting with Mr Spring in order to:-

- a. Explain to him the unexpected nature of our new market and oil price forecasts and the implications of these on our project evaluation.
- b. Confirm that we continue to attach importance to the project but that it must, at the minimum, meet its operating costs. In order to achieve this objective we are willing to meet its capital cost but we still need a price reduction equivalent to 4 to 5 pence per therm (at 1984 prices).

I am copying this minute to our E(A) colleagues, to Geoffrey Howe, and to Sir Robert Armstrong.

J. P.

Ineland
econ

5179
Co-opⁿ

22 JUN 1994





PRIME MINISTER

Andrew.Kinsale Gas.

NIO phoned following amendments: -

line 3: should read "If we made an irrecoverable contribution of £152m (or £122m net of assumed EC aid)...."

line 9: "The £141m would also be net of EC aid...
" onwards to end of the paragraph should be deleted.

Sue

0216.

CONFIDENTIAL

RG ECU



cc Mr Pascall

10 DOWNING STREET

From the Private Secretary

11 June 1984

PROPOSALS FOR SUPPLY OF NATURAL GAS
TO NORTHERN IRELAND FROM THE
REPUBLIC OF IRELAND

The Prime Minister has seen your Secretary of State's minute of 7 June and has noted the line which Mr Butler proposes to take in the House today. She looks forward to a further report in due course.

I am copying this letter to Len Appleyard (Foreign Office), David Peretz (Treasury), Michael Reidy (Department of Energy) and Richard Hatfield (Cabinet Office).

Andrew Turnbull

Derek Hill, Esq.,
Northern Ireland Office.

CONFIDENTIAL

5779
Ireland
Econ Co-op

de NO

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NBPM
AT
11/6

FCS/84/166

SECRETARY OF STATE FOR NORTHERN IRELAND

Proposal for the Supply of Natural Gas to Northern Ireland
from the Republic of Ireland

with
HSC

1. I have seen your minute to the Prime Minister of 7 June about the prospects for the Kinsale Gas project.
2. Although we obviously cannot ignore the economic realities, I naturally share your concern for the adverse effect cancellation of the project at this stage would have on Anglo/ish relations.
3. I would be happy to discuss the problem with you after Adam Butler has seen Mr Spring. In the meantime, I agree that Adam should take as neutral a line as possible in the House on Monday, 11 June.
4. I am sending a copy of this minute to the Prime Minister, Chancellor of the Exchequer, Secretary of State for Energy and Sir Robert Armstrong.

(GEOFFREY HOWE)

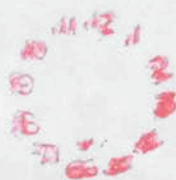
Foreign and Commonwealth Office

11 June 1984

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Ireland 5179 Econ
Co-opⁿ

08 JUN 1984



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1. CP to note
2 CF



cc DP
Prime Minister ②
To note at this stage
AT 8/6
MS

Prime Minister

PROPOSALS FOR SUPPLY OF NATURAL GAS TO NORTHERN IRELAND FROM THE REPUBLIC OF IRELAND

1. I am writing to warn colleagues of the serious and unexpected difficulties that have recently emerged for the Kinsale Gas Project.

2. In September 1983 colleagues in E(A) agreed that the project to supply natural gas to Northern Ireland should go ahead on the basis of outline terms and conditions of supply negotiated with the Republic of Ireland. Last year's economic evaluation, about which relevant Whitehall Departments were fully consulted, showed that the project was at the margins of acceptability. However, when other social political and economic factors were taken into account, colleagues agreed with me that the balance of advantage lay with concluding the deal. In October 1983 Adam Butler and his counterpart in the Republic signed a Memorandum of Understanding which provided the framework for implementation action. Since then the respective gas supply authorities (the Republic's Irish Gas Board and the Northern Ireland Gas Company Limited) have been engaged in detailed contract negotiations and have now reached the stage where a draft contract is ready for signature, subject to the approval of both Governments.

3. In parallel with these contract negotiations further work has been undertaken to reassess and refine forecasts and estimates in order that decisions could be taken on the organisational structure of the Province's gas industry and the nature and extent of any private sector participation in it. This process also provided the opportunity to re-examine and update the economic assumptions related particularly to gas purchase price forecasts. The two main results arising from this reassessment are that (a) the price of gas is likely to be higher than previously estimated primarily

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because of revised assumptions about the relationship between the prices of heavy fuel oil (the predominant element in the price formula) and crude oil and (b) the latest market forecasts are significantly less optimistic than those on which the 1983 evaluation had been based. The combined effect is to make the project non-viable by accepted standards and therefore, in the absence of Government subsidies, to render it completely unattractive to private sector interests.

4. Time is against us in this project. The Republic's Government is pressing for early signature of the supply contract which has been framed on the assumption that sales will be much higher than now estimated. The engineering consultancy and other commitments associated with implementation of the project are increasing steadily. The existing town gas industry requires early decisions on restructuring and the extent of gas supply in order to relieve the continuing and damaging uncertainty about its future. And there is the ever-present risk that our latest difficulties will become public knowledge and will therefore require responses in advance of a controlled statement describing the Government's stance.

5. I am in no doubt that we must in these circumstances defer any decision about signing a binding contract until we have had an opportunity to discuss urgently with the Irish the implications for both of us of our latest evaluation. I would envisage that Adam Butler should undertake this directly with the Irish Energy Minister, Mr Spring and I have instructed the Permanent Secretary of the Northern Ireland Department of Economic Development to contact immediately his opposite number in Dublin to prepare the ground. We shall have to test the willingness of the Republic to contemplate any adjustment of the terms embodied in last year's Memorandum of Understanding. I think it unlikely, however, that any adjustment that they would be willing to make would be adequate to give us confidence that the project could now be undertaken on commercially attractive terms. We would then have to consider whether it should nevertheless be undertaken on the best terms we can get.

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At that stage, we shall have to weigh the political consequences of alternative courses alongside the financial and economic ones. The political risks would certainly not all run in one way. A decision not to proceed at this late stage would inevitably cause some damage to cross-Border relations, and we would have to consider what ways might be open to us to limit and contain such damage. On the other hand a decision to proceed in the face of harsh economic realities, and at the price of significant extra public expenditure, after repeated assurances that we did not intend to establish a non-viable gas industry, could expose us to criticism from other quarters.

6. Adam Butler, who is at present in the United States on an industrial promotion exercise will have to take a Northern Ireland Appropriation Order Debate on Monday 11 June. It will not be possible for him to avoid reference to the natural gas project. It would, of course, be premature to reflect to the House the difficulties we now have with the project before Adam has had a chance to talk to the Republic. Insofar as reference to it is necessary, Adam will take as neutral a line on the future of the gas project as is possible in the circumstances.

7. I will report further to colleagues as soon as possible. I am sending copies of this minute to Geoffrey Howe, Nigel Lawson and Peter Walker, and to Sir Robert Armstrong.

Doyle

J. P.

7 June 1984.

(Approved by the Secretary of State and signed in his absence).

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Ireland
Ecom Co-operation May 79



07

104



016
From: THE PRIVATE SECRETARY



NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

David Barclay Esq
10 Downing Street
London SW1

7 October 1983

PA

Jms
10/10

Dear David

SUPPLY OF KINSALE GAS FROM THE REPUBLIC OF IRELAND TO
NORTHERN IRELAND

On Monday 10 October 1983 Mr Adam Butler MP and Mr John Bruton TD will sign the Memorandum of Understanding drawn up between HM Government and the Government of the Republic of Ireland concerning the supply of gas to Northern Ireland from the Kinsale Field. I enclose a copy of the main press release to be issued following the signing ceremony.

A copy of this letter and enclosure goes to the Private Secretaries to E(A) Members and to Robert Hatfield.

Yours ever

Dave

D A HILL



Northern Ireland Office

Press Notice

Great George Street, London, SW1P 3AJ. Telephone Enquiries 01 - 233 - 4626
Stormont Castle, Belfast, BT4 3ST. Telephone Enquiries Belfast 63011

10 October 1983

AGREEMENT ON KINSALE GAS

Agreement to pipe Kinsale gas from Dublin to Northern Ireland was announced in Belfast today by Northern Ireland's Industry Minister Mr Adam Butler MP and the Minister for Industry and Energy in the Republic of Ireland Mr John Bruton TD.

The formal Memorandum of Understanding between the Governments of the United Kingdom and the Republic of Ireland contains the main terms and conditions under which the gas will be supplied to Northern Ireland. The agreement comes at the end of 2 years of complex negotiations and will provide the basis for the development of a new natural gas industry in the Province.

Both Ministers today described the formal signing of the Understanding as a very satisfactory outcome to the lengthy negotiations which had been hard and businesslike but which had always been conducted in an amicable fashion.

The Ministers said that the Understanding signed today would form the basis of a legal contract which would be drawn up between the Republic's Supply Board, Bord Gais Eireann (BGE) and a new gas body to be known as The Northern Gas Company Limited (NIGAS). The contract will extend for a period of 22 years up to 2006. The contractual terms to be concluded by BGE and NIGAS are a matter of commercial confidentiality but the gas price to the Northern Ireland gas authority is in line with other international gas prices.

/The...

The construction of the pipeline link from Dublin to Belfast will take about 2 years and both Governments have agreed that routing and design work on the respective sides of the Border should start at once. The United Kingdom Government will make a contribution of £5m towards the cost of the Dublin/Border section of the pipeline.

It is expected that the project will qualify for grant aid from the European Regional Development Fund and both Governments intend to make an early joint approach to the European Commission for such assistance.



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E9 OCT 1983

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CHANCELLOR OF DUCHY OF LANCASTER

TRANSPORT

MAFF

CHIEF SEC TSY

CABINET OFFICE

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10 DOWNING STREET

From the Private Secretary

5 October 1983

KINSALE GAS

The Prime Minister has seen your Secretary of State's minute of 4 October which reports the improvements in the terms of the agreement with the Republic of Ireland. She is content that the Heads of Agreement should be signed and announced.

I am sending copies of this letter to the Private Secretaries of E(A) Ministers and to Brian Fall (Foreign and Commonwealth Office).

Andrew Turnbull

Derek Hill, Esq.,
Northern Ireland Office.

CONFIDENTIAL



Prime Minister ①

Yes
mt

Agree to conclusion of deal
subject to colleagues? Still outstanding
from E(A) will then be study of NIES
generating strategy, with aim of
reducing electricity subsidies.

PRIME MINISTER

KINSALE GAS

AT 4/10

At E(A) on 14 September colleagues agreed that the project should go ahead on the proposed terms subject to any further marginal improvements which might prove negotiable with the Republic.

I am pleased to be able to report that in further discussions with the Republic, Adam Butler has been able to secure enhancement of the terms as follows:-

- (i) the contract offered by the Republic will be extended from 20 to 22 years;
- (ii) the Northern Ireland contribution towards compression capital costs in the Republic will be £2½m rather than the sum of £5m previously proposed; this contribution will not become due until the first delivery date of gas but will be indexed from the signing of the Heads of Agreement on the basis of the United Kingdom retail price index;
- (iii) there will be an exchange of letters which will inter alia provide an assurance of best endeavours to maintain the initial contract terms when we reach the stage of renegotiation.

Peter Walker was particularly concerned that the details of the deal with the Republic should remain confidential, particularly in relation to the matter of price. The Republic has agreed that a confidentiality clause should be added to the Heads of Agreement and this will ensure that details will be revealed only

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by mutual agreement. Needless to say we will discuss with Department of Energy any proposals for disclosure of aspects of the terms of the agreement.

Formal texts covering all the terms of supply as agreed between Adam Butler and John Bruton have been drafted at official level and these will constitute formal Heads of Agreement when signed by Ministers of both Governments. The Heads of Agreement will then be the basis for a formal contract between NIGAS (the Northern Ireland company to be created which will handle the pipeline) and the relevant authority in the Republic of Ireland.

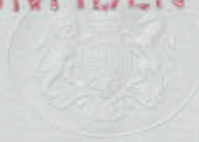
The way is therefore clear formally to sign and announce the Heads of Agreement. I would propose that this should be completed as soon as possible - Monday 10 October has been identified as a possible date and the venue would be Belfast.

