

CONFIDENTIAL

1. CP to note  
2 CF



Prime Minister <sup>cc DP</sup> 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

CONFIDENTIAL





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.



CONFIDENTIAL



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.

*Do till*

J. P.

7 June 1984.

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

CONFIDENTIAL



Ireland  
Ecom Co-operation May 79



07

104



CONFIDENTIAL



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