

**DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT**

Approved by the Board of Directors on 24 June 2020¹

CYPRUS

Cyprus FSRU

[Redacted in line with the EBRD's Access to Information Policy]

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¹ As per section 1.4.8 of EBRD's Directive on Access to Information (2019), the Bank shall disclose Board reports for State Sector Projects within 30 calendar days of approval of the relevant Project by the Board of Directors. Confidential information has been removed from the Board report.

For the avoidance of any doubt, the information set out here was accurate as at the date of preparation of this document, prior to consideration and approval of the project.

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ABBREVIATIONS / CURRENCY CONVERSIONS

bcm(a)	billion cubic meter (per annum)	GSA	Gas Sales Agreement
CAGR	Compound Annual Growth Rate	HFO	Heavy Fuel Oil
CCGT	Combined Cycle Gas Turbine	INEA	EU Innovation and Networks Executive Agency
CEER	Council of European Energy Regulators	IPP	Independent Power Producer
CEF	Connecting Europe Facility	LLCR	Loan Life Coverage Ratio
CERA	Cyprus Energy Regulatory Authority	LNG	Liquefied Natural Gas
CfDs	Contracts-for-Differences	MDB	Multilateral development bank
CNG	Compressed Natural Gas	MECI	Ministry of Energy, Commerce and Industry
CNPC	China National Petroleum Corporation	MMbtu	Metric Million British Thermal Unit
CO₂	Carbone dioxide	Mt(pa)	million tons (per year)
CPP	China Petroleum Pipeline Engineering Co Ltd	MW	Megawatt
DEFA	Natural Gas Public Company of Cyprus	NECP	National Energy and Climate Plan
DSCR	Debt Service Coverage Ratio	NO_x	Nitrogen oxides
DSO	Distribution System Operator	NPL	Non-Performing Loan
EAC	Electricity Authority of Cyprus	NTS	Non-Technical Summary
EBIT(DA)	Earnings Before Interest Tax (Depreciation and Amortisation)	OCCO	Officer of the Chief Compliance Officer
EC	European Commission	OTC	Over-The-Counter
EIA	Environmental Impact Assessment	PCI	Projects of Common Interest
EIB	European Investment Bank	PM	Particulate Matters
EPC(OM)	Engineering, Procurement, Construction, (Operation and Maintenance)	PP&R	Procurement Policies and Rules
ESAP	Environmental and social action plan	PPAD	Procurement Policy and Advisory Department
ESD	Environmental and social department	PRs	Performance Requirements
ESDD	Environmental and social due diligence	PRMS	Pressure Reduction and Metering Station
ESMS	Environmental and Social Management System	RAB	Regulated Asset Base
ESMP	Environmental and Social Monitoring Plan	RAVB	Regulated Asset Value Base
ESP	Environmental and Social Policy	SO₂	Sulphur dioxide
ETYFA	Natural Gas Infrastructure Company of Cyprus	SOE	State-owned enterprise
EU	European Union	SEP	Stakeholder Engagement Plan
EUR	Euro	SPV	Special Purpose Vehicle
EURIBOR	Euro Interbank Offered Rate	TC	Technical Cooperation
EU-ETS	EU Emissions Trading System	tcf	trillion cubic feet
FOPC	Financial and Operational Policies Committee	TCSA	Terminal Cost Sharing Cost Agreements
FSRU	Floating Storage and Regasification Unit	TI	Transition Impact
GDP	Gross Domestic Product	TSO	Transmission System Operator
GET	Green Economy Transition	TUA	Terminal Use Agreement
GHG	Green House Gas		

Measures

1 billion cubic meters (bcm) of natural gas = 35,800 Million British Thermal Unit (MMbtu)

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of Natural Gas Infrastructure Company of Cyprus (“ETYFA” or the “Borrower”) a special purpose vehicle incorporated in Cyprus and ultimately 100% owned by the Republic of Cyprus, are submitted for consideration by the Board of Directors.

The facility will consist of a loan to the Borrower in the amount of up to EUR 80 million to finance the acquisition of a floating storage and regasification unit (“FSRU”) and the development of related infrastructure in Vasilikos Bay, Cyprus (the “Project”). The Project will be co-financed by a parallel loan from EIB of up to EUR 150 million and by an EU grant under the Connecting Europe Facility (“CEF”) (EUR 101 million). The remaining project costs will be funded by an equity contribution from Electricity Authority of Cyprus (“EAC”). The loan will be guaranteed by the Republic of Cyprus.

The Project is a critical component in Cyprus' energy strategy with significant energy security, environmental and economic impacts. By giving Cyprus access to the global LNG market it will improve security of supply. By using gas to replace expensive and polluting heavy fuel oil in electricity generation it will reduce CO₂ emissions by 595,000 tonnes annually and substantially improve local air quality. Similarly it will reduce Cyprus's electricity costs, currently among the highest in Europe. In the longer-term the availability of natural gas will facilitate both the development of a liberalised wholesale energy market and much higher penetration of intermittent renewable energy. The significance of the Project is reflected in its designation as an EU Project of Common Interest, and the large scale EU grant support.

The Project accordingly targets the *Resilient* and *Green* Transition Qualities through its contribution to increasing Cyprus' energy security and decreasing the energy sectors emissions of both CO₂ and local pollutants. The Project is 100% GET.

I am satisfied that the operation is consistent with the Bank's Strategy for Cyprus, the Energy Sector Strategy, the Green Economy Transition Approach and with the Agreement Establishing the Bank.

The Project requires an exception from the use of EBRD's Procurement Policies and Rules (“PP&R”). The Project will be co-financed by grant funding from the CEF. As per the regulation establishing the CEF, procurement must be carried out by the European Commission or one of the relevant bodies in accordance with the EU and national public procurement principles. An exception from the use of the Bank's PP&R as envisaged under Clause 2.4 of the PP&R has been reviewed by FOPC on the 18th July 2019 and recommended for approval by the Board to allow the use of national procurement rules.

I recommend that the Board approve the proposed loan substantially on the terms of the attached Report.

Suma Chakrabarti

BOARD DECISION SHEET

CYPRUS – Cyprus FSRU – DTM 50634	
Transaction / Board Decision	Board approval ² is sought for a senior sovereign guaranteed loan of up to EUR 80 million in favour of Natural Gas Infrastructure Company of Cyprus (“ ETYFA ” or the “ Borrower ”), a special purpose vehicle incorporated in Cyprus. The proceeds of the loan will be used for the acquisition of a floating storage and regasification unit (“ FSRU ”) and the development of related infrastructure in Vasilikos Bay, Cyprus (the “ Project ”).
Client	<p>ETYFA is owned 70% by the Natural Gas Public Company of Cyprus (“DEFA”) and 30% by the Electricity Authority of Cyprus (“EAC”). Both DEFA and EAC are 100% state-owned.</p> <p>DEFA was established in November 2007 to facilitate the introduction and distribution of natural gas in Cyprus. DEFA and ETYFA are both newly established companies founded to develop the gas market in Cyprus with no sources of income yet.</p> <p>EAC is the Cypriot state-owned utility which owns and operates all three thermal power stations in Cyprus. EAC has been in operation for more than 65 years. [REDACTED].</p>
Main Elements of the Proposal	<p>Transition impact: Resilient: the investment will introduce natural gas to Cyprus for the first time thereby decreasing the country's high dependence on imported oil and petroleum products. The project also includes policy dialogue on electricity market reform with the Cypriot energy sector regulator and market operator. Green: the Project will contribute to the decarbonisation of Cyprus' energy sector by switching electricity generation from fuel oil to natural gas, with significant reductions in emissions of both CO₂ and local pollutants.</p> <p>Additionality: Financing structure: EBRD offers a tenor above the market average, which is necessary to structure the project. EBRD investment is needed to close the funding gap alongside EIB and EU funding.</p> <p>Sound banking: debt service capacity protected by a regulated tariff and robust contractual revenue structure. Sovereign guaranteed loan.</p>
Key Risks	<p>Management /Implementation risk: management capacity is being strengthened, strong owner's engineer support</p> <p>Construction risk/operational risk: single turnkey Engineering, Procurement, Construction, Operation and Maintenance (EPCOM) structure with strong EPC consortium, proven technology</p>
Strategic Fit Summary	<p>Energy Sector Strategy by supporting gas as a transitional fuel towards a low-carbon transition economy that is both secure and affordable.</p> <p>Strategy for Cyprus by supporting investments in new sources of energy and the switch of electricity generation from heavy fuel oil to cleaner fuels.</p> <p>Green Economy Transition Approach by promoting the transition to a low-carbon energy sector.</p>

² Article 27 of the AEB provides the basis for this decision.

