



Irish Offshore
Operators'
Association

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Brexit: Potential Impact on Irish Oil & Gas industry

INTRODUCTION

This submission, written in the aftermath of the EU Referendum in the UK on 23rd June 2016, reviews the observations and suggestions of the Irish Offshore Operators' Association (IOOA) regarding the potential impacts a UK exit from the EU could have on the oil and gas industry in Ireland. As part of the Contingency Framework announced on 24th June 2016, Minister Naughten announced that a full assessment of the issues that may arise for energy supply under different scenarios envisaged in the pre-negotiation phase will be undertaken by DCCA. In the spirit of constructive dialogue and information sharing, IOOA, whose members are key deliverers of energy supplies in Ireland and internationally, has identified issues, challenges, questions and potential solutions which need to be considered. Given the relative isolation of Ireland, it is imperative that exploration and development of Ireland's offshore natural energy resources continues to be supported to provide energy certainty and security in post-Brexit scenarios.

The general consensus among political and economic observers is that the UK leaving the EU will have a negative effect on the oil and gas industry in NW Europe, especially in the UK and also probably in Ireland. However, the nature of the impacts will depend upon EU-UK, and bilateral Anglo-Irish trade agreements that might be negotiated. Brexit immediately injected fresh uncertainty and volatility into the geopolitical landscape and economic markets throughout Europe and beyond. This is likely to continue, at least in the short to medium term, until there is clarity regarding the nature of the UK-EU divorce and of the successor trade and other agreements between the UK and Europe, and between Ireland and the UK. In the meantime, it is imperative to highlight some of the key issues and plan for mitigation of adverse effects as well as exploitation of potential opportunities.

MAJOR IRISH IMPACTS

The impacts of Brexit on the Irish oil and gas industry will depend upon the types of agreement the UK reaches with the EU, and also bilateral agreements with Ireland. Potential impacts on the Irish oil and gas industry are likely to be in the broad areas of:

1. Energy security.
2. Freedom of mobility for workers.
3. Loss of an experienced advocate at EU energy policy level.
4. Collaboration and information sharing.
5. Investment uncertainty for Irish Exploration & Production and major infrastructural projects.

1. Energy security

While there is currently a global surplus of oil and gas, this is likely to change in the coming years as a result of the current global drop in exploration, discovery and new field developments. Periodic interruptions of supply due to political instability need to be planned for (e.g., oil crises/shortages of 1973 and 1977; the 2009 Russia-Ukraine gas dispute which cut off supplies to southeastern Europe for 13 days). Many of the underlying factors leading to those interruptions still exist and Ireland remains one of the most vulnerable EU countries in terms of

energy security. One of the potential outcomes of the exit of the UK from the EU, is the physical separation of Ireland from the EU energy network, increasing the risk to energy security in the event of supply interruptions unless sustained and well supported measures are taken to source and secure alternative supplies.

Ireland imports all its oil requirements of 6.5-6.6 million tonnes annually^{1,2} (equivalent to c. 137,000 barrels per day²) necessary for transport, industry and domestic use. Approximately one third of crude for Whitegate refinery, which supplies up to 40% of the Irish retail market, comes from the UK. Towards the end of 2015 Ireland imported 95% of its annual gas consumption of 4.1 Bcm (c. 400 MMscf/d)². With the Corrib gas field coming on stream in late December 2015 imported gas volumes dropped rapidly and are now dipping below 50% of national requirements. However, production will plateau and begin to drop probably not long after completion of the Brexit process. Alternative supplies, either through imports or further indigenous discoveries and production, will backfill this production shortfall. If this alternative supply is imported gas, once again Ireland will be vulnerable to gas interruptions.

Currently Ireland’s gas imports come exclusively through the interconnectors to Scotland, with no direct link to mainland Europe gas or power networks. Until 2005 the UK was a net exporter of oil, natural gas liquids and gas. However, in the past decade the UK has been increasingly reliant on imports to meet energy needs (Fig. 1), with falling oil and gas production (Fig. 2).