There are sound reasons for making haste. The announcement of agreement, and the subsequent promotion of natural gas, will arrest the haemorrhage of customers from the existing industry. Each month the industry loses 300 customers or 0.3%. Furthermore the longer we delay beginning to introduce the new industry, the longer we will continue to pay nearly £1m each month in subsidies to the existing uneconomic undertakings. There are also political considerations; in that regard, I would wish this sensible deal to be presented for what it is - a practical example of cross-Border co-operation, nothing more. The longer we delay the announcement the more difficult it would be to keep the agreement confidential and leaks in advance of the announcement will allow those so inclined to present the deal, in the absence of the full facts, as a political measure inimical to the continued existence of Northern Ireland.

Adam Butler and John Bruton as chief negotiators would sign the Heads of Agreement and jointly announce the outcome. Both Ministers have major economic responsibilities and will be able

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to underline the significance of the project as an example of economic co-operation between the Republic of Ireland and Northern Ireland.

My officials will be in touch with your office, with FCO and with the Department of Energy about the text of the announcement and about press briefing.

A copy of this minute goes to E(A) colleagues and Sir Geoffrey Howe.

Derek Allitt

J P

(Approved by the Secretary of State and signed in his absence)

4 October 1983

CONFIDENTIAL

IRELAND: Supply of Natural Gas
May '79



4 OCT 1983



Prime Minister (4)

A report of E(A)'s

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Discussion and

conclusion to go ahead

with the Kinsale purchase

(at 27p a therm).

mes 2079

PRIME MINISTER

KINSALE GAS

At their meeting on 14 September (E(A)(83)4th Meeting) the Ministerial Sub-Committee on Economic Affairs considered a memorandum (E(A)(83)9) by the Secretary of State for Northern Ireland seeking endorsement for an agreement with the Republic of Ireland for the supply of natural gas to Northern Ireland from the Republic's Kinsale field on the revised terms now available.

2. Ministers had agreed in November 1982 that the proposal should go ahead on the basis of terms which were discussed the previous May. Since that date, however, the Republic had put forward revised terms, some of which were less satisfactory. Whereas under the previous terms the effects of fluctuations in the sterling/dollar exchange rate were to be shared equally by the parties, the Republic was now to have full protection against a fall in sterling against the dollar although the United Kingdom would stand to gain from any appreciation of sterling. The new formula would produce a gas purchase price of 27p per therm, if applied in April 1983, compared with 24p under the original proposals. This price nevertheless was in line with current international prices. Since last year, however, the Department of Energy's common economic assumptions, which were used for the financial and economic appraisal of the project, had also been changed. In particular, the new assumption for long term increases in electricity tariffs was for an annual increase of 2 per cent in real terms whereas in the 1982 appraisal it was assumed that tariffs would remain constant in real terms. Both the revised terms and the changed economic assumptions had altered the results of the financial and economic appraisal over the period to 2014/15. Although it was now estimated that there would be a resource cost saving of £316 million over 12 years, the rate of return was projected to fall from 6.9 per cent to 5.2 per cent (or 5.4 per cent if the Republic agreed to some marginal concessions). The PSBR effect over the 30 year period was now estimated to be adverse to the extent of £244 million rather than favourable to the extent of £287 million, these unfavourable effects arising largely in the third decade. The main explanation of



the less favourable outcome for the PSBR was that the change in the assumption about electricity tariffs had increased the projected loss of revenue of the Northern Ireland Electricity Service (NIES).

3. The Secretary of State for Northern Ireland argued that, notwithstanding the change in the terms, and the revised economic assumptions, it would still be desirable to go ahead with the project. The present Northern Ireland town gas undertaking was not viable. Its replacement by a natural gas industry based on supplies from Kinsale would be a more cost effective way of meeting energy demand than closure of the Northern Ireland gas industry and reliance on increased supply from other sources of energy. The project would provide employment, and the availability of natural gas supplies would help to attract industry to Northern Ireland. If the project did not go ahead, there would be pressure in the Northern Ireland Assembly to maintain a gas industry by other means, for example by supply from Scotland, which would be less economic. Failure to reach agreement would sacrifice a useful opportunity for practical cross-border cooperation and would have an adverse effect on Anglo-Irish relations. The Secretary of State for Northern Ireland undertook to accommodate the cost of the programme within the totality of the existing allocation to the Northern Ireland programme.

4. In discussion, it was pointed out on the one hand that the project would increase the subsidies required for the NIES arising out of the Government's undertaking expressed in a statement which you made in March 1981, that Northern Ireland electricity prices would not be increased beyond the highest level of electricity prices in Great Britain. The estimated first year of surplus for the project was Year 11 and a cumulative surplus would not be attained until Year 23; this lessened the chances of private sector involvement in the Northern Ireland gas industry.

5. It was argued on the other hand that Northern Ireland consumers could reasonably expect to be allowed access to Kinsale gas as a more economical supply of energy than existing sources. The social and employment effects, which had not been reflected in the financial and economic appraisal, would be beneficial. There were substantial political advantages within Northern Ireland,

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for Anglo-Irish relations, and in improving overseas perceptions of the Government's policy in Northern Ireland.

6. The Sub-Committee therefore agreed that the project should go ahead on the terms proposed, subject to any further marginal improvements which might prove negotiable with the Republic. They also agreed that, within the terms of the Government's commitments on electricity prices in Northern Ireland, it would be desirable to explore what economies might be made in the operations of the NIES, for example by reviewing its generation strategy, with the aim of reducing the cost of the electricity subsidies.

7. I am sending copies of this minute to the other members of the Ministerial Sub-Committee on Economic Affairs, the Minister of State, Foreign and Commonwealth Office (Lady Young) and to Sir Robert Armstrong.

(N.L.)

16 September 1983

Ireland
Economic Co-operation
between N.Ireland & the
Republic of Ireland

May 79



20 SEP 1983

COMPTON

Mr. Fletcher

E(A) Kinsale Gas

Core of the discussion will be as follows:

The proposal that Northern Ireland should purchase gas from the Republic's Kinsale field was approved in principle in November 1982. Since then currency movements and increasing costs to the taxpayer have made the economics of the scheme very marginal. The Treasury are therefore proposing that it should not be proceeded with. Other Ministers will agree that the need to ~~supply~~ assure Northern Ireland's energy supply (currently town gas) and the demonstration of politico/economic cooperation with the Republic make the scheme still worthwhile.

PM 7/9



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10 DOWNING STREET

From the Private Secretary

24 December 1982

COAL DEPOSITS IN NORTHERN IRELAND

Thank you very much for your letter of 23 December about coal deposits in Northern Ireland.

I showed this to Mrs. Thatcher. She was most grateful for the work that had gone into it.

M. C. SCHOLAR

D.A. Hill, Esq.,
Northern Ireland Office.

From: THE PRIVATE SECRETARY



NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

Michael Scholar Esq
Private Secretary
No 10 Downing Street
LONDON SW1

Prime Minister (2)

You asked

23 December 1982

about this.

Ms 23/12

Dear Michael

You wrote to John Lyon on 15 December about the Prime Minister's enquiry about coal deposits in Northern Ireland.

Unfortunately there are no known commercially exploitable reserves of hard coal in Northern Ireland. Small seams were worked in the nineteenth and early twentieth centuries at Ballycastle and Coalisland - but both deposits petered out in the early part of this century. There has however been recent publicity about lignite deposits on the Eastern shore of Lough Neagh. Although their existence has been known for many years and samples were examined from time to time, the deposits were not regarded as worthy of commercial exploitation until recent times.

A mineral exploration licence covering the area of the deposit is held by the firm Mining Investment Corporation (Mincorp) which is a subsidiary of Burnett & Hallamshire Ltd. The reserves of lignite which can be regarded as proven at this stage are nearly 100 million tons in two seams at depths down to about 500 feet. The site is on the edge of Lough Neagh with a high water table. At the moment the study of the hydrology of the area is incomplete and the results of that study will have very great significance for the financial viability of a mining operation.

At its recent half-yearly shareholders' meeting Burnett and Hallamshire made a very "bullish" presentation on the Northern Ireland lignite speculating that additional deposits located under Lough Neagh could raise the reserve to 400 million tons or 500 million tons and suggesting this could provide Northern Ireland's total energy demand for many decades. Our expert advice is that a statement on the extent of any deposit beyond the 100 million tons already proven can only be speculative. Even if there were additional deposits under the Lough the possibility of recovering them at economic cost is open to severe doubt at this stage. The bullish projection by Burnett and Hallamshire of the prospects for exploitation of the deposit is probably conditioned by their need to point to prospects for growth in the next decade at least as good as they have had in the last.

/...



For the record, lignite (which the company insists in its public presentation on calling "coal") is a less mature fuel than the normal hard coal mined in Great Britain. The lignite available at Crumlin will have a moisture content of around 60% when mined and will require to be dried to about 10% moisture content before it is ready for processing to the forms in which it is likely to be used. Some 2.6 tons of mined lignite will produce about one ton of dried fuel, with about two-thirds the calorific value of one ton of hard coal. For the purposes of a financial comparison with coal we can assume wet lignite might be mined at £10 per ton. Dried lignite would then cost around £26 per ton and for equal calorific value the purchaser would be paying a coal-equivalent price of £39 per ton. Any further processing of the lignite - pelleting, briquetting, pulverising - would add to the cost as would transport. In all the circumstances, finding the optimum use of the lignite resource involves examination in depth of a complex set of options. The Department of Economic Development has therefore commissioned a group of relevant consultancy firms under the co-ordinating umbrella of Coopers & Lybrand to report on the exercise from mining to end-use.

A copy of this reply goes to Julian West at Department of Energy.

*Yours ever
Derek A Hill*

D A HILL

Ireland. Economic Cooperation : May 79.

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10 DOWNING STREET

From the Private Secretary

15 December 1982

NATURAL GAS IN NORTHERN IRELAND

The recent correspondence about the proposal to bring natural gas to Northern Ireland from the Irish Republic has led the Prime Minister to enquire whether she is right in thinking that Northern Ireland has extensive but unworked coal deposits.

BAH
I would be grateful for a note on this subject.

I am sending a copy of this letter to Julian West (Department of Energy).

M.C. SCHOLAR

John Lyon, Esq.,
Northern Ireland Office

CONFIDENTIAL



Am I right in thinking
that Northern Ireland
has extensive but
unworked coal deposits?
mt

Prime Minister (2)

ms 4/12

Northern Ireland Office
Stormont Castle
Belfast BT4 3ST

The Rt Hon Leon Brittan MP
Chief Secretary to the Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

13 December 1982

Handwritten signature

Handwritten initials

Thank you for your letter of 30 November in response to my minute to the Prime Minister of 11 November about the proposals to bring natural gas to Northern Ireland from the Irish Republic.

I am grateful for your confirmation that subject to your provisos and to the attitude of our colleagues, you do not oppose the project going ahead.

As far as your provisos are concerned, I can confirm that PES costs will be borne within the existing Northern Ireland PES allocations.

As I explained in the opening paragraph of my minute to the Prime Minister, my objective was to establish a viable Northern Ireland gas industry. It is certainly not my intention that the industry should be subsidised other than in the transitional years until it moves into profitability as foreseen in the project evaluation. I am, however, sure that you do not expect me at this stage to guarantee against all future contingencies, nor to commit succeeding administrations.

I have no objection to officials discussing financial targets. On the assumptions used in the analysis, the Kinsale project yields an internal rate of return of 6.9% in real terms. As you know, I intend private sector involvement if at all possible and, if I am successful in this respect, financial targets would not be appropriate. If, however, you



feel that it would be helpful to plan against the possibility that the industry will remain completely in the public sector, I am content that we should do so.

I am sending copies of this letter to the Prime Minister and to other recipients of yours.

*Yours
Truly*

cc. PS/PJS (L+B)
PS/Sir E Bell
Secretary
MR Angley
MR Cole ✓
MR Burns
MR Alexander
MR Shepard
MR Stummond
MR Warnock



Ireland
Prime Minister (2)

MUS 30/11

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon James Prior MP
Secretary of State
Northern Ireland Office
Great George Street
London SW1P 3AJ

30 November 1982

R. J.

Thank you for sending me a copy of your minute to the Prime Minister of 11 November. I have since seen her reply of 15 November, and Nigel Lawson's minute of 25 November.