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	<ul style="list-style-type: none"> • Senior loan of up to EUR 80 million in favour of ETYFA to finance the acquisition of an FSRU and the development of related infrastructure in Vasilikos Bay, Cyprus (the Project). ETYFA is 70% owned by DEFA and 30% owned by EAC. Both DEFA and EAC are 100% state-owned. • The Loan will benefit from a sovereign guarantee from the Government of Cyprus. • Parallel debt financing will be provided by EIB and the Project will receive grant financing from the EU Connecting Europe Facility (CEF) [REDACTED]. EAC will provide equity financing. [REDACTED].
Existing Exposure	None
Maturity / Exit / Repayment	Tenor of 20 years from the date of signing of the Loan Agreements [REDACTED].
AMI eligible financing	N/A
Use of Proceeds	<ul style="list-style-type: none"> • The proceeds of the EBRD loan will be used to finance the acquisition of an FSRU and the construction of associated infrastructure (including jetty, offshore and onshore pipeline) to import, store and regasify liquefied natural gas (LNG) back to its normal gaseous state. The FSRU will be permanently anchored to the seabed about 1.3 km off the coast of Limassol in Vasilikos Bay and will connect directly to the adjacent and largest power station in the country, the Vasilikos power station. • The Project is being procured under a single Engineering, Procurement, Construction, Operation and Maintenance (EPCOM) contract and the proceeds of the loan will be disbursed against EPCOM invoices. • EBRD will hire a Lender's Engineer to provide technical consultancy services in relation to the Project implementation and effective monitoring of the disbursements and use of proceeds. The Bank will also receive regular covenanted construction and operating reports.
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	<p>Sponsors: DEFA and EAC</p> <p>Co-financiers: EIB and the European Union (through the Connecting Europe Facility)</p> <p>Sovereign guarantee: Ministry of Finance and Ministry of Energy, Commerce and Industry (MECI)</p>
Conditions to subscription / disbursement	[REDACTED]
Key Covenants	<ul style="list-style-type: none"> • Limitation on additional capex and financial debt. • Maintain the owner's engineer with adequate resources and suitably qualified personnel • Carry out the Project in accordance with the Project Implementation Plan • [REDACTED]
Security / Guarantees	Sovereign guarantee
Other material agreements	Guarantee Agreement, Terminal Use Agreement and Terminal Cost Sharing Agreement.
Associated Donor Funded TC	Project Preparation: the technical due diligence and analysis of the carbon intensity of the Project were completed and supported by TC assignment. [REDACTED]

	<i>Policy dialogue:</i> Electricity Market Reforms in Cyprus. The Bank is working with Cyprus Energy Regulatory Authority (CERA) and the Electricity Market Operator to assess the suitability of the new electricity arrangements and associated market rules being proposed in Cyprus for the development of the market and achievement of a single energy market (<i>more details are provided Section 1.2 Transition Impact, objective 1.2</i>). [REDACTED]		
CLASSIFICATIONS		APPROVAL TIMETABLE	
Environment	Category B	Concept Review	8 Feb 2019
Procurement	Public	PSD release date	9 Aug 2019
Portfolio	Public sovereign (sovereign guaranteed)	PSD translation release date:	23 Aug 2019
Probability of Default (PD rating 1-7, not %)	[REDACTED]	Structure / Final Review	1 Nov 2019
Loss Given Default (LGD %)	[REDACTED]	Board Approval	10 June 2020
RAROC (before costs)	[REDACTED]	Signing	[30 June 2020]
ETI Score	67		
GET % share of project	100%		

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

Cyprus's energy sector faces major challenges arising from its isolation, small size and lack of indigenous resources. It is the only member of the European Union which remains fully isolated without any electricity or gas interconnections. In particular, 90% of its electricity supply relies on imported, expensive and polluting petroleum products. As a consequence, Cyprus:

- has one of the highest levels of CO₂ intensity in Europe;
- has the highest electricity prices in Europe; and

relies heavily on power plants burning heavy fuel oil that produce large volumes of local pollutants.

The proposed Project addresses these challenges by delivering the infrastructure that will allow Cyprus to import natural gas. It comprises the purchase of a floating storage and regasification unit (FSRU) and construction of associated infrastructure. Once complete, the Project will allow the Vasilikos power station, the main supplier of electricity to Cyprus, to switch its operation from heavy fuel oil and diesel to gas.

The Project is of critical strategic, economic and environmental importance to Cyprus. It will transform the electricity sector from its current polluting and expensive model. More specifically the Project will:

- **Dramatically improve the environmental characteristics** of the country's power sector. The Project will result in the reduction of CO₂ emissions by 595,000 tonnes annually. In Cyprus, CO₂ emissions savings will represent more than 10% reduction in the national carbon emissions. It will also reduce SO₂ emissions by 6,000 tonnes and dust emissions by 175 tons annually on average. The Bank's economic analysis values the emissions reductions at EUR 100 million annually on average.
- **Reduce the cost of electricity** by reducing EAC average generation cost by at least 10% and up to 30%, thanks to the improved efficiency at EAC's power station with the use of gas, the reduced costs of emissions allowances and the lower cost of gas compared to petroleum products³.
- Significantly **improve Cyprus's energy security** by improving energy reliability and flexibility and by giving the country access to the global LNG market (*see further Section 4 and Annex 3*).
- **Demonstrate best international practices for gas infrastructure projects.** The Project will apply the highest standards in the industry by including a procedure and systems of detection, measurement and reduction of methane fugitive emissions to reduce the carbon footprint of natural gas.
- Allow for greater **penetration of renewable energy**. Cyprus' ambitious long-term goals for renewable energy penetration require flexible capacity to match intermittent wind and solar, a role for which gas-fired generation is well suited.

The Project will complement the Bank's ongoing policy dialogue initiative in the electricity sector. Cyprus is currently undertaking a revision of its market model and rules towards the development of an electricity market that will allow competition in electricity generation and

³ These estimations include the scenario where oil prices remain low in the long-term post Covid-19 crisis.

supply. The Bank is providing technical assistance to the Cyprus Energy Regulatory Authority (CERA) and the Electricity Market Operator to assess the new electricity arrangements and associated market rules being proposed under the new market model. The Bank's support aims at optimising and facilitating the participation of renewables in the electricity market of Cyprus.

The Project is in line with the priorities of both the **Energy Sector Strategy 2019-2023** which emphasises the role of gas in enabling the low-carbon transition to shift away from carbon-intensive fuels. The Project also in line with the **Strategy for Cyprus** which recognises the challenges faced by the energy sector and seeks to support "*investments in new sources of energy to increase the competitiveness of local enterprises*" and "*the switch of electricity generation from heavy fuel oil to cleaner fuels*". The Project is 100% compliant with the **Green Economy Transition approach** by promoting the transition to a low-carbon energy sector⁴. Reflecting the Project's strategic importance it has been designated as an EU Project of Common Interest (PCI) and benefits from a significant grant under the EU Connecting Europe Facility.

The Project was developed well before the COVID-19 crisis and its fundamental long-term benefits of significant environmental improvement, reduced energy costs and increased energy security are only more relevant in this new context. The Bank's support in a time of reduced availability of finance generally is crucial in ensuring this transformative project progresses.

The Project requires an exception from the use of EBRD's Procurement Policies and Rules ("PP&R"). The Project will be co-financed by the Connecting Europe Facility (CEF) and EIB. As per the regulation establishing the CEF, procurement must be carried out by the European Commission or one of the relevant bodies in accordance with the EU and national public procurement principles. An exception from the use of the Bank's PP&R as envisaged under Clause 2.4 of the PP&R has been reviewed by FOPC on the 18th July 2019 and recommended for approval by the Board to allow the use of national public procurement rules.

1.2 TRANSITION IMPACT

The table below sets out the TI Objectives and details of the project. The relevant Monitoring Indicators and timing for their delivery are shown in Section 2.

Obj. No.	Objective	Details
Primary TI Quality: Resilient		
1.1	The Project will introduce gas into a country for the first time and will significantly contribute to the diversification of the country's energy mix.	Cyprus is the only member of the EU which is fully isolated without any electricity or gas interconnections, and is one of the most vulnerable EU member states in terms of energy dependency and security of supply. Cyprus currently relies on imported oil and petroleum products for almost its entire energy consumption, accounting for more than 90% of total primary energy supply and over 8% of its GDP. The project will introduce natural gas to Cyprus for the first time, thereby improving the country's security of energy supply and the diversification of imported energy sources. At present, most of

⁴ The investment is an activity that results in power plants' switch from a more GHG-intensive fuel to a different and less GHG-intensive fuel type as in the joint-MDB list of activities eligible for classification as climate mitigation finance.