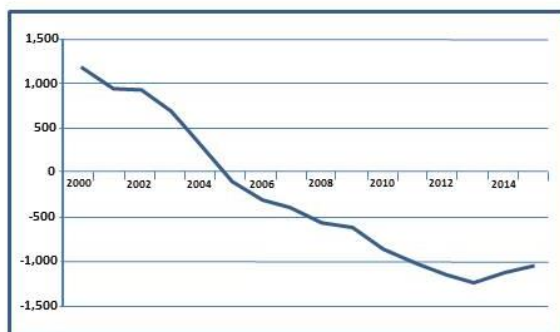


Fig. 1. UK oil and gas imports (negative) and exports (positive). 000 boe/d. Source: OilVoice, 20th July 2016)

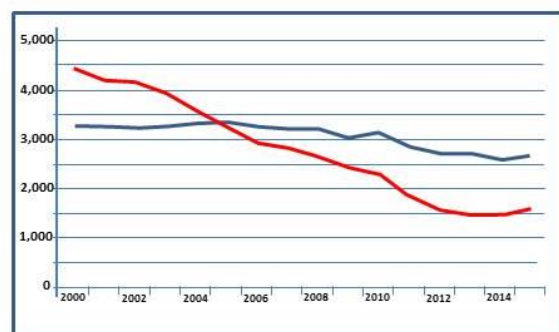


Fig. 2. UK oil and gas production (red) and consumption (blue). 000 boe/d. Source: OilVoice, 20th July 2016)

The UK currently imports more than 1 million barrels of oil equivalent per day to meet its needs, and UK energy import dependency is anticipated to reach 55% by 2030. 57% of the UK’s gas needs (~70 Bcm per annum) are imported. 33% of Europe’s gas comes from Russia, while 21% comes from Norway³. Therefore, while not insignificant, the impact of Brexit on the UK’s security of gas supply is likely to be less problematical as it is not as reliant on EU countries for gas. Ireland, however, remains heavily reliant on the UK for gas.

Oil and gas production from the mature North Sea province is in long-term decline. This has been compounded by the impact of the global commodities slump and an uncertain investment environment in the wake of Brexit. The drop in oil prices to less than US\$50 a barrel has left approximately 30% of fields in the UK North Sea operating at a loss, according to a recent report from Wood Mackenzie⁴. Prior to Brexit the price collapse was already pushing more producers

¹ http://www.seai.ie/Publications/Statistics_Publications/Energy_in_Ireland/Energy-in-Ireland-1990-2014.pdf

² <https://www.bp.com/content/dam/bp/pdf/energy-economics/statistical-review-2015/bp-statistical-review-of-world-energy-2015-full-report.pdf>

³ <https://www.britishgas.co.uk/the-source/our-world-of-energy/energys-grand-journey/where-does-uk-gas-come-from>

⁴ <http://www.bloomberg.com/news/articles/2016-07-18/north-sea-field-shutdowns-to-climb-as-brexit-deepens-oil-gloom>

towards field decommissioning. This has increased the number of fields likely to cease production in the near term, which has increased decommissioning costs. The apparent lack of a clear energy policy mandate for UK political leaders following Brexit adds further uncertainty and complexity to investment decisions. This also illustrates the vulnerability of Ireland's exclusive reliance on gas imports from the UK when it, as an energy importer itself, will lie outside the EU.

Supply interruptions in Ireland can be partly mitigated by use of either strategic oil reserves or stored gas. However, part of Ireland's strategic oil reserve of 90 days' supply (required under EU law) is held overseas in other EU Member States. Ireland currently holds oil stock agreements with Denmark, UK, Netherlands, Spain, Sweden and Germany. The arrangement to store oil in the UK should be reassessed in the light of UK withdrawal. Kinsale Head currently stores some strategic gas supplies but this facility will be decommissioned soon, further increasing the exposure to supply interruptions. An ESRI Working Paper (2010)⁵ estimated that the cost of losing three months of gas-fired electricity could equate to almost 50% of Ireland's GDP.

Additionally, if the UK's role in the EU internal energy market changes (current indications are that the UK is keen to support and participate in an integrated energy market), the lack of direct access to the EU market for Irish oil or gas exports could be a factor in inhibiting the market for future Irish oil or gas discoveries.

The most secure strategy to achieve Irish energy independence remains exploration and development of indigenous offshore natural resources. Lingering uncertainty post-Brexit highlights the importance of supporting this strategy. Gas is of particular importance as Ireland is heavily reliant on imports from the UK through the Ireland-Scotland interconnectors. It is imperative that a competitive fiscal regime, robust and simple regulation and political leadership support exploration, development and production activities in all Ireland's offshore area. With existing offshore gas infrastructure currently servicing the south (Kinsale Head) and west (Corrib) coasts, another potential approach is an incentivised focus in the short term in the vicinity of these areas could shorten the lead-time for development, reduce capital and operating costs and ensure minimal environmental impact.