I have some reservations about this proposal:

- First, I see that it will lead to a sizeable increase in expenditure next year, especially if the gas is to be supplied throughout Northern Ireland as you prefer. The conclusion that it will save public expenditure depends on the forecasts for the period after 1990, which are bound to be very uncertain.

- Secondly, the forecasts assume that supply of Kinsale gas will make possible a five-fold increase in sales of gas in Northern Ireland. Indeed, such an increase is stated to be "necessary for a viable industry". But we cannot be certain that it will take place given the poor prospects for growth of energy demand, and the escalation of the price of Kinsale gas with the price of oil.

interruption

- Thirdly, there is clearly cause for concern about the security considerations. You quote your security advisers as saying only that these considerations 'would not be an insuperable obstacle' and that terrorist attacks are likely. The Prime Minister has referred to the possibility of intervention of supply.

- Fourthly, I have noted Nigel Lawson's reservations about the proposed terms of the deal with the Irish Republic.

Nevertheless, I accept that the project has important employment implications, and if colleagues generally are content, I would not want to oppose its going ahead, on these provisos:

- First, that any additional costs are borne within your PES allocation. I see that you have accepted this, and your acceptance helps substantially to deal with my worries.

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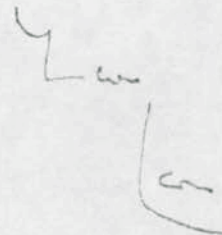
7 DEC 1968

- Secondly, I am concerned that there should be no question of Kinsale gas following the precedent of the Northern Ireland Electricity Service, whose price is of course subsidised at a level equivalent to the highest in Great Britain. I should be grateful to have your assurance now that the transitional subsidies provided for under the terms of your project, and due to be phased-out by 1987-88, will be the limit of Exchequer subsidy to the Northern Ireland gas industry.

- Thirdly, I should like to ask for your agreement that financial targets based on a percentage return on net assets, on the pattern of those we set for nationalised industries in Great Britain, should be set for the Northern Ireland gas industry. The industry as a whole is not projected to move into operating profit until 1988-89. But I should like to suggest that our officials should study, and report back to us on, the feasibility of setting annual deficit targets for the industry, which would plot a path to eventual profitability. I would envisage these targets being formally set for the industry, as is our practice for certain deficit industries in Great Britain such as British Rail.

I should be glad to have your agreement to these provisos.

I am sending copies of this minute to the Prime Minister and to other recipients of yours.



LEON BRITTAN

Ireland

Economic Co-operation

May 79

30 May 1982





Prime Minister (2)

MS 29/4

MS

Secretary of State for Energy

PROPOSAL FOR SUPPLY OF NATURAL GAS TO NORTHERN IRELAND FROM IRISH
REPUBLIC

I have seen a copy of your minute of 23 November to the Prime Minister.

I am glad that you accept the case made in my minute to the Prime Minister of 11 November concerning the supply of natural gas from the Republic of Ireland to Northern Ireland. For my part I fully understand your concern that any arrangements made in this deal do not cause problems for UK energy policy and it is for that reason that my officials have been in very close touch with yours during the negotiations and during the process in which we are now engaged of refining the Heads of Agreement. The expanded Heads which we are currently discussing with the Republic have, as you know, resulted from the advice of BGC and solicitors who were recommended to us by the BGC. Your officials have been kept in the picture and it is my intention that my officials and yours should remain in close contact through the remainder of the process. I see no difficulty in meeting the points made in your minute; indeed, most of them are already catered for. On the specific point you make about a supply of gas to the Republic, clearly there can be no question of our putting HMG under any obligation of that nature which did not have the specific agreement of Department of Energy.

Finally, I note your point about the wider significance of any EC assistance to the project and I will ensure that your officials and those of other interested Departments will be kept fully consulted on any developments.

I am/...



I am copying this minute to the Prime Minister, Members of E Committee and Sir Robert Armstrong.

A handwritten signature, possibly "JP", written in ink.

J P

29 November 1982



Ireland

②

Prime Minister

Some solid points here.To note.

Mes 23/11

Prime Minister

PROPOSAL FOR SUPPLY OF NATURAL GAS TO NORTHERN IRELAND FROM
IRISH REPUBLIC

I fully understand the political and economic case for the proposals contained in the Secretary of State for Northern Ireland's minute of 11 November. There are however several areas of concern to me, and I hope that close attention can be given to them before finalising the terms of the deal, as the draft Heads of Agreement attached to the minute contain only the barest outline of these terms.

My principal concern is that the terms should not be such that they are thought to endorse the upward trend of prices for gas traded internationally, which a number of producing countries have been actively seeking. This is particularly important at a time when the British Gas Corporation is entering negotiations for the purchase of Sleipner gas from the Norwegians. If these negotiations are successful, Sleipner gas will become as significant a part of supply to the British market in the 1990's as Frigg gas is now. While I do not wish to exaggerate the influence of the Kinsale terms, a poor deal would be unhelpful.

On the face of it, the price proposed for the Kinsale gas (taken with the escalation clause and including transmission costs and capital contribution) appears high in comparison with the prices for other internationally traded gas. It is not so far out of line however that I would wish to argue against acceptance in this particular case. But the conditions under which gas is supplied are crucial in determining the reasonableness or otherwise of a given price, and many of these are left open in the Draft Heads of Agreement. The following points in particular are not fully dealt with:

- The extent to which gas will be made available to meet peak demand in winter;
- the precise priority and cut-off arrangements for supply as between customers in Northern Ireland and the Republic;
- the financial provisions should demand in Northern Ireland grow more slowly than projected;

Ireland, May '79, Natural Cen.



29 Nov 1982



- the starting date, reference prices, formulae and other key conditions for escalation provisions.

I believe that these points are being discussed with the Republic but a satisfactory understanding will have to be reached on them before we can safely conclude that the proposed deal is reasonable.

I understand also that the Republic negotiators have proposed an exchange of side-letters, as part of which HMG would undertake to use its best endeavours, in the event that gas was not available to the Republic in 20 years time, to offer supplies which Northern Ireland may then have from "another source". Any such understanding would be most unwise. It would certainly constrain the Government greatly in relation to any possible decision to supplement gas supplies to Northern Ireland at a later date from the UK Continental Shelf, if we would thereby put ourselves under a contingent obligation to make a supply available to the Republic as well. I see less objection to a side-letter referring to gas discovered in Northern Ireland, but would much prefer any such understanding to be avoided altogether unless this is essential to finalising the deal.

Finally, I note that EC assistance is being sought for the project. Provided such assistance is made available under existing schemes (for example, the ERDF), I see no objection. If however the Commission were to propose a special instrument, this might provide a precedent for other special cases relating to gas pipelines or conversion of appliances to natural gas. In that event, we would need to weigh up very carefully the likely overall benefit to the UK of such a precedent being set.

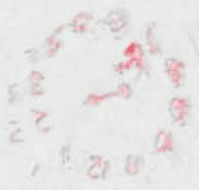
I am copying this minute to Members of E Committee and to Sir Robert Armstrong.

YL.

SECRETARY OF STATE FOR ENERGY

23rd November 1982

Ireland, May 79
Natural Gas to N. Ireland



23 NOV 1984

COMMUNICATIONS

LONDON



Foreign and Commonwealth Office

London SW1A 2AH

18 November, 1982

Dear Mike,

Proposals for Supply of Natural Gas to Northern Ireland from
the Irish Republic

Mr Pym has seen the Northern Ireland Secretary's minute of 11 November to the Prime Minister, and the attached memorandum. He agrees that the Kinsale project should go ahead on the terms agreed with the Irish Republic.

I am copying this letter to the Private Secretaries to the other members of E and to Richard Hatfield (Cabinet Office).

Yours ever

J E Holmes

(J E Holmes)

M Hopkins Esq
Private Secretary
Northern Ireland Office



IRELAND

10 DOWNING STREET

From the Private Secretary

15 November 1982

PROPOSALS FOR SUPPLY OF NATURAL GAS TO NORTHERN IRELAND FROM
THE IRISH REPUBLIC

The Prime Minister was grateful for your Secretary of State's minute of 11 November and the attached memorandum.

The Prime Minister agrees, subject to the agreement of colleagues, to your Secretary of State's proposal. She has commented that the heads of agreement and the contract will need to be carefully drafted against the possibility of intervention of supply.

I am copying this letter to the Private Secretaries to the other members of E and to Richard Hatfield (Cabinet Office).

M.C. SCHOLAR

Mike Hopkins, Esq.,
Northern Ireland Office.

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Prime Minister (1)

PRIME MINISTER

PROPOSALS FOR SUPPLY OF NATURAL GAS TO NORTHERN IRELAND FROM IRISH REPUBLIC

MS 12/11

Yes - we shall need some carefully drafted clauses of contract of supply not

In October 1981, colleagues agreed that we should open negotiations with the Government of the Republic of Ireland on a supply of natural gas to Northern Ireland from the Republic's field at Kinsale. The purpose of those negotiations was to establish whether the terms attaching to such a supply could provide the basis of a viable gas industry for Northern Ireland.

2. Agreement in principle has now been reached with the Republic for a supply of gas. The terms agreed were reached after lengthy and tough negotiations, and I am completely satisfied that the package which has been negotiated represents the best deal that could be obtained. I am now writing to seek colleagues' approval to going ahead with the project on the basis of these proposals.

3. The proposal will, in the long term, involve a substantial saving on public expenditure. Funds have already been allocated for the closure of the Northern Ireland gas industry (until we were offered natural gas from the Republic we were committed to closing the industry, and this remains the only alternative to accepting the natural gas), but, as the public expenditure analysis shows, a net present value saving of £140m over the 30 year period will result if we adopt the project instead of closure. During the current survey period there will be additional demands on public expenditure. However notwithstanding the difficulties and pressures I face I am prepared to meet these out of the Northern Ireland total recently agreed in the context of the 1982 PE Survey. I will be looking at the incidence of the capital expenditure critically and may have to provide natural gas for Belfast only first, with the remainder of Northern Ireland being phased in over a period of years.

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4. As the appraisals (agreed with the Treasury at official level) in the attached memorandum show, a supply of gas on the terms now available from the Republic would offer the basis of a profitable and viable gas industry which (unlike the present gas industry in Northern Ireland) would make no further financial calls on Government. The resource cost analysis shows that there is a clear advantage in meeting additional energy demands by introducing natural gas as compared to increasing the use of electricity, oil and coal. The financial analysis indicates that the natural gas project should yield an internal rate of return well in excess of our test discount rate of 5%.

5. If we do not proceed with the project we shall have to revert to our earlier, much criticised plan to close down the gas supply industry in Northern Ireland. Closure of the gas industry would have a significant impact on public expenditure and would result in a further and early loss of employment in Northern Ireland; it would deprive the region's industry of a piece of infrastructure which industrialists elsewhere take for granted; and it would seriously disadvantage the consumer by restricting his choice of fuels.

6. As it is organised at present, much the greater part of the gas industry in Northern Ireland is run by local authorities. The evaluation of the proposals which has been carried out assumes that an industry based upon natural gas from the Republic would continue to lie within the public sector and therefore that any profits would be retained within the public sector and would thus accrue to Government. However, although such a public sector project can be justified fully on grounds of viability, my objective is to secure private sector participation to the maximum extent possible and discussions to this end are being pursued. Obviously there are great advantages in the maximum private investment and with Adam Butler I am seeking from private investors an immediate and substantial capital contribution which would affect public expenditure in return for the profits foregone by the public sector in the later years of the project.

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7. The supply of natural gas would be drawn from the single source of the Kinsale field. Access to a multi-field system would have attractions but at the present time there is no opportunity to tap into additional sources, since a decision was made in 1979 on the basis of an inter-Departmental study that the natural gas would not be supplied to Northern Ireland from Great Britain. The known recoverable reserves of the Kinsale field, and the projected depletion rates, leave no doubt that the Republic will be in a position to meet its supply obligations to Northern Ireland under the terms of the agreement. Strategic storage facilities have been included in the project and would give protection against limited disruptions of supply.