		<p>the imported oil is sourced from Greece and Israel and, due to relatively small import amounts, Cyprus faces barriers in changing to other source countries. In contrast, LNG can be imported from a wide range of countries.</p> <p>Natural gas will initially be directed towards power generation, connecting with the Vasilikos power station which currently produces more than half of Cyprus total electricity from heavy fuel oil and diesel. Subsequently, remaining gas capacity may be made available to two other existing power stations as well as independent power producers (IPPs). The Electricity Authority of Cyprus will therefore be the initial buyer of gas but the excess capacity of the FSRU will be made available to third parties and will be subject to periodic market tests for gas allocation. The project is therefore the first step in the creation of a competitive gas market in Cyprus while enabling increased competition in the electricity market. At a later stage, the use of gas may be extended beyond the power sector to the industrial, transportation, petrochemical and residential sectors.</p>
1.2	The project entails a policy dialogue initiative that has been assessed as Good by the sector economist.	<p>The gas and power sectors share the same regulator in Cyprus (CERA). The country is currently undertaking a revision of its market model and rules towards the development of an electricity market that will allow competition in electricity generation and supply and to be in line with the EU's Target Model. The introduction of natural gas for power generation in Cyprus is a prerequisite for an effective market liberalisation. In this context, the Bank will, through a technical cooperation assignment, work closely with CERA and the electricity market operator to assess the new electricity arrangements and associated market rules being proposed. The assignment will make recommendations for changes to the rules to ensure completeness, consistency and suitability with a particular focus on implications for promoting investment in renewables.</p>
Secondary Transition quality: Green		
2.1	The percentage of EBRD use of proceeds allocated to the project that qualifies as GET is 50% or higher	<p>The project qualifies as 100 per cent GET, contributing to climate mitigation.</p> <p>The project will allow Cyprus to switch from fuel oil to natural gas based electricity generation. The gas imported to the market through the FSRU will be supplied to the Vasilikos power plant, which is designed to run either on fuel oil or natural gas. No capex or lifetime extension of the plant will be required to enable this switch. The transition to natural gas fired generation will enable a significant reduction of the plant's GHG emissions and will importantly result in a substantial improvement of local air emissions, thanks to the significant reduction of SO₂, particulate matters and NO_x, emissions.</p> <p>The project will also support the integration of the increasing penetration of intermittent renewable energy in Cyprus, through enabling gas fired generation as a flexible and reliable source of capacity.</p> <p>Moreover, once operational, the project will apply the highest standards in the industry by including a procedure and systems</p>

		of detection, measurement and reduction of methane fugitive emissions (i.e. sensors and instrumentation).
2.2	The environmental impact of the Project is expected to meet or exceed one or more of the quantitative physical scale thresholds as outlined in the GET TI assessment methodology	<p>The switch from GHG-intensive fuel to cleaner fuel for electricity generation will lead to greenhouse gas emissions savings of 595,000t CO₂/year.</p> <p>The project will also bring about significant local air pollution benefits. According to quantification as part of the GHG assessment, SO₂ and PM emissions reductions are expected to amount to 6 thousand tons and 175 tons per year respectively on average over the life of the facility.</p>

Delivery risks

The main risks to delivery include: (i) commercial success of the FSRU, which is mitigated by analysis showing sufficient demand for the FSRU to justify the investment across all plausible scenarios; and (ii) commitment of the government and the sector regulator to liberalise the electricity sector.

1.3 ADDITIONALITY

[REDACTED]	[REDACTED]

Additionality sources	Evidence of additionality sources
<p>Financing structure EBRD offers a tenor and/or a grace period above the market average, which is necessary to structure the Project.</p> <p>[Public sector] EBRD investment is needed to close the funding gap. At the same time, EBRD does not crowd out other sources, such as from IFIs, government, commercial banks and/or complements them.</p>	<p>The Loan tenor of 20 years would not be achievable by the client without IFI involvement. Few commercial banks can offer [REDACTED] tenors which is still not suitable for financing very long duration assets like this FSRU. Short project periods increase the annual project amortisation charge for the infrastructure to a point that this leads to an unacceptable increase in the cost of electricity generation. The Project will be co-financed by the EIB. [REDACTED].</p>
<p>Standard-setting Client seeks EBRD expertise on higher environmental standards, above 'business as usual' (e.g. adoption of emissions standards, climate related ISO standards etc.).</p>	<p>Actions under the ESAP go beyond local requirements including in terms of stakeholder engagement, grievance mechanisms and emissions control and reporting. As part of EBRD conditionality the company will include a procedure and systems of detection, measurement and reduction of methane fugitive emissions.</p>

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
Sponsors/ Management Risk	<i>Low/ Medium</i>	<p>DEFA, the lead sponsor and the entity effectively managing the Project, currently has limited in-house managerial or technical capacity for a project of this scale.</p> <p>Mitigation:</p> <ul style="list-style-type: none"> - <i>DEFA will be advised by an Owner's Engineer who will act in the interest of DEFA/ETYFA as an interface with the EPCOM contractor in the Project oversight role. Its role will include project, risk and engineering management as well as FSRU, jetty and onshore technical lead. The Owner's Engineer will also lead the commissioning and inspection. It is in the process of being selected through competitive open tender.</i> - <i>The Project is a strategic priority for Cyprus and the government retains an important role in the implementation of the Project through the Project's Steering Committee.</i> - <i>EAC retains a close control and interest over the Project as a 30% shareholder and sole initial offtaker. EAC has an extensive and proven track-record on successfully implementing and managing large scale utility projects over the past 65 years.</i>
Construction, technology and operation Risk	<i>Low/High</i>	<p>The Project could be adversely affected by construction delays and cost overruns and could be also exposed to operational problems and/or failure to perform.</p> <p>Mitigation:</p> <ul style="list-style-type: none"> - <i>The Project is being sourced under a single turnkey EPCOM approach with a single point of responsibility. The EPCOM provider is a consortium with extensive experience and proven track-record.</i> - <i>The Project uses proven technology and technology risk is limited.</i> - <i>The EPCOM includes appropriate and customary performance guarantees [REDACTED].</i> <ul style="list-style-type: none"> - <i>The Lender's Engineer will monitor the construction, will regularly visit the site and will inspect the Project at completion. The co-financiers (EIB and CEF) will also closely monitor the Project.</i>
Regulatory risk	<i>Low/High</i>	<p>DEFA/ETYFA activities and sources of revenues are regulated by CERA and are exposed to regulatory changes.</p> <p>Mitigants:</p> <ul style="list-style-type: none"> - <i>The Project brings substantial benefits to the country as detailed in this document and, as such, benefits from the strong support of the Government of Cyprus and the EU.</i> - <i>Cyprus has a transparent regulatory framework in line with EU rules and regulations. CERA has a proven track-record as the regulator on the electricity market and a key mandate to support the introduction, viability and continuity of natural gas supply within the country's energy mix. The regulatory framework and tariff methodology for natural gas is transparent about anticipating the liberalisation of the market and the current emergent status of the market.</i>
Debt service capacity	<i>Low/ Medium</i>	<p>The repayment of the loan will depend on the revenues of ETYFA which is a newly established SPV.</p> <p>Mitigations:</p> <ul style="list-style-type: none"> - <i>The Project is a regulated asset, [REDACTED] and are protected by a robust contractual structure over the full tenor of the financing.</i>

		<p>[REDACTED]</p> <ul style="list-style-type: none"> - <i>The sensitivity analysis confirms the robustness of the Project financial structure and debt service capacity.</i> - <i>The Loan will benefit from a guarantee from the Government of Cyprus.</i>
Off-take risk, gas demand & price risk	<i>Low/ Medium</i>	<p>At the beginning of operations EAC will be the sole offtaker. In addition, there is a risk that a sustained lower gas demand (e.g. steep rise in international LNG prices) may create pressure from EAC to renegotiate the Terminal Cost Sharing Agreement (TCSA).</p> <p>Mitigations:</p> <ul style="list-style-type: none"> - <i>EAC is a shareholder of ETYFA and the Project makes commercial sense for its stakeholders. It will allow EAC to increase the efficiency of its main power station and substantially reduce its generation costs even in a long-term low oil prices environment scenario. There is a strong alignment of interests between the Borrower and the initial offtaker.</i> - <i>EAC is an acceptable and creditworthy counterparty as being the dominant vertically integrated state owned player in the Cypriot electricity market. EAC benefits from its ability to pass through costs to its end users via regular tariff adjustments and has broadly stable credit metrics and moderate leverage in recent years.</i> <ul style="list-style-type: none"> - <i>Once new gas buyers will enter the market, under the TCSA, each gas buyer will have to provide a standby letter of credit to DEFA in an amount adequate enough to cover its obligations (capacity charge participation share) for a period of six months</i> - <i>Both EAC and DEFA are state-owned and regulated by the CERA. There is a strong interrelation between the gas (i.e. the Project) and electricity markets and the offtake risk is mitigated by the strategic nature of the Project for Cyprus's broader energy situation and security.</i> - <i>Both the financial analysis and the Economic Assessment sensitivities confirm the robustness of the Project to major price changes.</i> - <i>The Loan will benefit from a Sovereign guarantee.</i>
Sovereign Risk	<i>Low/High</i>	<p>The Loan ultimately relies on guarantee from the Republic of Cyprus. Although visibility over the full impact of the Covid-19 crisis on the Cyprus economy remains limited and will depend on its duration, the Cypriot economy is expected to contract by 5-9.7% in 2020 according to initial government's estimations, with the impact expected to be temporary. IMF forecasted a 6.5% contraction of GDP in 2020 followed by a sharp rebound in 2021. As of May 2020, EBRD expects GDP to fall by 6% in 2020, with a rebound of 5% in 2021.</p> <p>Mitigations:</p> <ul style="list-style-type: none"> - <i>Cyprus is investment grade (rated 4.3, BBB- reconfirmed by Fitch on 3rd April 2020) and the government's commitment to the Project is well defined.</i> - <i>The fundamental economic, environmental and energy security benefits of the Project continue to be relevant in the current situation, including with low hydrocarbon prices.</i>