Key industry Questions:

- What gas interconnector arrangements are required to ensure security of supply, and export facilities into the EU gas grid via the UK for Irish gas discoveries surplus to Irish needs?
- What measures will be taken to provide/ensure strategic gas and oil storage facility to replace Kinsale Head and oil stocks currently held in UK?
- What measures will be taken to encourage and incentivise exploration and development of indigenous offshore oil and gas in order to improve energy security and independence?

2. Freedom of mobility

Many UK workers employed by oil and gas companies work in EU countries and *vice versa*. Following a UK exit, the likelihood of experienced UK oil and gas industry workers gaining non-EU citizen status could increase bureaucracy and therefore costs for employers - an outcome that the oil and gas industry would like to avoid, especially as companies are trying to reduce operating costs. In the future many EU companies may favour employing workers from the EU over the UK thereby losing decades of irreplaceable North Sea experience.

The Irish offshore oil and gas sector is currently in a phase of active renewal, with recent successes in the 2015 Atlantic Margin Licensing Rounds and indications of increased exploration.

⁵ <https://www.esri.ie/publications/the-cost-of-natural-gas-shortages-in-ireland/>

At this critical stage in the industry development the necessity to maintain free travel arrangements between the UK and Ireland is paramount in order to facilitate the transfer of appropriate skills vital to oil and gas exploration, development and production.

Key industry Questions:

- What actions will be taken to ensure free travel arrangements between UK and Ireland in order to facilitate the transfer of appropriate skills for the oil and gas industry?
- What actions will be taken to ensure that there will not be increased bureaucracy and resultant costs and delays due to travel restrictions on UK oil industry workers working in the Irish offshore?

3. Loss of an experienced advocate at EU energy policy level

With the departure of the UK, Ireland will lose an experienced, pro-business advocate and ally at EU level in the development of EU energy policy and legislation, and in ongoing negotiations.

The UK has had a major influence on many aspects of the EU energy market over several decades. Marine- and petroleum-related EU Directives have been influenced significantly by the UK which brought a wealth of experience in oil and gas operations and in offshore research. Most recently, for example, major changes in the Emissions Trading Scheme were won through the efforts of the ETS Phase IV Reform Group led by the UK's Ian Duncan MEP (who resigned immediately following the Referendum result but at the request of colleagues on the Environment Committee has agreed to continue as rapporteur pending any change in parliamentary rules in relation to UK MEPs). Significant recent progress has been made in discussions on the Marine Strategy Framework Directive through UK-led efforts.

In future, new petroleum-related EU Directives are likely to have greater shaping by mainland European thinking and experience than hitherto, and may not be optimally crafted or appropriate for application in Irish offshore North Atlantic waters. They are likely to lack the 50 years' experience of offshore exploration, built on more than 4,000 wells, that hitherto came from the UK.

Key industry Questions:

- What actions will be taken to ensure that the experienced voice of NW European environmentally responsible resource development will be heard at EU policy level?
- What actions will be taken to ensure that the knowledge gained through 50 years of offshore exploration and development will not be lost in the development and implementation of ongoing and future energy policy, legislation and practice.

4. Collaboration issues

In the operation of the EU-wide Petroleum Safety Framework (PSF) Directive, the exit of the UK from the EU may result in the UK deciding not to participate in information sharing on Incident Reporting under the PSF. This is a vital source of information and learning on operational, safety and environmental issues to operators and regulators in the Irish offshore from the larger and more mature North Sea exploration and production industry. As Norway (not an EU member) does not participate in the Information Sharing under the PSF, Ireland would receive little information from relevant North Sea and North Atlantic drilling operations.

In recent years there has been growing Ireland-UK collaboration on many aspects linked to natural resources research, exploration and development. These are of mutual benefit for sedimentary basins that lie across both jurisdictions. They include regional surveys and studies

in the Rockall, Irish and Celtic Sea regions. It is unclear how such collaboration may be effected following Brexit.

Being part of the EU has enabled the UK to receive significant and sustained science research funding, while many hydrocarbon-related research programmes in Ireland, funded by the EU, involved critical UK research partners. The oil and gas industry benefitted from research results by working closely with research institutions in Ireland, the UK and EU. Through access to cutting edge research and excellent levels of education given to future oil and gas geoscientists and engineers in universities, this has allowed companies operating in the North Sea and in NW Europe to maintain their competitiveness over the years and has enhanced their reputations as world leaders in new technology adaptation. The likely exclusion of UK research institutions from participation in such EU-wide programmes in the future, with the loss of research personnel exchange, is likely to have a detrimental effect on scientific and technological advancement, training and information exchange.