8. There are important security considerations attaching to the project, particularly in the Border areas. The view of the experts is that the security problems can be overcome, and the plan includes provision for the necessary security precautions.

9. Within Northern Ireland, Catholic and Protestant representatives are likely to adopt different attitudes to a supply of natural gas based upon an agreement with the Republic. The Unionist parties have argued consistently for a pipeline link with North Sea sources via Scotland. Kinsale gas and other energy topics will almost certainly be the subject of considerable interest in the Assembly, where the Unionist parties are likely to make known the above views - although they, too, will be sensitive to any loss of jobs arising from a closure of the gas industry. Closure of the gas industry would draw opposition from all quarters.

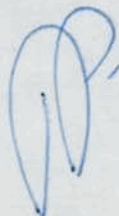
10. As far as our relationship with the Republic of Ireland is concerned, this project has consistently been treated as a matter of practical co-operation likely to be of real benefit to the United Kingdom, and to the Republic. I think this is the line we should continue to take. We shall need to take special care to ensure that no attempt is made to make party political capital out of the project in the period leading up to the Republic's General Election on 24 November.

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11. I am in no doubt that it makes sense financially, economically and politically to confirm that the United Kingdom Government is prepared to approve the purchase of natural gas on the terms provisionally agreed. This confirmation would be followed by the signature of Heads of Agreement with the Republic after which negotiations would proceed for the drawing up of a contract between the Irish supplying authority and a Northern Ireland purchasing organisation. Meanwhile, engineering and other preparations for the project would be progressed and proposals would be developed for the re-organisation of the gas industry in Northern Ireland to ensure that it is appropriately structured and managed to exploit the new source of supply.

12. I therefore commend to my colleagues the terms of supply which have been agreed provisionally. I recommend that these terms should be accepted, that the project for a natural gas industry in Northern Ireland should go ahead on the basis which they represent, and that officials should as soon as possible proceed as outlined in the preceding paragraph, assuming that confirmation of the agreement is forthcoming from the Government of the Republic.

13. I am copying this minute to 'E' Committee colleagues and to Sir Robert Armstrong.



J P

11 November, 1982.



KINSALE PROJECT

PROPOSALS FOR A SUPPLY OF NATURAL GAS FROM THE REPUBLIC OF IRELAND
TO NORTHERN IRELAND1. SUMMARY

- 1.1 The proposals to bring a supply of natural gas to Northern Ireland from the Kinsale field in the Republic of Ireland offer the last remaining alternative to the politically contentious and costly operation of closing the Northern Ireland towns gas industry. An agreement in principle for the supply of natural gas has been reached with the Republic after lengthy negotiations and this package represents the best deal that could be obtained. The terms of the agreement, when evaluated in conjunction with professional consultancy assessments of market potential and engineering requirements, show that on resource cost and financial analysis grounds there is a strong case for going ahead with the project. It may be possible to reduce the public expenditure implications of the project through the involvement of private funds.
- 1.2 The following paragraphs deal with the economic and public expenditure evaluation of the Kinsale proposals. They describe the background against which the proposals have developed, including the negotiations with the Republic, the present circumstances of the gas industry in Northern Ireland and some of the measures which will be required for the development of a successful industry based upon natural gas. Political considerations attaching to the proposals are also discussed.

2. BACKGROUND

- 2.1 In July 1979 the Government announced its conclusion that a supply of natural gas from Scotland did not hold out the prospect of providing the basis for a financially viable gas industry in Northern Ireland and that the provision of public funds for such a project could not be justified. The same announcement also made it clear that the existing towns gas industry would not be subsidised

on an on-going basis but that Government would be prepared to provide financial resources to facilitate the orderly run-down of those gas undertakings which decided to close. The estimated cost of such support is £147 million (October 1981 prices).

- 2.2 Arrangements for the run-down of the industry, including the necessary legislation, were well advanced when in the autumn of 1980 the then Administration in the Republic of Ireland indicated, for the first time, that it would be prepared to consider making natural gas available to Northern Ireland from the Kinsale field. Following preliminary assessments, negotiations were begun with the Republic in December 1981 on the main terms and conditions on which such a supply might be made available. Arrangements for the run down of the Northern Ireland gas industry were suspended pending the outcome of these negotiations.

3. NEGOTIATIONS WITH THE IRISH REPUBLIC

Negotiations with the Republic began in December 1981 and were interrupted by the Irish General Election of March 1982. Agreement in principle was reached in May 1982 between Adam Butler and the Irish Minister for Industry and Energy on terms which each felt could be recommended to their Ministerial colleagues. These terms, which are set out in Annex 1, have been incorporated in the detailed project evaluations. Officials are working with their counterparts in Dublin to translate these terms into a more complete form of Heads of Agreement appropriate for signature by Ministers and which would serve as the basis of a legally binding contract. This work is still in progress, but there are indications that the Republic side is willing to accept additions to the original terms which would provide significant further safeguards for the purchasing organisation in Northern Ireland. These improvements would be achieved without disturbance of the agreed price for the gas.

4. KEY ASPECTS OF THE KINSALE PROJECT

The following paragraphs deal with some of the characteristics and implications of the project:

- (1) The present gas industry in Northern Ireland is an amalgam of 13 disparate and generally inefficient undertakings, some public, some private, some profitable but most loss-making. They require high levels of Government support (of the order of £10 million pa). To switch to gas from the Kinsale field would involve making the transition from oil-based feedstock to natural gas, and establishing a viable and efficient industry.
- (2) The industry and Northern Ireland gas consumers have been burdened by considerable uncertainty about the future of gas for a number of years. The decision now being sought will eliminate this uncertainty and hopefully clear the way for the creation of a progressive and forward-thinking new industry.
- (3) Towns gas in Northern Ireland is at least twice as expensive for the consumer as natural gas in Great Britain and would be even dearer were it not for the Government deficit support which has been provided in recent years. It is estimated that the selling price of natural gas from Kinsale would be some 25%-30% below the equivalent of present Northern Ireland tariff levels. Gas prices in Northern Ireland would however still be above those applying in Great Britain.
- (4) In heat supplied terms, towns gas accounts for some 3% of all energy supplied to Northern Ireland consumers compared to 40% in the UK as a whole. In the domestic sector the respective figures are 4% and 53%.

- (5) Current towns gas sales in Northern Ireland are 21 million therms (70% in Belfast). The marketing consultants who have been retained to advise on the project envisage sales increasing to approximately 115 million therms by 2003/4, with the main load increase arising from domestic space heating. This expansion, which is necessary for a viable industry, could only be achieved with the support of a major marketing effort and significant increases in operational efficiency.
- (6) The capital cost of supplying natural gas to the existing gas undertakings in Northern Ireland is expected to be of the order of £147 million at October 1981 prices (coincidentally this equates with the estimate of the cost associated with closing down the gas industry.) This expenditure would include the costs of the main and supplementary transmission pipeline, strategic storage facilities for liquefied natural gas, compression equipment, conversion of the existing towns gas distribution system, equipment and appliances and expansion of the existing distribution network.
- (7) The most significant criterion used in the evaluation of the project has been the resource cost analysis. Priority has also been given to the financial analysis, and to the public expenditure comparison between Kinsale gas and the only other alternative, closure of the gas industry.
- (8) The project has been carried forward on the assumption that initial financial provisions will have to be met from the public sector. Efforts are continuing to attract private sector involvement.
- (9) A five to six-fold increase in gas sales over the next twenty years will have an impact on other fuel industries. Total demand for energy over this period is likely to be sufficient to accommodate the increased gas share of the market without eroding the position of other fuels. The coal industry in particular disagrees with this thesis. It takes the view that (a) the energy market will not increase significantly and (b) it is unfair that the coal sector should lose any of its share of that increase in the market to gas.



- (10) The advent of natural gas to Northern Ireland would require changes to be made to the existing structure of the gas industry in Northern Ireland. The extent and nature of any re-structuring is at present under consideration. The possibility of introducing a private sector involvement forms part of this consideration.
- (11) European Community assistance would be sought for this project. Commission officials have responded encouragingly to preliminary contacts. Almost certainly the project would qualify for assistance under the Regional Development Fund, and in addition the possibility is being pursued of some special form of assistance.
- (12) There are important security considerations attaching to the project, particularly in the Border areas. The view of the security advisers is that security considerations would not be an insuperable obstacle if it were decided to implement the Kinsale proposals. This view is however associated with the conclusion that the gas project would be an economic target and as such is likely to be the subject of terrorist activity, during construction as well as later. On the basis of this threat assessment the security advisers have therefore recommended certain physical protection measures involving very marginal increases in capital and operational costs which have been included in the evaluation. Arrangements are in hand for discussions on security considerations to continue as the project develops; these will certainly cover pipeline routing, depth of pipeline and other facilities, contingency storage and the co-operation of the Irish authorities.
- (13) If the project is approved, the earliest date at which gas could be made available in Northern Ireland would be in the second half of 1984. A contract with the Republic would initially be for a 20 year supply but there is the prospect of continued supplies beyond that period.



- (14) A decision to proceed with the Kinsale project would safeguard most of the 1,000 jobs in the gas industry and the construction work would in itself provide additional work within the Province.
- (15) Although the project is based upon the importation of gas and therefore has some balance of paymetns implications, it should be noted that the use of Kinsale natural gas would to an extent offset other, increasing, imports of fuels. The proposals would provide a part of the United Kingdom with a supply of natural gas without the penalty of faster depletion of finite North Sea reserves. They would also entail the maintenance and development of the infrasturcture of the gas industry within Northern Ireland in such a way as to enable the Province to utilise any indigenous resources which may become available in the future. The project is therefore compatible with important aspects of energy policy at the national and regional levels.

5. EVALUATION OF THE KINSALE PROJECT

- 5.1 The evaluation includes a resource cost analysis, a financial analysis and an examination of the public expenditure implications and has incorporated outside consultancy advice on the potential market for natural gas and on certain engineering costs.
- 5.2 The resource cost analysis makes a comparison between providing for a given energy demand by either introducing natural gas or increasing supplies of electricity, petroleum and coal. The comparison indicates that in resource cost terms the advantage lies in introducing natural gas since this results in a present value saving of £190m over 30 years.
- 5.3 The financial analysis sets out the total expenditure and income streams of the project over its lifetime in order to show the amount and timing of deficits and surpluses and hence to assess whether the project is likely to make an acceptable financial return. On the assumptions used in the analysis, the Kinsale Gas project yielded an internal rate of return of 6.9% in real

terms (the test discount rate for public expenditure has been assessed by HM Treasury at 5% in real terms).

5.4 The public expenditure analysis has recognised that there are two courses of action open to Government. On the one hand, a decision to bring in natural gas will automatically mean that the gas industry will continue in being while on the other hand a decision against a Kinsale project will entail closure of the gas industry. If the decision is against a natural gas project, the consequential closure of the industry will require expenditure by Government, to which it is already committed, under two broad headings:

- (a) grants amounting to £65 million to assist consumers to convert towns gas appliances to other forms of energy; and
- (b) transfer costs - deficit support and redundancy payments - amounting to a further £82 million.

5.5. If the decision is in favour of the natural gas project, PE implications arise only to the extent that the expenditure differs in amount or phasing to that already earmarked for closure of the existing industry. Assessed over a 30 year period and taking account of trading surpluses which are expected to accrue, introduction of natural gas results in a PE saving (compared to closure) of some £140 million. (Further details are given in Annex 2.)

The information which is provided at Annex 2 distinguishes between a supply of gas to Northern Ireland and a supply which would be confined to the Belfast conurbation and to locations along the route of the pipeline from the Irish Border. There is no financial advantage to HMG in confining a supply of natural gas to 'Belfast' and the resource cost and financial analyses are also neutral in this comparison. It would in any case be impossible to defend politically an exclusion of the North and West of the Province which would be seen as discriminating against some of the most socially and economically deprived parts of the United Kingdom.