2. MEASURING / MONITORING SUCCESS

<i>Overall objectives of project</i>	<i>Monitoring benchmarks</i>	<i>Implementation timing</i>
On-time Project implementation	Completion according to the timeline and within the budget	During implementation

<i>Transition Impact Monitoring Indicators and Benchmarks</i>						
Quality	Obj. No.	Monitoring Indicator	Details	Baseline	Target	Due date*
Resilient	1.1	Net increase in infrastructure (FSRU) usage	Annual fuel volumes supplied through the FSRU above 0.7 bcma	N	Y	31 Dec 2023
	1.2	New product (gas) introduced to the Cypriot market	Opening of the gas market: launch of the first Open Season / Market Tests for FSRU excess capacity to be made available to third parties.	N	Y	31 Dec 2025
	1.3	Legal, institutional or regulatory frameworks in target areas improved (Y/N)	Adoption by CERA and Electricity Market Operator of the revised market model and rules in line with key recommendations from the Bank's TC.	N	Y	31 Dec 2023
Green	2.1	CO _{2e} reduced/avoided (tonnes/yr)	Total reductions in CO _{2e} emissions of 595,000 ton per annum.	0	595,000	31 Dec 2023
	2.2	Air emissions reduced: SO ₂ (ton/yr)	Total reductions in air emissions per annum of 6,000 tons SO ₂ .	0	6,000	31 Dec 2023
	2.3	Air emissions reduced: PM (ton/yr)	Total reductions in air emissions per annum of 175 tons PM.	0	175	31 Dec 2023
	2.4	Improved environmental standards	Fugitive emission control standards improved through the development and implementation of fugitive methane emissions monitoring, reporting and verification system	N	Y	31 Dec 2025

3. KEY PARTIES

3.1 BORROWER

The FSRU will be owned by a newly established special purpose entity in Cyprus, the Natural Gas Infrastructure Company of Cyprus (**ETYFA**) which is owned by DEFA (70%) and EAC (30%).

3.2 SPONSORS

The Natural Gas Public Company of Cyprus (**DEFA**) will be the entity effectively managing the Project. It is 100% state owned and was established in November 2007 as a Limited Liability Company to facilitate the importation and distribution of natural gas to the Cyprus energy market. DEFA will be established as a Public Law Entity prior to operations and will be granted monopoly status in buying (importing), selling, transmitting, distributing and storing natural gas. This is compliance with the EU gas Directive 2009/73/EC under which Cyprus, as an emergent and isolated market, has secured derogation rights allowing natural gas commercial operations under a monopolistic regime for a limited period of time. DEFA is governed by a 9 member Board of Directors and has so far been advised by a group of coordinated independent reputable companies for the implementation of the Project (Navigant, WSP, Rogan Associates, DLA Piper). DEFA's financial highlights are included in Annex 5.

Electricity Authority of Cyprus (**EAC**) is the Cypriot state-owned vertically-integrated utility which owns and operates all three thermal power stations in Cyprus with a combined installed capacity of 1,478MW, of which 1,018MW have dual fuel capacity all situated at Vasilikos and Moni. EAC is also responsible for supplying and distributing electricity to all consumers. EAC has been in operation for more than 65 years. [REDACTED]EAC will initially be the sole consumer of natural gas when the Project is brought into operation. It is expected, however, that independent gas-fired generation projects will be constructed in the next few years. EAC's financial highlights are included in Annex 5.

3.3 EPC CONTRACTOR

The Project will be delivered under a comprehensive, turnkey engineering, procurement, construction, operating and maintenance contract. ETYFA procured this contract under an open international tender launched in October 2018. ETYFA received three bids and selected the preferred bidder on 23rd August 2019. It signed the EPCOM contract in December 2019 and expects to initiate the works by August 2020. The Bank reviewed the tender and contract award and proposed an exception from the Bank's PP&R on the basis set out in the memo to FOPC on 18th July 2019 (FOPC Minutes at CS/FO/M/19-33).

The selected EPCOM contractor is a consortium comprised of (i) a joint venture led by China Petroleum Pipeline Engineering Co Ltd (**CPP**) with METRON S.A. (**Metron**); (ii) Hudong-Zhonghua Shipbuilding Co. Ltd; and (iii) Wilhelmsen Ship Management Limited.

- **CPP** is an oil & gas pipelines and tanks engineering and construction firm based in Langfang, China. CPP is a subsidiary of the state-owned energy group China National Petroleum Corporation (**CNPC**), the third largest oil company in the world [REDACTED]. CPP was founded in 1973 for the building of Daqing-Fushun oil pipeline, the first long-distance crude oil pipeline in China, and has built over 22 million tons capacity of LNG terminals including the Shenzhen LNG Peak Shaving Station.
- **Metron** is a private Greek EPC contractor founded in 1997, specialized in the supply and installation of electromechanical solutions in the oil and gas industry supplying prefabricated solutions (skids) for transportation, processing, treating and measuring of gases and liquids. [REDACTED]

- **Hudong-Zhonghua Shipbuilding** is a major shipbuilding company and it is owned by China State Shipbuilding Corporation, the second largest shipbuilding conglomerate in the world. It has three shipyards in Shanghai and has built more than 3000 various ships including the first LNG carrier built in China. Hudong-Zhonghua Shipbuilding will be in charge of the FSRU conversion.
- **Wilhelmsen Ship Management** is part of the Wilhelmsen Group of companies, a leading maritime industry group headquartered in Norway and employing more than 21,000 people. Wilhelmsen Ship Management provides third party ship management services including technical management, crew management, risk management and systems, vessel accounting and procurement services. [REDACTED].

4. MARKET CONTEXT

- There are currently no gas or electricity interconnectors to Cyprus and the country does not currently produce any primary sources of energy other than small amount of renewables. Imported oil and petroleum products continue to dominate the energy mix, representing c.91% of the gross power generation in 2018. Most of the imported energy sources are from neighbouring countries refineries (Greece and Israel) and the possibility to diversify the energy supply from third countries is limited due to the relatively small demand.
- There are currently three conventional power stations in operation in Cyprus out of which Vasilikos represents more than 60% of the generation. Cyprus has one of the highest electricity prices in Europe, at approximately EUR 0.16 per kWh for non-households and EUR 0.22 kWh for households at end of 2019. The implementation of the Project is expected to reduce Cyprus average generation costs by at least 10% and up to 30%, depending *inter alia* on forecast LNG and oil prices⁵.
- Cyprus is expected to start producing indigenous gas from 2025 from Aphrodite offshore gas field (sole proven reserves at present, 200km offshore Cyprus). The gas will be transported via pipeline to Egypt's Idku facility for liquefaction and further export. Proven reserves from recent gas discoveries at Calypso and Glaucus fields (made in February 2018 and 2019 respectively) still need to be confirmed.
- There is a plan to connect Cyprus to the power grids of Greece and Israel via a 1,518km multidirectional undersea cable (EuroAsia Interconnector). This [REDACTED]2,000 MW interconnector project which has not yet reached final investment decision. If it proceeds, commissioning of the second phase of the interconnector (from Crete to Cyprus) is not expected before 2025 and the third phase (connecting Cyprus to Israel) thereafter.
- The energy policy of Cyprus is harmonised with the energy policy of the EU. The Cyprus Energy Regulatory Authority (CERA) regulates both the electricity and gas markets. Cyprus, as an emergent and isolated market, has secured derogation rights from certain provisions of the EU gas Directive (2009/73/EC) which are provided for assisting such markets in their transition to becoming functional and competitive. Cyprus' gas market will therefore operate under a monopolistic regime for an expected period of 10 years. The Project will receive an exemption from the Third Party Access rule for new infrastructures (as per Article 36 of EU gas Directive). More details are provided in Annex 4.
- While the electricity supply has been gradually liberalised, EAC remains the sole supplier in the country and generates more than 90% of Cyprus' electricity. The country is in a