Key industry Questions:

- What measures will be taken to minimise the information deficit in the PSF and other industry and marine areas resulting from the UK withdrawal?
- What measures will be taken to ensure continued collaboration between Ireland and the UK in the offshore areas that run across both jurisdictions?
- What measures will be taken to mitigate the likely impact of the exclusion of UK scientific expertise from EU-funded programmes that impact on marine and petroleum research?

5. Investment uncertainty for offshore and linked infrastructural projects

Success and downturns in the UK oil and gas industry are often mirrored to a greater or lesser extent in the Irish offshore as Ireland has been seen globally as part of the NW European oil and gas province. Companies exploring successfully in the North Sea and offshore UK could look to Ireland as their next venue, conveniently adjacent, for exploration. As both UK and Ireland were members of the EU it was relatively easy for UK-based explorers to move to offshore Ireland with geological, legislative and regulatory similarities. In recent times an exploration synergy with the eastern Canadian offshore has been developing, offering new potential opportunities for attracting companies to explore offshore Ireland.

Upon completion of EU withdrawal, an independent UK would have greater freedom on energy policy, e.g., freedom from the constraints of the Hydrocarbons Licensing Directive that sets standards which all member states must follow when licensing operators to explore for and produce hydrocarbons, freedom from EU rules prohibiting unauthorised state aid, and possible opt out from EU renewables targets and emissions limits. This could make the UK more attractive and possibly attract new or existing companies that might otherwise have expanded operations into Ireland.

The departure of the UK from the EU could potentially lead to a second Scottish Independence referendum. For the oil and gas industry the uncertainties associated with another such referendum may result in companies delaying or cancelling projects in the UK until the outcome is known. Uncertainty contagion in the UK is likely to extend to Ireland, leading to lack of investment in Irish E&P projects. In addition to the uncertainty of the status of Scotland, in whose offshore most of the UK production occurs, the lack of a direct pipeline connection to another EU country, thereby limiting access to the EU market for Irish gas exports, could be a factor in inhibiting the market for future Irish oil or gas discoveries.

In the latest call for proposals under the Connecting Europe Facility (CEF) to help finance key EU energy infrastructure projects, €200 million will be made available. The money will be focussed on projects already identified as eligible for this funding. Projects include the Moffat gas interconnector between the UK and Ireland to allow reverse flows from Ireland, rather than just from Britain as at present. However, such infrastructure funding for gas interconnectors between Ireland and Scotland may be in doubt following Brexit as the requirements for eligibility are that two or more EU member countries must benefit from the investment.

Key industry Questions:

- What measures will be taken to minimise uncertainty contagion surrounding economic, political and legislative uncertainty in the wake of the referendum result?
- What actions will be taken to minimise the loss of EU finance for Ireland-UK collaborative infrastructural projects such as the upgrading of the gas interconnectors?
- What measures will be taken to attract industry that might be considering early exit from UK offshore waters or extending exploration in North Atlantic conjugate margins?

KEY INDUSTRY MESSAGES

1. The withdrawal of the UK from the EU will increase Ireland's vulnerability in terms of energy import dependency. Ireland will then have no physical energy connection with the EU's energy network as our only gas interconnectors are to Scotland. An obvious route to energy security and independence is through the exploration and development of indigenous offshore natural resources - oil and especially gas. This would also provide substantial economic benefits to Ireland. The challenge is how to continue to foster the momentum of offshore exploration. Encouragement and support for hydrocarbon exploration and development, through appropriate fiscal and regulatory framework, can lead to energy security, help build a low-carbon society through the increased use of indigenous gas, and exploit opportunities for attracting new foreign direct investment.
2. Clarity is required around the issue of access to the EU energy market; both in terms of importing and exporting hydrocarbons.
3. Greater certainty is needed around maintenance of free travel arrangements between UK and Ireland to facilitate the transfer of oil and gas exploration and production expertise from the North Sea, with no added administrative restrictions that would increase costs of exploration and production in Ireland.
4. Ireland will need to cultivate experienced, like-minded allies at EU Parliament, Council and Working Group levels to ensure that any future marine- and petroleum-related Directives and legislation are appropriate to the specific conditions of the Irish offshore, and to ensure that they support the timely and environmentally-responsible development of our much-needed natural resources.
5. The strong links with UK oil and gas agencies, developed over the past decades, need to be maintained in order to be able to draw on their legislative, operational and technical expertise to support our developing oil and gas industry.
6. IOOA will be pleased to partner with government in identifying and addressing the challenges resulting from the UK withdrawal from the EU, and work towards achieving energy security and independence for Ireland.

October 2016