6. POLITICAL IMPLICATIONS

- 6.1 All of the political parties within Northern Ireland actively opposed the Government's decision to close the gas industry. The Unionist parties have argued tenaciously and consistently in favour of a gas pipeline link from Scotland though this has long been rejected by Government on cost grounds. They regard the proposed supply from the Irish Republic as a very poor substitute for a connection with Great Britain and there are clear signs of opposition to the Kinsale project from Unionist sources amounting in some cases to rejection. By contrast, the mainly Catholic SDLP will see the Kinsale project as one to which they can lend full weight.
- 6.2 In the wider political context, a Kinsale gas link is the only major cross-Border project on the horizon which provides opportunity for securing practical economic co-operation of advantage to Northern Ireland. The Ministerial negotiations have been carried out under the aegis of the Anglo-Irish Inter Governmental Council and a decision to proceed would demonstrate the potential for co-operation between the UK and the Republic in technical matters where this would be of advantage to us.

7. PRIVATE SECTOR INVOLVEMENT

- 7.1 The possibility of private capital involvement has been pursued with a number of major oil companies but the only proposition currently on the table has come from the firm of Calor Kosangas. This firm has recently put forward a proposal which envisages a partnership with some (but not all) of the existing gas undertakings in the retailing of natural gas in Northern Ireland. Discussions with Calor Kosangas are proceeding in order to determine the extent of the managements willingness to contribute financially to the project. The association of a company with a proven commercial track record could be expected to strengthen the marketing capability of a new gas industry.



7.2 The interest expressed by Calor Kosangas relates solely to the retailing of natural gas. It does not extend to the transmission of the gas nor its wholesaling to retail undertakings. This aspect of the activity would almost certainly have to fall to the public sector.

KINSALE GAS - HEADS OF AGREEMENT

1. Quantities

Gas to be supplied as per schedule of Northern Ireland requirements. Details of allowable fluctuation in demand to be discussed.

2. Supply will be initially for 20 years but open to extension beyond that period so long as supplies are available - subject to review of the base price, escalator and currency adjustment.

3. Priorities for Supply

Northern Ireland premium users would receive the same priority as that of premium users in the Republic. This would apply both to the initial period of supply and to any agreed supplies to Northern Ireland beyond that period.

4. Price

To be 25p per therm for the first 5 years of supply and 25.5p per therm for the remainder of the 20 year period of supply.

5. Transmission Costs

To be 1p per therm over the 20 year period of supply, escalated as per the basic price.

6. Capital Contribution

Northern Ireland to make a capital contribution of £5 million sterling towards the capital costs of the pipeline from Dublin to the Border.



7. Currency

Currency of price denomination and settlement to be sterling, the effects of sterling/dollar exchange rate movements to be shared equally by the parties.

8. Price Escalator

The formula to be 50% Gas Oil; 50% HFO with international index.

9. Application of Escalator

Six monthly; however, if after three months from the last adjustment, the escalator showed a change in excess of plus or minus 10% an immediate adjustment would be effected.

10. Five Yearly Review

There would be a five yearly review of the effect of the price escalator and currency clauses with any changes to be implemented only on agreement by both sides. The contract would continue unchanged even in the event there was no agreement on any adjustments.

1. The attached table shows the public expenditure implications of introducing natural gas to Northern Ireland, compared to the PE which is already earmarked for closure of the existing towns gas industry.
2. Column 1 shows the costs involved in establishing a natural gas industry compared with closing the existing industry.
3. Column 2 shows the trading expenses which are expected to arise from 1991/92 onwards.
4. To facilitate comparison of financial terms which occur over a period of time, the net total costs shown in Column 3 are discounted at 5% per year and shown in Column 4.
5. The totals of Column 3 and 4 show the PE implications summed over 30 years.
6. Two scenarios are shown:
 - (i) extending the supply of natural gas to all existing towns gas undertakings;
 - (ii) restricting the supply of natural gas to Belfast and the existing undertakings currently supplied by Belfast and to undertakings en route from the Border with the Republic of Ireland to Belfast.
7. Under both scenarios the total of Column 4 shows a saving to PE compared with closure of the order of £140 million.

KINSALE GAS; PUBLIC SECTOR FINANCIAL EFFECTS COMPARED WITH CLOSURE (£m)

(Positive numbers indicate a saving compared with closure, negative numbers additional expenditure compared with closure)

1 2 3 4 1 2 3 4

Northern Ireland Option

'Belfast' Option

Year	Compared to Closure	Retailer Surplus	Total	NPV		Compared to Closure	Retailer Surplus	Total	NPV
1982-83	+ 9.0	-	+ 9.0	+ 8.6		+ 5.8	-	+ 5.8	+ 5.
83-84	-26.0	-	-26.0	-23.6		- 7.2	-	- 7.2	- 6.
84-85	+ 3.3	-	+ 3.3	+ 2.9		+ 5.9	-	+ 5.9	+ 5.
85-86	+11.7	-	+11.7	+ 9.6		+14.5	-	+14.5	+11.
86-87	+ 8.4	-	+ 8.4	+ 6.6		+ 9.7	-	+ 9.7	+ 7.
87-88	-11.0	-	-11.0	- 8.2		-10.3	-	-10.3	- 7.
88-89	+ 4.1	-	+ 4.1	+ 2.9		+ 4.0	-	+ 4.0	+ 2.
89-90	+ 5.7	-	+ 5.7	+ 3.9		- 1.9	-	- 1.9	- 1.
1990-91	+ 8.7	-	+ 8.7	+ 5.6		+ 4.0	-	+ 4.0	+ 2.
91-92	+42.8	+ 1.5	+44.3	+27.2		+38.7	+ 0.5	+39.2	+24.
92-93	+31.2	+ 3.0	+34.2	+20.0		+18.6	+ 1.7	+20.3	+11.
93-94	+23.7	+ 4.6	+28.3	+15.8		+ 1.6	+ 3.0	+ 4.6	+ 2.
94-95	+ 9.8	+ 6.2	+16.0	+ 8.5		+16.4	+ 4.2	+20.6	+10.
95-96	+11.1	+ 8.0	+19.1	+ 9.6		+16.1	+ 5.6	+21.7	+11.
96-97	- 0.4	+ 9.9	+ 9.5	+ 4.6		+ 3.0	+ 7.1	+10.1	+ 4.
97-98	+ 2.7	+11.9	+14.6	+ 6.7		+ 4.9	+ 8.5	+13.4	+ 6.
98-99	-17.5	+13.9	- 3.6	- 1.6		- 8.8	+10.2	+ 1.4	+ 0.
99-00	+ 7.8	+16.1	+23.9	+ 9.9		+13.0	+11.8	+24.8	+10.
2000-01	- 2.5	+18.4	+15.9	+ 6.3		+ 1.2	+13.6	+14.8	+ 5.
01-02	-22.2	+20.8	- 1.4	+ 0.5		- 8.4	+15.4	+ 7.0	+ 2.
02-03	-13.5	+23.3	+ 9.8	+ 3.5		+ 1.6	+17.3	+18.9	+ 6.
03-04	-24.6	+25.9	+ 1.3	+ 0.4		-14.7	+19.3	+ 4.6	+ 1.
04-05	-22.2	+28.3	+ 6.1	+ 2.0		-12.8	+21.5	+ 8.7	+ 2.
05-06	-22.2	+28.3	+ 6.1	+ 1.9		-12.8	+21.5	+ 8.7	+ 2.
06-07	-22.2	+28.3	+ 6.1	+ 1.8		-12.8	+21.5	+ 8.7	+ 2.
07-08	-22.2	+28.3	+ 6.1	+ 1.7		-12.8	+21.5	+ 8.7	+ 2.
08-09	-22.2	+28.3	+ 6.1	+ 1.6		-12.8	+21.5	+ 8.7	+ 2.
09-10	-22.2	+28.3	+ 6.1	+ 1.6		-12.8	+21.5	+ 8.7	+ 2.
2010-11	-22.2	+28.3	+ 6.1	+ 1.5		-12.8	+21.5	+ 8.7	+ 2.
11-12	-22.2	+28.3	+ 6.1	+ 1.4		-12.8	+21.5	+ 8.7	+ 2.
12-13	-22.2	+28.3	+ 6.1	+ 1.3		-12.8	+21.5	+ 8.7	+ 1.
13-14	-22.2	+28.3	+ 6.1	+ 1.3		-12.8	+21.5	+ 8.7	+ 1.
TOTAL	-159.4	+446.8	+287.4	+135.8		-19.6	+333.2	+313.6	+142.

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M. Alexander
Ireland
(4)



Prime Minister

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

And

PRIME MINISTER

mt *As* *12* *279*

IRELAND

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You may like to see the attached paper about the economies of Northern Ireland and the Irish Republic. It was prepared within the Treasury at my request - largely to satisfy curiosity which had been aroused by conversations with my Irish opposite number at recent EEC meetings. Humphrey Atkins' people have kindly checked the facts. The paper leads to no particular conclusions, but as background is not without some interest.

2. I am copying this minute to Peter Carrington and Humphrey Atkins.

g.u

G.H.

7 September 1981

The economies of Northern Ireland and Eire

1. In economic terms Northern Ireland and Eire have much in common: they are small economies, highly dependent on international trade; they are both poor by European standards; they both suffer from high unemployment and a tendency to net outward migration most of the time; and they both benefit from income transfers from their richer neighbours. This note documents these features of the two economies and considers their relevance to alternative political 'solutions' to the Irish problem.

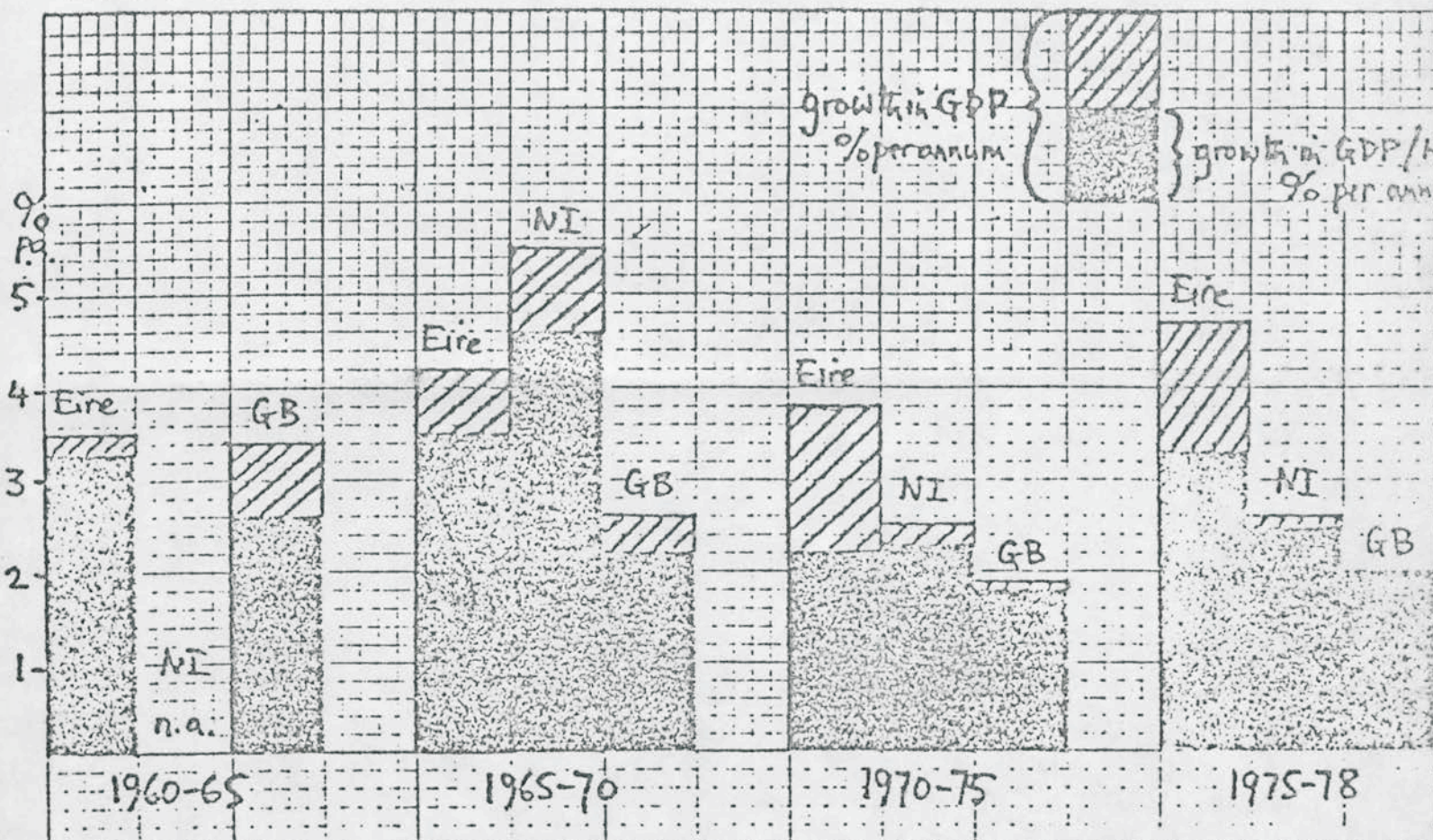
2. The small size and comparative poverty of Ireland can be seen from the following figures -

Population, Output and Personal Incomes in NI, Eire and the UK in 1978

	Population	GDP at factor cost	Personal Income	GDP p.head	Personal Income p.head
	m	£m	£m	£	£
N.I.	1.5	2998	3131	1948	2034
Eire	3.3	5788	6022	1748	1819
U.K.	55.9	144442	142093	2587	2545

A comparison of GDP per head in the EC shows that only parts of Italy are poorer than Ireland and that the richest region, Hamburg, is three times better off.