⁵ Source: Economic Assessment. This includes a scenario where oil prices would remain low and gas prices would remain stable in the long-term post Covid-19 crisis.

transitional phase towards a revision of its electricity market model that will allow more effective liberalisation and competition in supply and generation.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 FINANCIAL PROJECTIONS

[REDACTED]

5.2 SENSITIVITY ANALYSIS

[REDACTED]

5.3 PROJECTED PROFITABILITY FOR THE BANK

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Categorized B (2014 ESP). The Project was initially categorised as IESE. The initial examination considered the Environmental and Social Policy (ESP) requirements and specific criteria that trigger the classification of a project as ‘A’, including the EU EIA Directive provisions in respect of projects that have significant effects on the environment and should be subject to a systematic assessment, Cypriot EIA legislation and the outcome of the project’s EIA. Taking into consideration the above combined with the Project’s manageable potential environmental and social risks and the site location within an industrial area, the Project is categorised as Category ‘B’ as per EBRD’s ESP.

Environmental and social due diligence (ESDD) has been conducted by an external consultant and included review of categorisation of the Project; review of the local EIA and the corporate systems in place prepared for the Project against the applicable Performance Requirements (PRs); identification of the key Environmental and Social (E&S) issues and risks of the Project; and identification of actions required to bring the Project in line with the EBRD’s PRs. The ESDD also included the development of a Non-Technical Summary (NTS) and a stakeholder engagement plan (SEP) to guide future stakeholder engagement and information disclosure activities.

The main risks associated with the Project are related to impacts to marine biodiversity, safety of the facility and emergency response planning and possible impacts to existing fishing activities in the area. The main impacts on biodiversity are related to marine flora and fauna disturbed by construction works (sediment suspension and water turbidity) and the navigation and mooring of vessels at the operational stage. A Marine Environmental Baseline Study was prepared for the Project and a Biodiversity Management and Monitoring Plan including provisions for Marine Mammals and Turtles will be prepared for the Project as per the permit issued by the Ministry of Environment.

As with any project requiring construction and operation, there may be potential impacts on the health and safety of the workers. The EIA proposes several mitigation measures for this issue. Training will be provided to the workers and a Health and Safety Management Plan will be developed for the Project by the EPCOM contractor. In addition, health services will be provided to the employees at the construction sites and a Grievance Mechanism will be established for the workers. Road safety signs and protective equipment will also be provided

and a Traffic Management Plan for the construction phase of the Project will be prepared to ensure community health and safety.

The location of the FSRU ensures adequate distance from the shore with regard to protection of community health and safety. The onshore facilities will be fenced and the access will be restricted. It is planned that the FSRU and the equipment used will have safety systems in place to identify and prevent safety risks (emergency shutdown, leakage limitation, fire protection, flood control and crew escape as well as any other security system and equipment required by the competent authorities and good industry practice). A safety zone will also be defined around the FSRU in collaboration with the port authorities and the Vasilikos Bay management authority to minimise collision risk and occupational and community health and safety risks (e.g. fishermen). A series of risk assessment studies in accordance with the Seveso III Directive have been prepared for the Project. All the scenarios that may potentially have an impact on community health and safety have been assessed. A Risk Assessment Analysis has been prepared for the Project where the hazards and the likelihood of accidents and their impact on the public safety are investigated. The Project design has taken into consideration the seismicity of the region and the potential risks resulting from damage of the pipeline and FSRU because of earthquakes. Other natural hazards like extreme waves, winds and temperatures have also been taken into consideration. The client will review and monitor its contractors to ensure that proper actions are taken for the protection of the community in terms of environment and health and safety.

The area of the Project includes a small area with historic contamination (phosphor-gypsum lagoon) from previous industrial activities in the area (fertiliser plant). The Project will have positive impacts as remediation of the phosphor-gypsum lagoon area will be completed prior to the commencement of the construction works.

The nearshore and offshore area is used by local fishermen although fishing is prohibited according to the Master Plan of the area. The offshore area is already disturbed due to several industrial activities taking place and it is expected that the access restriction, loss of fishing fields and temporary impacts caused by the FSRU operation might impact further the limited fishing activities which are ongoing in spite of the prohibition. Potential impacts associated with this will be further assessed and addressed in accordance with PR5 prior to the start of the construction. The client will identify the extent of the fishing activities in the area and consider further consultation with stakeholders involved in fishing activities within the SEP.

Although the direct CO₂ emissions of the Project are expected to be between 15 -20Kt CO₂ per year (depending on the technology that will be finally selected for the regasification process), the Project will contribute to the reduction of CO₂ emissions in power generation on a national level by substituting the current use of heavy fuel and diesel oil, which are currently the main fuels used in Cyprus for energy generation and produce higher CO₂ emissions. Additionally, the switch to natural gas will contribute significantly to reduction of SO₂ and particulate matters in the area around Vasilikos Power Station.

An Environmental and Social Action Plan (ESAP) has been prepared and agreed with the client in order to ensure the Contractor / ETYFA implements the project as planned and that the Project is developed in line with the PRs. The ESAP includes amongst others: development of Environmental and Social Policy; establishment of a project specific Environmental and Social Management System (ESMS) to define the processes, monitoring and reporting requirements; strengthening ESHS capabilities to monitor and follow up the environmental and social performance of the Project; preparation of an Environmental and Social Monitoring Plan (ESMP) and Health and Safety plan; further consultation with affected communities and relevant groups/stakeholders involved in fishing activities; development and implementation of a Marine Biodiversity Management and Monitoring Plan including the observation of the area for the potential presence of marine mammals; development and

implementation of a Stakeholder Engagement Plan (SEP) appropriate to the nature and scale or the risks, impacts and development stage of the Project.

With implementation of the ESAP and the ESMPs this project is structured to be compliant with the EBRD Performance Requirements. ESD will monitor construction to verify this compliance.

6.2 INTEGRITY

In conjunction with OCCO, integrity due diligence was undertaken on the Borrower (ETYFA), its shareholders (Natural Gas Public Company of Cyprus (DEFA) 70%; Electricity Authority of Cyprus (EAC) 30%), senior management, and members of the EPCOM consortium (China Petroleum Pipeline Engineering Co Ltd; Metron S.A.; Hudong-Zhonghua Shipbuilding Co Ltd; and Wilhelmsen Ship Management Ltd).

The review [REDACTED] concluded that this Project does not pose an unacceptable integrity or reputational risk to the Bank. The project will be co-financed by the EIB and an EU grant. [REDACTED].

All actions required by applicable EBRD procedures relevant to the prevention of money laundering, terrorist financing and other integrity issues have been taken with respect to the project, and the project files contain the integrity checklists and other required documentation which have been properly and accurately completed to proceed with the project.

6.3 ECONOMIC ASSESSMENT

The GHG emissions due diligence conducted for this project showed that the investment will entail expected Scope 1 and Scope 2 annual GHG in the range of 15,000-20,000 t CO₂e/year. At these levels this would not fulfil the qualifying criteria for an economic assessment. However, as the EBRD is keen to consider the upstream or downstream impact of its projects, the methodology for the economic assessment of EBRD projects with high GHG foresees that Scope 3 GHG emissions may be taken into consideration in some infrastructure investments, where these are significant. This is the case of this Project, where GHG mostly relate to the use of gas that the investment facilitates. Thus management has decided to undertake the assessment on this basis.

The economic assessment concludes that the Project would offer a positive benefit to society if implemented. It has the potential to significantly reduce electricity generation costs, entail environmental benefits in terms of emissions (both GHGs and local air pollution) and increase the security of electricity supply of Cyprus. This conclusion is robust to plausible sensitivity checks.

The assessment compared these outcomes with those that could be obtained through other energy infrastructure options available to Cyprus. Based on our assessment, the highest benefits to society are in a scenario in which the Project is combined with an interconnector alongside an enhanced roll out of renewable generation. In the scenario where these infrastructure options are deployed together, the Project is utilised less but overall generation costs are lower, emissions reductions are higher and there is enhanced security of electricity supply.

Given the short lead time of the Project, reduced generation costs and emissions savings can be delivered from 2022, while the interconnector is assumed to come online no earlier than 2025. The assessment shows that even if the Project was retired when the interconnector

comes online, the economic value of its benefits would warrant investment. In practice, the implementation of the Project offers insurance against a delay in the interconnector or disruption to its operation.

The risk of locking-in of fossil fuel infrastructure in the medium and long term are considered low. Comfort is taken for three reasons: first, the Cypriot electricity system is covered by the EU-Emissions Trading System (ETS), which is the key EU instrument to cost-effectively deliver an electricity system consistent with EU climate change ambition. Second, it is likely that some gas generation will be required even in 2040 to support the cost-effective implementation of renewables. Third, the Project could support the use of low-carbon gas in the form of synthetic methane should it become economically viable in the long term, although this is not expected to be the case in coming decades..

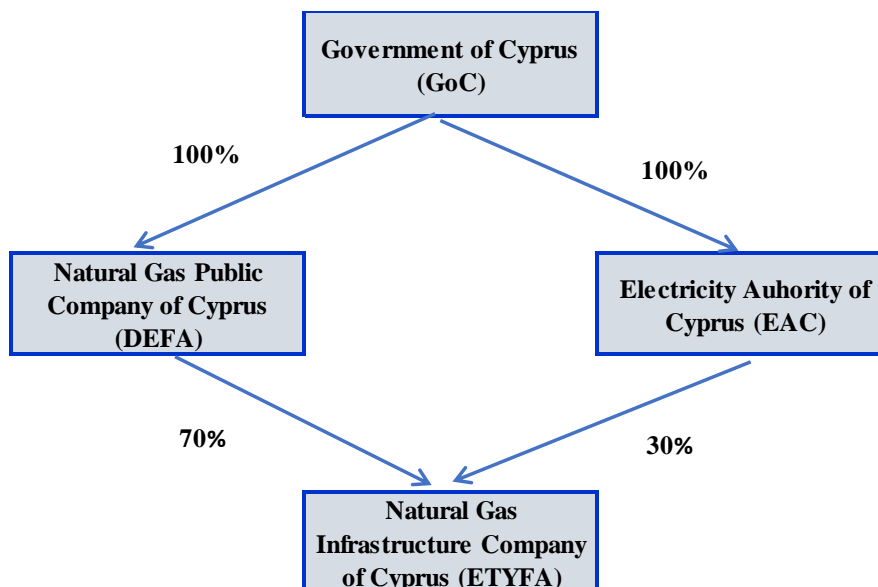
More detailed results of the economic assessment can be found in Annex 8.

ANNEXES

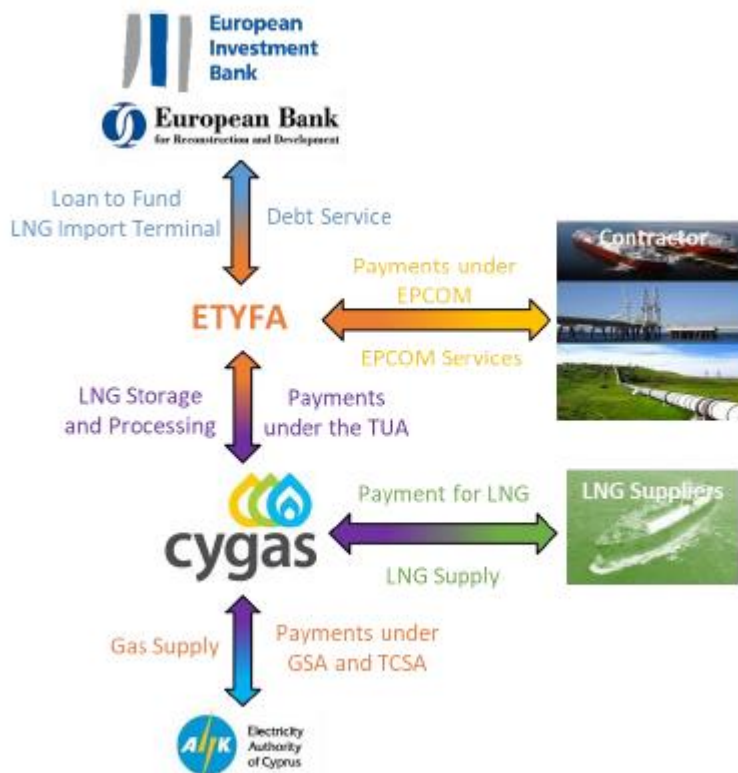
ANNEX 1	Shareholding and Commercial Structure
ANNEX 2	Project description
ANNEX 3	Market Overview
ANNEX 4	Regulatory Annex
ANNEX 5	EAC and DEFA financial highlights
ANNEX 6	Transition Impact Scoring Chart
ANNEX 7	Greenhouse gas emissions analysis
ANNEX 8	Cost Benefits Analysis
ANNEX 9	Project Implementation and Procurement Plan

ANNEX 1- Shareholding and Commercial Structure

Shareholding structure of the Borrower



Commercial structure of the Project



DEFA will enter into a **Terminal Use Agreement (TUA)** with ETYFA, pursuant to which ETYFA will provide storage and regasification services at the LNG import terminal in exchange for a fee payable by DEFA. [REDACTED]

In turn, DEFA will enter into the **Terminal Cost Sharing Cost Agreements (TCSA)** with companies wishing to procure natural gas, allowing DEFA to pass through the Terminal Facilities Charge to gas buyers. EAC will be the initial anchor buyer of the gas supplied through the project facilities [REDACTED].

In addition, DEFA will enter into **Gas Sales Agreements (GSAs)** with the gas buyers. [REDACTED]

ANNEX 2 – Project Description

The project involves the design, construction and operation of a LNG receiving facility in Vasilikos Bay in Cyprus. The major project components are:

- The acquisition an FSRU. FSRUs are vessels similar in design to a Floating Storage Unit but they also have on board facilities for regasifying LNG from its liquid storage facility or from a docked LNG carrier. The LNG will reach the FSRU by means of LNG carriers and will then be transferred into the floating unit and temporary stored in its cryogenic tanks. Afterwards, the LNG will be regasified directly on-board of the FSRU. After the regasification process, the natural gas is directed to a metering unit for measurement and to the jetty-borne pipeline for its transmission onshore.



[REDACTED]

- Construction of a jetty platform for permanent FSRU berthing, including mooring equipment, loading platform, offshore components, shore protection work etc. The jetty will be located 1.3 km west of the main breakwater of Limassol Port – Terminal 2 (Vasilikos)
- Construction of a jetty-borne gas pipeline and installation of the ship-to-shore gas loading arms and fire-protection system and the onshore gas pipeline. The overall length of the pipeline will c.2km. Once the pipeline has left the jetty it will be buried using normal trenching techniques for the remainder of the route up to the buffer storage facility and the Pressure Reduction and Metering Station.
- Construction of natural gas buffer storage solution which is an underground piping arrangement designed to provide the system with additional gas storage capacity. The facility will include for 125 tonnes of natural gas storage within both the gas pipeline and the buffer solution.
- Construction of a Pressure Reduction and Metering Station (PRMS) to condition the gas delivered to Vasilikos station to the required gas pressure and temperature conditions. This above-ground installation will be located close to the Vasilikos station delivery flange.

FSRUs are flexible by nature and the Project has been designed so as to allow flexibility in the use of the facilities: the FSRU will include an LNG bunker vessel connection and an LNG off-loading system so as to be able to use the infrastructure as a ship-to-ship bunkering facility. The marine infrastructure has also been designed so as allow a future expansion with additional berthing positions, which can be used to serve ships for the purpose of exporting natural gas. The natural gas pipeline will also be bidirectional. Finally, the FSRU will also have the ability to disconnect from its berth and travel under its own motive power as a regular LNG carrier if required.

ANNEX 3 – Market Overview

Cyprus energy sector overview.

The energy sector in Cyprus is undergoing fundamental transformations concerning its structure and organisation, its institutional framework and the diversification of its energy mix.

Until 2010, electricity in Cyprus was generated almost entirely from imported fossil fuels. Despite recent developments of renewable energy sources, oil and petroleum products continue to dominate the energy mix, representing 91.4 % of the gross energy generation in 2018 the highest share within the EU. Despite concrete steps having been taken towards market liberalisation following Cyprus' accession into the EU, EAC remains the sole supplier and distributor in the country and generates more than 90% of Cyprus electricity

Oil and oil products represent approximately 92% of Cyprus's total primary energy supply and 8% is sourced from renewable energy, including solar, wind and biofuels.

More than 50% of the energy consumption in Cyprus is attributed to transportation sector, c.20% to residential use, c.13% to services and c.12% to industry, while only c.2% is attributed to the agriculture-forestry sector.

The cost of energy is highly sensitive to international oil price fluctuations in Cyprus and is consistently among the highest in Europe, representing c.8% of its GDP.

While Cyprus does not have indigenous fossil energy resources, natural gas has recently been discovered off the southern coast of the island.