3. As the following chart shows, GDP has grown faster in both parts of Ireland than in GB since the mid 1960s. The growth rate in the South was faster than in the North throughout the 1970s, a result being that GDP per employee is now higher in Eire than in NI. Eire's dependent population is, however, proportionately higher than that of NI. The outcome is that GDP per head of population remains higher in NI than in Eire, despite the rapid growth of the Republic's economy in recent years.

Growth in GDP and GDP per head, 1960-1978

4. In both parts of Ireland unemployment is high, the most recent figures being 17% in NI and 13% in Eire. One result of the failure of the two economies to provide a sufficient number of jobs for a rapidly growing population has been net emigration from Ireland. However, the 1970s saw a change in the pattern, since Eire gained rather than lost population.

Net migration per 1000 population

	<u>Eire</u>	<u>N.I.</u>
1951-61	-14.2	- 6.6
1961-66	- 5.7	- 5.2
1966-71	- 3.7	- 4.6
1971-79	+ 2.9	- 5.7

The causes of the turn-around may have included the success of policies to attract new industry, the reduced 'pull' from GB, and an improvement in the level of social security benefits (expenditure on 'social security and welfare' increased from 8.8% of personal incomes in 1971 to 10.7% in 1978, and Eire's aim is said to be eventually to match the level of benefits in the UK). Net emigration has continued from NI.

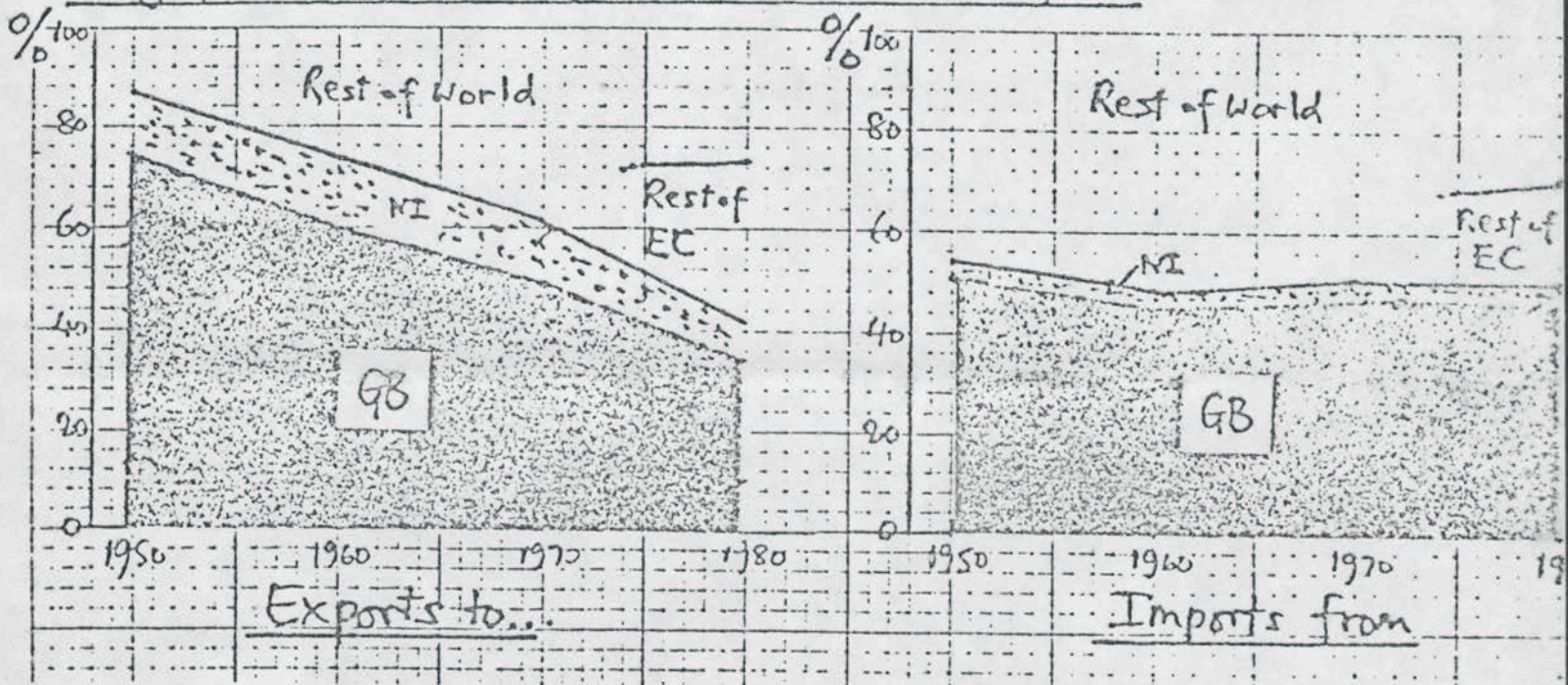
5. The industrial structures of the two economies have been becoming increasingly similar (see the table at the back showing the distribution of employment among broadly defined sectors). Agriculture's share of total employment has been falling faster in Eire than in NI but it is still double that of NI (22% as compared with 10%). Manufacturing accounts for some 20 to 25% of employment in both North and South; but the most vulnerable sectors, namely textiles, clothing and footwear, shipbuilding and other vehicle production account for 47% of manufacturing employment in the North as compared with 23% in the South. The services sector has a slightly bigger share of employment in NI than in Eire.

6. An academic assessment of the effectiveness of Irish industrial policy has concluded that it has made a very substantial contribution to net job creation in manufacturing, amounting to about a quarter of total manufacturing employment in NI, and just over one-third in Eire during the period 1960 to 1974. One result of this success has been that manufacturing output has grown very rapidly in Eire; it is now about three times higher than in 1962. The increase in NI has been much less impressive because the new industries were needed to offset the declining output of the old. Indeed in the 1970s the NI index of manufacturing output rose by only 4%. The current recession has hit manufacturing output and employment much harder in NI than in Eire. Between June 1979 and December 1980 manufacturing employment fell by 2.1% in Eire and by 14.8% in NI.

7. Both NI and Eire are very open economies, NI more so than Eire. Exports are equal to some 90% of GDP in NI and some 50% of GDP in Eire. Imports are similarly large. NI depends heavily on GB both for imports and exports: in 1974 82% of exports went to GB and 75% of imports came from there (the figures somewhat exaggerate the position since they include goods exported to and imported from third countries via GB).

8. Though Eire is still closely linked to the British economy as the chart below shows, it has been reducing its dependence on export sales to GB. A number of factors are responsible for the loosening of these ties - the broadening of the country's industrial base and the rundown of agriculture (which in 1955 accounted for 74% of exports, compared with 30% to-day); entry into the EEC; and now the break with sterling.

Geographical distribution of Eire's Exports and Imports



9. The two Irish economies are not particularly closely linked to one another. Eire sends 7% of her exports to NI and obtains 4% of her imports from NI. The most important

trade links between North and South involve the exchange of agricultural products and livestock.

10. The level of UK Exchequer support for NI is considerable: in 1981/82 it will be well over £1 bn. The main elements are a £785m transfer to the NI Consolidated Fund, £325m to pay for law and order and an, as yet unknown, transfer from the GB National Insurance Fund (worth £74m in 1979/80). The benefits to the Province from the CAP are not separately distinguished, but NI farmers received direct grants and subsidies from MAFF worth £40 m in 1979-80. In addition, the cost of maintaining the troops in NI is estimated to be £100m, and the Lord Chancellor's Department incurs expenditure on court services.

11. All in all, the transfers which the rest of the UK is making to NI are currently worth about one-quarter of personal incomes in NI. This is not to say that incomes would fall by a quarter without them - some of the benefits are passed to the consumers of NI products in the form of lower prices, some to "foreign" firms operating in NI in the form of higher profits; other parts of the transfer buy services which NI may not need indefinitely, most notably the present level of expenditure on law and order. Nevertheless, there can be no doubt that the UK subvention has enabled NI to achieve a level of income significantly above that which it could maintain on its own and retain resources which otherwise would have relocated in regions of greater economic opportunity. It has also supported a high and growing level of public sector employment: in 1974 the public sector provided 30% of all jobs in NI; by 1979 this figure had risen to 35% (the equivalent figures for the UK as a whole are 27% and 29%).

12. The South too relies on income transfers from "overseas", particularly from the EC. It has been estimated that Eire's benefit from the CAP amounted to some £600m in 1980. In addition there were receipts of some £100m in 1979 in respect of industrial development.

Political 'Solutions'

13. Three political 'solutions' with variants have been canvassed from time to time, namely (i) independence for NI, (ii) some form of union between North and South, and (iii) closer co-operation between North and South within the existing political framework. The first point to make about these is that, although any of them would be beneficial in economic terms if it led to a restoration of peace and a more settled environment in which business could be carried on, none of them would 'solve' the economic problems of low income and high unemployment. Indeed if they caused an interruption or scaling down of fiscal transfers to Ireland they could exacerbate the Island's economic problems.

(i) Independence for NI

14. So long as NI relies as heavily as it does on the GB economy both as a source of raw materials and as an outlet for its final products, it is hard to see how it could be in any worthwhile sense independent in economic terms. In particular it could not gain by devaluing the NI pound against the pound sterling; and it would be bound to experience the same cyclical fluctuations as GB. Moreover if independence meant forgoing the fiscal transfers which NI at present receives from the UK, it would have a high cost in terms of national income. In sum, economic independence looks to be a non-starter.

(ii) Some form of political union between North and South

15. The economic and monetary unification of North and South would raise all the problems which have so far prevented the economic and monetary unification of the EC as a whole. In particular, the necessary harmonisation of tax structures and rates and the alignment of social security payments, would cause considerable difficulty. Harmonisation could not take the form of a levelling up of social security payments and a levelling down of taxes if the

budget balance were to remain undisturbed. Thus there would be difficult compromises to be reached and considerable upheaval.

16. The problems of harmonisation alone would take time to resolve. In addition there would be currency changes to consider and ^{most important of all,} the future of the income transfers to N.I. which are currently being made by GB. Enthusiasts for economic and monetary unification would say that none of the problems which would arise is insoluble. But they could scarcely deny that the preparatory work to be done is very considerable and that a smooth and orderly transition would take a number of years. At least for the immediate future, by far the most promising 'solution' is the third one, closer co-operation. This could be a step on the way to eventual economic and monetary unification; or it could be the framework for a long-term preservation of the political status quo.

(iii) Closer Co-operation

17. The joint planning of roads, electricity supplies and other physical links could obviously be beneficial to both sides; and with the return of more settled conditions there would presumably be a backlog of such projects to be carried out (the border areas having been particularly unsettled). The joint promotion of tourism is an obvious example of another form of co-operation which would be easier if tensions were less. More generally the case for closer co-operation is to take advantage of economies of scale in an island too small to justify the separate development of North and South.

18. Although EC membership may have generated some cross-border traffic in agricultural produce to take advantage of differences in green exchange rates, the graphs on page 4 of this note do not suggest that membership has caused trade between North and South to grow particularly fast. The fact is that the economy of N.I., like that of the other regions of this country, is oriented over-whelmingly towards the rest of the UK, whereas, as the first graph on page 4

/shows

SECRET & PERSONAL

shows, Eire has been steadily diversifying its trade away from the UK ever since World War II. It is entirely possible that unsettled conditions may have delayed an adjustment to EC membership which will come about once normality has been restored.

19. In economic terms the Government's role is to ensure that the natural forces making for closer co-operation between North and South are allowed to run their course. Beyond that, the big question concerns the future of the present Exchequer contributions to NI. Whether NI should be aided indefinitely to the present extent raises broad issues going beyond the scope of this note. It is, however, relevant that the NI economy is adjusted to the present level of subvention and that there would be considerable difficulty in scaling down this level quickly.

18 August 1981

(percentages)

DISTRIBUTION OF EMPLOYMENT AMONG SECTORS

	<u>Eire</u>		<u>NI</u>	
	1968	1978	1968	1978
Agriculture	29	22	12	10
Mining	1	1	1	-
Manufacturing	19	20	31	24
Food, drink, tobacco	5	5	5	4
Chemicals and allied ind.	1	1	1	-
Engineering and metal ind.	2	3	6	4
Shipbuilding	-	-	2	2
Vehicles	1	1	2	2
Textiles	2	1	8	5
Clothing	3	2	4	3
Timber and furniture	1	1	1	1
Paper, printing, publishing	2	2	1	1
Bricks, pottery, cement	1	1	1	1
Miscellaneous	1	2	1	1
Construction	7	8	10	8
Gas, electricity, water	1	1	2	2
Services	38	41	39	46
Public Administration	4	6	6	9
<u>Total</u>	100	100	100	100

Ireland

NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

R Lyne Esq
Foreign and Commonwealth Office
London
S W 1

8 June 1981

Dear Rodin,

NAPN

Print 9/6

COOPERATION NORTH

Cooperation North was set up in Dublin in June 1977 to encourage the improvement of understanding and cooperation, notably through economic collaboration, between Northern Ireland and the Republic. It receives considerable international support from business and financial institutions and has made contacts with individual members of the Irish Government. Its Council members are influential and important figures in their own fields which cover both the private and public sectors. The organisation is genuinely non-political and since its inception has worked hard to promote economic, social and cultural contacts across the border. It has also been active in encouraging an exchange of views between professional bodies, town councils and other agencies from both Northern Ireland and the Republic.

At the beginning of this year, Cooperation North established itself in the United States under the title of Ireland Cooperation North Incorporated. During a visit there in February, its energetic Chairman Dr O'Regan was received by the Minister at the Washington Embassy and by other officials in the United States. He is returning to the United States later this month to seek finance from large foundations there. In view of the Anglo-Irish nature of Cooperation North's work and now its American angle, my Secretary of State thought that Lord Carrington might like to see the attached note of a recent meeting between NIO officials and Dr O'Regan. We are now considering how best to advise him on how he might raise funds in Great Britain.

In view of the relevance of Cooperation North's work to the development of Anglo-Irish relations, I am sending a copy of this letter with its enclosure to Michael Alexander at No.10.

Stanley

S W BOYS SMITH

~~E.R.~~NOTE OF A MEETING WITH DR O'REGAN IN NIO (L) ON MONDAY 11 MAY
AT 12 NOON

Present: Mr Moriarty Dr O'Regan
 Mr Benson
 Mr Abbott

1 After initial courtesies, Dr O'Regan explained that in its first 2½ years Cooperation North had striven to promote economic collaboration and good relations generally between the two parts of Ireland. Their non-political stance was widely accepted North and South, and they now wished to build on their promising start by expanding their operation both in Ireland and also in the United States. The organisation received about a £100,000 a year from banks and industry for its Irish operation. Currently this was largely channelled into their series of study papers on North/South cooperation. An American counterpart - Ireland Cooperation North Incorporated - had recently been launched and Dr O'Regan would seek finance in the United States from large foundations there during his forthcoming trip from 18 May - 20 June. He also hoped to direct interest in, and concern about, Northern Ireland into constructive channels by encouraging support for his organisation's activities. To function effectively Cooperation North now needed some £½ million a year. The organisation could not be seen to be taking money from either the United Kingdom or Irish Governments, but the two Governments could nevertheless complement its work by coordinating their efforts in certain spheres and by preparing public opinion North and South for closer relations between all the people of the island.

2 Dr O'Regan agreed with Mr Moriarty that for well understood political reasons much of this work must be done at one remove from government. The recent successful joint visit to the United States by the Lord Mayors of Dublin and Belfast under Cooperation North's auspices was an example of what could be achieved. But in Dr O'Regan's view, the two Governments could be more positively involved, albeit behind the scenes, by encouraging public bodies to work together in the interests of the island as a whole. For

R.

example, the Northern Ireland Tourist Board and Bord Fáilte should be seen to be promoting Ireland abroad. There had been excellent cooperation in the mid-1960s but this had been overtaken by the outbreak of violence: that cooperation should be revived. More substantially, the two development agencies in Ireland should collaborate in attracting inward investment; and in international markets goods from the two parts of Ireland should appear side by side. There could be greater cooperation within Ireland. For example, demand for and supply/^{of} University places North and South should be properly articulated: the current vacancies in the New University of Ulster should be filled by students from the Republic which could not meet student demand.

3 In reply, Mr Moriarty said that these points were well taken. Much of what Dr O'Regan had said was in line with the philosophy which underlay the current programme of joint studies. But cooperation was/^a sensitive subject politically. Moreover, at the practical level, there would doubtless be limits on the extent to which the two development agencies could work effectively together given that they were in competition.

4 To keep up Cooperation North's momentum, Dr O'Regan said that a letter would issue shortly to selected individuals in both parts of Ireland eg Chief Executives of state bodies, captains of industry and church leaders, explaining Cooperation North's objectives and seeking their support. The organisation could do much if it had sufficient funds. For example, it needed £20,000 to run a series of conferences: Gallaghers had been asked to help. Thanks to support from the ^governments of the United Kingdom and the Republic, they now had £40,000 from EEC. Hitherto, they had not approached bodies in Great Britain. Could we think who might help?

5 Mr Moriarty undertook to consider who in Great Britain might be worth approaching. We would be happy to give letters of introduction and support. In conclusion, Mr Moriarty encouraged Dr O'Regan to keep in touch with NIO as we would like to help as and when we could.

R.

6 (Note. Dr O'Regan has recently seen Sir Kenneth Stowe and Mr Bell and he will see HM Ambassador to Dublin shortly. During his visit to the United States in February to establish Ireland Cooperation North Incorporated Dr O'Regan was received by the Minister at the Washington Embassy and also by the staff of BIS New York and NIIDO.)

N.C. ABBOTT

N C ABBOTT

13 May 1981

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CONFIDENTIAL



10 DOWNING STREET

From the Private Secretary

4 June 1979

Anglo/Irish Economic Co-operation

Thank you for your letter of 31 May, in which you conveyed your Secretary of State's views on the programme for Anglo/Irish economic co-operation and his recommendation that, on political grounds, this co-operation should continue. Paul Lever wrote to me on the same subject on 1 June.

In the light of the background set out in your letter, the Prime Minister agrees with Mr. Atkins that the Anglo/Irish economic co-operation exercise should continue in its present form.

I am sending copies of this letter to Paul Lever (Foreign and Commonwealth Office) and Martin Vile (Cabinet Office).

B. G. CARTLEDGE

J.G. Pilling, Esq.,
Northern Ireland Office.

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Foreign and Commonwealth Office

London SW1A 2AH

1 June 1979

Dear Bryan,

Anglo-Irish Economic Cooperation

In your letter of 18 May you sought further advice in the light of the Prime Minister's comments on the brief I sent you on 16 May.

You will now have seen Joe Pilling's letter of 31 May giving the Northern Ireland Secretary's views, which the Foreign and Commonwealth Secretary very much shares. The crucial point, in terms of our relations with the Irish Republic, is that the existence of formal machinery helps Mr Lynch demonstrate to Irish public opinion that his policies are working, however slowly, to bring about the "coming together of the peoples of Ireland". To the extent that this makes it easier for him to resist pressures to take new initiatives, it is helpful also to us. And, from our point of view, Anglo/Irish economic cooperation helps to maintain the positive aspects of a relationship which it is in our overall interest to prevent from being dominated exclusively by the security issue.

We should perhaps have explained in greater detail in the earlier brief that the various sub-groups were not set up to further cooperation as an end in itself. For example, British and Irish Customs officials have been in close contact with one another for many years, and no additional machinery was established in this area. All the same, the Joint Steering Group was able, for example, to give some political impetus to bring about improvements in duty-free facilities for air travel between Britain and the Republic, which, although not intrinsically an important issue, is a factor affecting public attitudes in both the UK and Ireland.

The only additional official machinery which has been established is the Joint Steering Group itself. The Foreign and Commonwealth Secretary believes that, so long as the Irish themselves see this as a useful symbolic element in Anglo/Irish relations, it will be worth retaining. Its activities are under close control and there is no question of its getting out of hand or of involving itself in studies which are not of value in terms of the UK (including Northern Irish) interest.

I am sending copies of this letter to Joe Pilling (Northern Ireland Office) and to Martin Vile (Cabinet Office).

Yours GEX

Paul

P Lever

Private Secretary

Bryan Cartledge Esq
10 Downing Street

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From: THE PRIVATE SECRETARY

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Prime Minister

NORTHERN IRELAND OFFICE

GREAT GEORGE STREET,
LONDON SW1P 3AJ

You expressed considerable
suspicion (below) about
Anglo-Irish Economic co-operation. In the light of

B G Cartledge Esq
10 Downing Street
London
SW1

these comments from 31 May 1979

Mr. Atkins, are you
content that the existing machinery
should remain in operation? Yes

Dear Bryan,

Don't expect me to be 31/5
content - but I will agree!

ANGLO-IRISH ECONOMIC COOPERATION

In your letter of 18 May to Paul Lever, you asked for the
comments of the Secretary of State for Northern Ireland on
this issue.

Quite apart from the economic considerations, which are
discussed below, there are from the Northern Ireland point
of view strong political arguments for maintaining the
existing machinery for Anglo-Irish economic cooperation
(AIEC). The Republic are always anxious to give expression
to what they regard as the essential unity of Ireland, and
this economic machinery has made it possible for us to divert
this acute Irish interest in cooperation between the North
and South from political forums into a relatively less
embarrassing channel. Otherwise we should have found ourselves
having to oppose all Irish initiatives for joint action since
the Unionists will only stomach a limited measure of cross-border
cooperation, which they see as the "Irish dimension" being
introduced through the back door. The difficulty is that
consistent opposition to the Irish on this front is not in our
interest. We need to be as forthcoming as we can on the economic
front in order to sweeten the political medicine that we have
to give them (no satisfaction of their aspirations for Irish unity)
and - perhaps more important - to create the best possible
atmosphere for discussion of matters of security cooperation
(where we ourselves are the demandeurs).

On its own terms, we believe that the AIEC machinery justifies
itself, by bringing together those contacts which have developed
over the years between Government Departments in London, Belfast
and Dublin in response to practical problems of mutual concern.
It is designed to achieve the maximum benefit for relations with
the Republic at minimal cost to the UK in terms of both public
expenditure and administrative expenses.