The Ministry of Energy, Commerce and Industry (**MECI**) is responsible for the design and implementation of government policy in the fields of energy, trade/ commerce, industry, competition and consumer protection. Among others, MECI has the overall responsibility for the rationale and sustainable use of indigenous energy sources (including hydrocarbons and renewables), the monitoring and coordination of the supply and availability of sufficient energy capacity for domestic needs and the promotion of renewable energy sources and energy efficiency.

Electricity Market

The current structure of the Cypriot electricity sector is defined by a vertically integrated monopoly. While the electricity supply has been gradually liberalised: 35% on 1st may 2004, 65% on 1st January 2009 and finally the whole market on 1st January 2014, EAC remains the sole supplier in the country and generates more than 90% of Cyprus electricity. The country is in a transitional phase towards a revision of its market model that will allow more effective liberalisation and competition in supply and generation.

EAC owns and operates all three conventional power stations Vasilikos (868MW), Moni (150MW) and Dhekelia (460MW) representing 83% of the installed capacity. Several of the existing units have the capability to run on natural gas.

The total electricity generation in 2018 was 5 GWh for a total electricity consumption of 4.5 GWh, Transmission losses between production and distribution represented c.4.6% of power injected to the grid.

Vasilikos power station, to which the proposed FSRU will be connected, is the largest in terms of capacity and the most up to date power station located on the south coast of the island; it consists of 3 x 130 MW steam turbines (of which 2 are designed to run on gas), 2 x 220 MW combined cycle technology units and 1 x 37.5 MW gas turbine, with a total capacity of 868 MW. It produced 63% of the Cyprus thermal power generation in 2018.

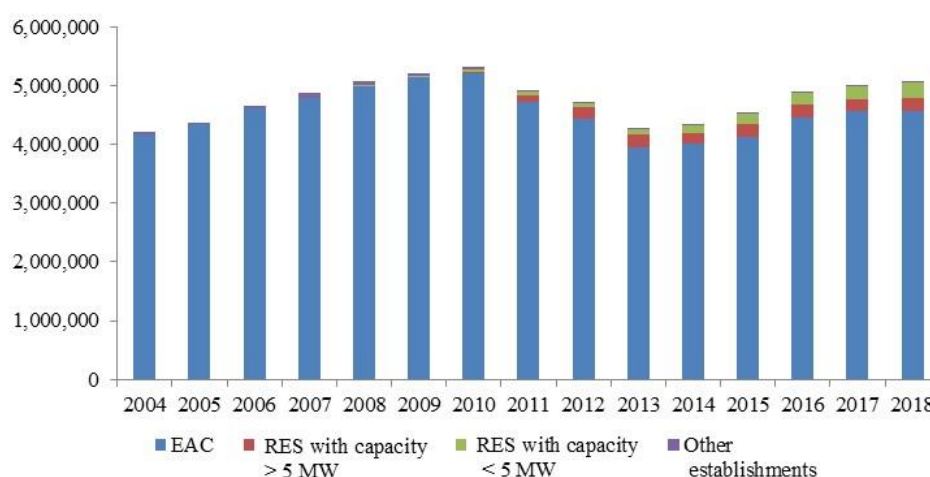
EAC Power Station Location



Source: Company

In addition to EAC's own generation capacity, there are six wind farms (157.5MW, 2020 target⁶ : 175MW) and numerous small solar generators (124MW, 2020 target: 288MW) and biomass/biogas (12.8 MW, 2020 target: 15MW). All existing and operational projects receive contracts-for-differences (CfDs). Approximately 10% of the renewable energy generation in Cyprus is for own consumption.

Gross Production of Electricity 2014-2018 (000's kWh)



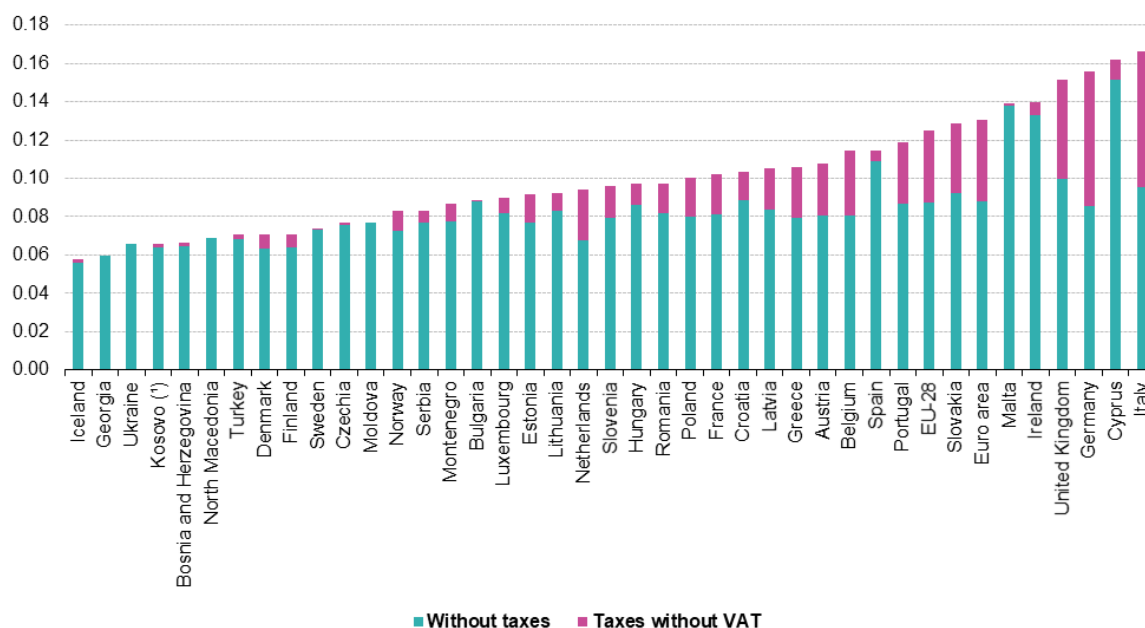
Source: Cyprus Statistical Service

Electricity prices

Because of the high reliance on imported oil products for power generation, Cyprus has one of the highest electricity prices in Europe, at approximately EUR 0.16 per kWh for non-households and EUR 0.22 kWh for households at end of 2019.

⁶ The binding 2020 national target of Cyprus for the share of renewable energy in the final energy consumption is 13% (i.e. electricity, heating and cooling and transport sectors combined). This represents a target set for renewable electricity at 16% which were translated into these targeted capacities.

Electricity prices for non-household consumers, first half 2019 (EUR per kWh)



Source: Eurostat

Vasilikos power station currently generates more than half of Cyprus electricity. The implementation of the Project is therefore expected to significantly reduce electricity generation costs in Cyprus thanks to:

- a lower price of gas compared to liquid fuels in general;
- lower maintenance costs at Vasilikos station due to longer intervals between regular maintenance when gas is used instead of conventional liquid fuels;
- reduced emissions due to the lower carbon content of gas compared to liquid fuels and due to a more efficient use of CCGTs leading to reduced payments associated with the emissions allowances;
- the EU grant for the infrastructure facilities is approximately 33% of the overall projected capital expenditures and will reduce the amount to be recovered through sale of gas;
- the increase in electricity generation competition being enabled by the Project.

EuroAsia Interconnector

There is a plan to connect Cyprus to the power grids of Greece and Israel via a 1,518km undersea cable. This is a [REDACTED]2,000 MW interconnector project listed as a European Project of Common Interest (PCI). The tenders for the construction were launched in 2019 but suffered delays [REDACTED]. There remains uncertainty as to the development of the EuroAsia Interconnector which has not yet secured full funding. To date, commissioning of the second phase of the interconnector (from Crete to Cyprus) is assumed to be 2025 and the third phase (connecting Cyprus to Isarel) in 2026.

EAC Unbundling and electricity market liberalisation.

The Cyprus Energy Regulatory Authority (**CERA**) was established in 2004 pursuant to the Law on Regulating the Electricity Market of 2003, which was enacted for the harmonisation of Cyprus law with the relevant EU Directives. CERA regulates the country's electricity and natural gas markets as the national independent regulatory authority. CERA's role includes:

- Oversee and regulate the market for the electricity and gas
- Ensure effective and fair competition
- Protect the interest of the consumers

- Ensure safety, quality, competence, continuity and reliability in the energy supply
- Encouraging the use of renewable energy

Since January 2014, the Cyprus electricity market has been fully liberalised to allow all consumers to choose their electricity supplier. However, despite the EU Directives having been transposed into domestic legislation, there is currently no other supplier in Cyprus apart from EAC. EAC remains the main generator with more than 90% market share in generation, 100% market share in supply and is the national TSO. This is partly due to Cyprus' relatively small electricity sector and isolated system.