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The AIEC forum does not encourage additional demands on national resources. AIEC activity is geared to facilitating practical and mutually beneficial contacts and in fact helps to ensure that any schemes considered are limited in extent and application, and to prevent the Irish working up and publicising ambitious and undesirable projects. On the specific matters mentioned in the brief, the conclusion of a bi-lateral road-haulage agreement would be to the UK's economic advantage, and electricity interconnection is considered principally in terms of its own commercial viability. The current disruption to the North/South interconnector is, for example, costing the Northern Ireland Electricity Service at least £2m a year. Cross-border cooperation is encouraged and aided by the EEC, who have part-funded the consultants' studies (2 of which were in fact undertaken before the AIEC exercise as such was begun). Almost all the expenditure involved in implementing the Londonderry/Donegal report was already in Northern Ireland programmes and while some projects were brought forward this was at the expense of others. It is made clear that the implementation of study recommendations (and of any other proposals for cross-border projects) is subject to national spending priorities and public expenditure restraints. The Irish Government also of course have to consider carefully the financial implications of any proposals they make.

The AIEC sub-committees are small-scale, meet only when there is something of substance to discuss, and take up little of officials' time. The Steering Group, which meets no more than twice a year, is a useful means of ensuring that contacts with the Republic are properly processed and coordinated.

The Secretary of State accordingly believes that there is considerable advantage in continuing the Anglo/Irish Economic Cooperation exercise. He is as concerned as the Prime Minister however that the emphasis must be on practical contacts - and not grandiose and wide-ranging schemes of the economic planning variety put forward at regular intervals by Dr Fitzgerald when his Government was in power in the Republic - and that time and effort should not be wasted on discussing projects for which there will be no resources available. He is also anxious to ensure that the exercise does not lead to the development of any superfluous or wasteful bureaucratic structures.

I am sending copies to Paul Lever and Martin Vile.

Yours ever,

Joe

J G PILLING

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Ireland
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10 DOWNING STREET

From the Private Secretary

18 May 1979

Anglo/Irish Economic Cooperation

Thank you for supplying, in response to the Prime Minister's request following her discussion with the Taoiseach on 10 May, a note on economic cooperation between the United Kingdom and the Republic of Ireland.

The Prime Minister has read the note and has reacted with some scepticism to the picture which it presents of a proliferation of official groups studying numerous high cost projects for which, in all probability, funds will not in the event be available. The Prime Minister has indicated that, on the basis of the evidence in your note, she sees no case for the continuation of the joint steering group and its various sub-groups.

I recognise that your note is purely descriptive and that there may be political aspects to Anglo/Irish economic cooperation which it was not designed to cover. I should be grateful for any further advice which you, in consultation with the other Departments involved, may wish to offer in the light of the Prime Minister's reaction. I believe the Prime Minister would be particularly glad to have the comments of the Secretary of State for Northern Ireland on this issue.

I am sending copies of this letter to Joe Pilling (Northern Ireland Office) and Martin Vile (Cabinet Office).

B. G. CARTLEDGE

Paul Lever, Esq.,
Foreign and Commonwealth Office.

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Foreign and Commonwealth Office

London SW1A 2AH

16 May 1979

Dear Bryan,

Thank you for your letter of 10 May about the Taoiseach's call on the Prime Minister earlier that day.

I attach, as requested, a brief on Anglo/Irish Economic Co-operation. This has been agreed with the Northern Ireland Office.

I am copying this letter to Joe Pilling in the Northern Ireland Office.

Yours WGL

Paul

(P Lever)
Private Secretary

Bryan G Cartledge Esq
10 Downing Street
LONDON

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*P.A. -
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17/5*

Prime Minister

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Mr. Lynch referred briefly to economic co-operation when you saw him on 10 May; and you asked for a note.

BRIEF BY THE FOREIGN AND COMMONWEALTH OFFICE
ANGLO-IRISH ECONOMIC COOPERATION (AIEC)

see comments end, but 17/5

1. At the meeting between the then Prime Minister and the Taoiseach on 28 September 1977 it was agreed that it would be of mutual advantage to improve practical cooperation between the UK and the Republic of Ireland on economic matters, and that officials would meet to review the arrangements and opportunities for economic cooperation with particular reference to Northern Ireland. Officials would review current and proposed cross border studies and identify subjects for further examination, with assistance from EEC funds where appropriate. (The Commission has indicated that it will look favourably on projects with a "communautaire" flavour.)

another group
2. UK and Irish officials met in London in November 1977 and agreed to establish a Joint Steering Group (JSG) to oversee and coordinate all kinds of Anglo-Irish economic contacts without, however, interfering with existing contacts where these were satisfactory. They identified five areas of economic activity:

Transport, Energy, Customs, Economic Planning, and North-South Contacts.

The JSG meets on ad hoc basis. It met in February 1978 in Dublin and December 1978 in London. It is likely to meet again in Dublin within the next few months. A JSG report on Anglo-Irish economic cooperation was considered by UK and Irish Ministers in May 1978 and published in June 1978 (Annex A).

3. There have been continuing regular contacts within the sub-groups. Notable recent developments are:-

- (a) Energy - all aspects of electricity interconnection are to be explored, including the possibility of a multi-link connection between Northern Ireland and the Republic (the existing interconnector has been put out of action by terrorists), an Irish proposal for a Wales-Wexford link, and the alternative possibility of a link between Scotland and Northern Ireland.
- (b) Transport - discussion continues on a proposed bilateral road freight agreement between the UK and the Republic which it is hoped will allow GB hauliers greater access to the Republic whilst preserving favourable arrangements for Northern Irish hauliers.
- (c) North-South Contacts - in addition to regular departmental contacts, and agreement in February in the EEC Council of Ministers to a cross-border drainage programme, a number of joint economic studies, in most cases with financial assistance from the EEC, have been or are being undertaken:-
- (i) Communications Study for the Londonderry/Donegal area in which substantial progress has already been made on the implementation of the Consultants' main recommendations, published in October 1977, which are estimated to cost over £25 million in Northern Ireland. Two recommendations concerning joint transport ventures required further expert study by both Governments and reports are expected shortly.



- (ii) Study of the Mourne Herring Fishery in the Irish Sea (Consultants' Report due December 1979).
- (iii) Study into Tourism and Drainage in the Erne Catchment Area (Consultants' Report due December 1979).
- (iv) Study of various aspects of infrastructure in the Newry/Dundalk area (report by officials due May 1979).

4. The Irish Government attaches particular political importance to cross-border economic cooperation because of its "All-Ireland" flavour. While the existing level and range of such cooperation is regarded by the Irish as generally satisfactory, they are likely to press for urgent implementation of further reports as they become available and for completing action on the Londonderry/Donegal Report. Mr O'Kennedy, the Irish Foreign Minister, has said that he hopes the new British Government will be more active in promoting cross-border projects than the previous Government. But at his meeting with the Prime Minister on 10 May Mr Lynch commented that cross-border economic cooperation was going ahead very well.

British Interests

5. The cooperation machinery described above has contributed a certain amount to the projects under way. The fact is, however, that there are extensive links between the Republic and Northern Ireland, and where projects are of mutual advantage they are likely to go ahead anyway. Initially there was some concern that the "institutionalization" of North-South links would cause concern to Unionists in Northern Ireland

(for the same reason as they were welcomed by Mr Lynch). In the event it did not. The publication of the May 1978 report attracted no adverse attention. So it can be said that so far there has been some modest benefit: cooperation is seen in the North as acceptable to some degree. However, cross-border projects are not an end in themselves and all proposals involving Government expenditure (including those which receive EEC support) have to be considered in terms of spending priorities in the province as a whole.

Levellers committees
 for endless projects
 for endless expenditure
 for which there is no money.

I hope this can soon
 be done down

arb.

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*Subject file Ireland Ireland
- Taoiseach Vintis.
May 1979*

10 DOWNING STREET

From the Private Secretary

10 May 1979

B.F. 17/5 P.2

Dear Paul,

The Taoiseach's call on the Prime Minister
at 10 Downing Street on 10 May 1979

As you know, the Taoiseach, Mr. Jack Lynch, called on the Prime Minister at No.10 this afternoon at 1530. He was accompanied only by his Private Secretary, Mr. Dermot Nally. The following are the main points of substance which arose during half an hour's conversation.

Northern Ireland

Mr. Lynch said that he was very glad that the Government had come to office with a majority sufficient to allow them to take positive action. The Prime Minister said that she had complete confidence in the new Secretary of State for Northern Ireland and that she was sure that Mr. Atkins would carry out his responsibilities very successfully. Mr. Lynch referred with appreciation to the message which Mr. Atkins had addressed to the Irish Foreign Minister Mr. O'Kennedy. The Prime Minister said that they would of course be very satisfied to work for a solution to the Northern Ireland problem but that the problem was of a nature which did not yield to instant solutions. Mr. Lynch stressed that he was not attempting to force any substantive discussion of Northern Ireland on the Prime Minister and recognised that she would need time to study the problem.

Later in the discussion, Mr. Lynch said that the Irish Government were looking forward to a more positive political approach in Northern Ireland. He would not use the phrase "power sharing", which he knew would not be well received, but the Irish Government did hope to see some form of shared responsibility in the North. Mr. Lynch referred to the late Mr. Airey Neave's ideas on Regional Councils and went on to comment that the local authority regime in Northern Ireland had in his view tended recently to revert to the old system, with all the discrimination in housing and other matters which had been associated with it. This process could quickly break down the goodwill which had slowly been created. Mr. Lynch said that he thought that co-operation between the Northern Irish police and the Republic on security matters had been of a high standard. It was of course difficult to control everything which happened south of the border; the Irish Government had set up

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special courts and had made it possible for convictions to be obtained for membership of the IRA on the evidence of a senior Garda officer. But, Mr. Lynch said, the Government's task was made much more difficult when people like Mr. James Molyneaux talked about the Republic being a "haven for terrorists".

Mr. Lynch said that in his view Mr. Roy Mason had made a mistake in proclaiming so loudly that the security forces in Northern Ireland were getting the better of the IRA. This put the IRA on their mettle and spurred them on.

Economic matters

Mr. Lynch said that the CAP had been of great benefit to Irish farmers, enabling them to increase production by 300% in five years. The Anglo/Irish trade agreements, however, had been very unfavourable to the Republic. On the EMS, Ireland had feared that when she joined the scheme the pound sterling would depreciate against the Irish pound; in the event, the reverse had happened and this was a great help to Irish industry. Mr. Lynch said his Government warmly welcomed the Foreign and Commonwealth Secretary's recent statement on the EEC and the British Government's positive approach to Europe. Under the Labour Government, the United Kingdom had seemed to be dragging its feet at every level. Mr. Callaghan had been slow to encourage the concept of the EMS and in both the Agricultural and Energy Councils progress had been very significantly obstructed by British positions. The same had been true over fisheries. The Prime Minister commented that fisheries policy was a problem of great difficulty for the United Kingdom: fish was a common resource without a common market. Acknowledging this, Mr. Lynch described Irish efforts to build up Ireland's fishing industry.

In conclusion, Mr. Lynch commented that cross-border economic co-operation between Northern Ireland and the Republic was going ahead very well - with a low profile, but effectively. The Prime Minister has said that she would like to be briefed on this: I should be grateful if a note on the progress made in cross-border economic co-operation to date could be prepared in time to reach me by 17 May.

Mr. Lynch suggested to the Prime Minister that they should get in touch in due course, with a view to arranging a more substantive meeting; the Prime Minister said that she would need some time to study the issues which they would wish to discuss. Mr. Lynch suggested that the Prime Minister might join the other EEC Heads of Government in attending the signing ceremony for the accession of Greece to the Community, which was to be held on 28 May. The Prime Minister said that she could not commit herself at this stage. I should be grateful for advice

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dealt with on Tsavris file

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how she should respond to any more formal invitation which may be addressed to her.

It was agreed that Mr. Lynch's visit to No. 10 would be described to the Press by both sides as a courtesy call and that it would be made clear that there had been no substantive political discussion. Questioned by journalists outside No. 10 (with the Prime Minister looking on) Mr. Lynch said that although Northern Ireland, security matters and cross-border economic co-operation had been mentioned during his talk with Mrs. Thatcher, none of these subjects had been covered in detail.

I am sending copies of this letter to Joe Pilling (Northern Ireland Office), Roger Facer (Ministry of Defence) Tom Harris (Department of Trade), Garth Waters (Ministry of Agriculture, Fisheries and Food) and Martin Vile (Cabinet Office).

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Paul Lever, Esq.,
Foreign and Commonwealth Office.

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