CERA has begun EAC's operational unbundling in 2014 and functional unbundling of EAC is at official operation since December 2016. This has entailed the separation of EAC's operations into five functionally autonomous business units (production, transmission, distribution, supply, other activities). Units are expected to keep separate accounts to ensure that decisions taken by the Board of Directors or Management do not compromise each unit's independence. CERA's 2014 official decision emphasized the distinction between the owner of the transmission system and the operator. As a result of CERA's decision, TSO was established to work as a functionally and legally separate grid operator, independent from EAC.

Cyprus is now undertaking a revision of its market model and rules towards the development of an electricity market in compliance with the EU "Target Model". [REDACTED].

To cover the time that will inevitably pass until the full commercial operation of the new electricity market model (originally planned for July 2019 but postponed to 2020), the market currently operates under a transitional arrangement based on bilateral contracts between producers and suppliers for the supply of a standard quantity of electricity on a monthly basis.

Gas Market

Cyprus does not own, import and hence nor currently use gas for electricity generation. Developing the sector is however a priority for the country combining the development of indigenous production (following the recent large discoveries offshore Cyprus), import capacity and the internal gas market and network. The long-term goal is the establishment of a functioning, competitive gas market in Cyprus with a level playing field. A mature gas market will have decisive effects on the introduction of competition in the electricity sector.

The Project represents therefore the first phase of the wider initiative of the government of Cyprus to develop the internal gas market, network infrastructure, storage facilities and ancillary systems. The plan is first to develop a backbone network for the supply of natural gas to the main industrial areas of the island, either via pipelines or through a system of transport and storage; and, at a later stage, develop the use of natural gas by the transport sector, or by the heat intensive industries.

Future Gas Demand

In 2016 an Advisory Committee with members from DEFA, MECI, EAC (CERA participated as an external observer) was set up and was given the mandate to calculate the quantities of natural gas for electricity generation for the period 2019-2040. The simulation model was based on a cost optimal approach, which minimises generation cost by allowing dispatching of existing units and installation of new natural gas burning units and renewable energy sources.

Three scenarios were examined with each scenario using a different price of gas and CO₂ (high, base and low gas prices). The gas prices used in these scenarios therefore determine the degree of renewables penetration in the electricity generation system of Cyprus. The estimated annual quantities of natural gas demand for electricity generation for each scenario for the period 2019-2040 are shown in the graph below. [REDACTED].

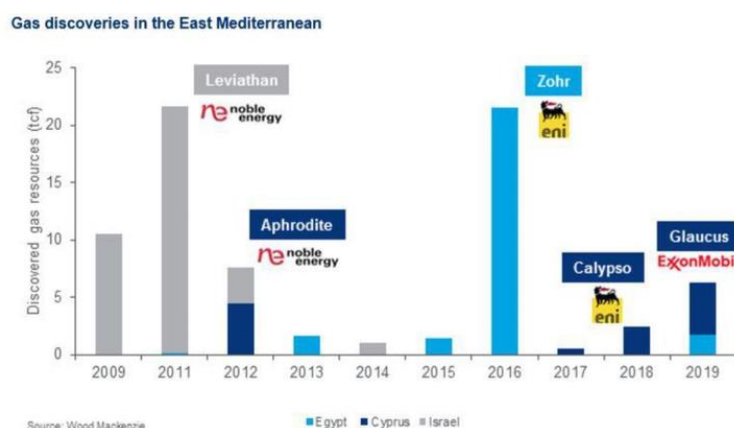
Once DEFA will have built the necessary gas transmission network, it is likely that over 90% of non-renewable power will be met with gas. The government's objective is to extend gas use beyond the power sector to the industrial, transportation and petrochemical sectors which would further increase the demand. [REDACTED].

Gas Discoveries, exploration and development

Since Cyprus defined its exclusive economic zone (EEZ) in 2004, it divided the south of the island into 13 offshore exploration Blocks. The government has gone through multiple rounds of licensing for offshore hydrocarbon blocks and gas exploration projects are ongoing.

Its first licensing round related to Block 12 which was awarded to the US energy company Noble Energy led-consortium in 2008. In 2011, Noble Energy alongside its partners Shell and Delek Drilling, announced a world-class discovery of natural gas in Block 12 – known as Aphrodite. Two years later, appraisal drillings confirmed natural gas reserves of 4.54 trillion cubic feet (tcf) equivalent to c. 130bcm. Aphrodite is the most advanced development in the country so far [REDACTED]. Aphrodite gas will be piped to the Egyptian Idku LNG facility for liquefaction and further export.

In February 2018, other gas reserves were discovered by Italian energy company ENI in Block 6 off Cyprus – known as Calypso, with estimated reserves of 3 to 5 tcf (i.e 85 to 142 bcm) . The US company ExxonMobil announced in February 2019 a discovery estimated at 5 to 8 tcf (i.e 142 to 227 bcm) in Glaucus-1, the second well of a two well drilling program in Block 10. Further analysis are performed to better determine the recoverable resources potential . [REDACTED].



Source: Wood Mackenzie

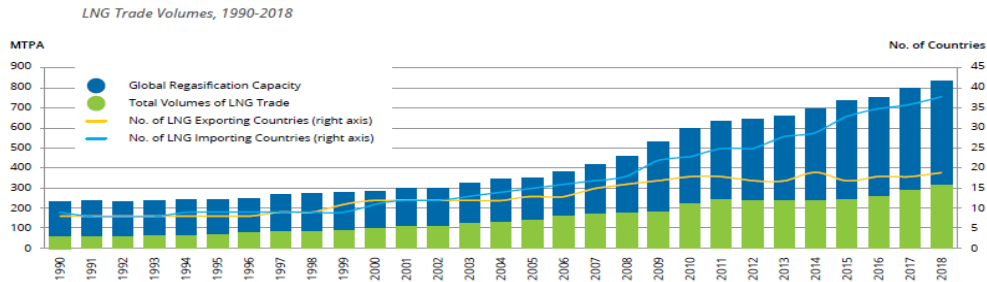
Natural Gas discoveries offshore Cyprus coincided with a series of similar large gas discoveries offshore of Israel and Egypt since 2010 and Cyprus is now part of a wider discussion on the best gas export options for Eastern Mediterranean gas. The need for inter-connected infrastructure have accelerated regional cooperation and inter-governmental discussions. This led to agreement in 2018 between Cyprus and Egypt to pipe Aphrodite gas to Egypt's liquefaction plants.

Cyprus is also in discussions with Greece, Italy and Israel about the potential of transporting gas from the eastern Mediterranean to Europe, via Greece and Italy ("EastMed Pipeline"). The project is designed to transport up to 16 billion cubic meters of gas per year from the off-shore gas reserves in the Leviathan Basin (Cyprus and Israel) as well as from the potential gas reserves in Cyprus, with the aim to diversify Europe's natural gas source of supply. [REDACTED]. Current proven gas reserves in Eastern Mediterranean are currently insufficient to back this 2,200 km project.

Global LNG Market

LNG is the fastest growing gas supply source worldwide, as structural changes in power markets and competition from substitutes require more flexible supplies of gas in terms of volume, destination and pricing. In particular, LNG solves a number of gas market uncertainties, such as declining domestic production, pipeline disruption, air pollution and renewable intermittency.

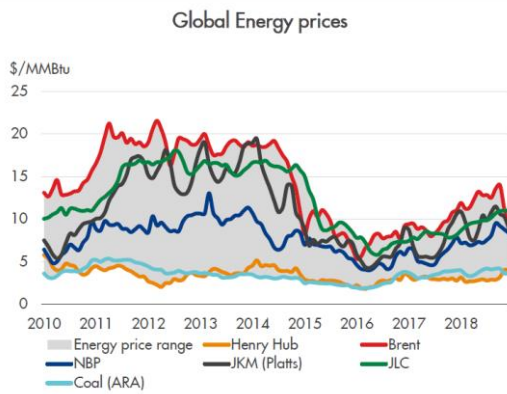
Globally-traded LNG volumes in 2019 increased by 13% from 2018, setting a new annual record of 354.7 Mt. Combined with 2017, this marks the strongest three-year growth period for international LNG demand since 2010-11. Total liquefaction capacity worldwide is 427 Mtpa compared to 920 Mtpa regasification capacity.



Source: IHS Markit, IEA, IGU

Global LNG market is experiencing significant oversupply which caused downward price pressure since 2015 and larger quantity of LNG being traded on a gas index basis (rather than oil index). The contracting regime for LNG trading is changing rapidly with contract lengths becoming shorter as buyers are securing greater flexibility. The continuing structural LNG oversupply, exacerbated by the Covid-19 crisis, is expected to maintain downward pressure to gas and LNG prices and sustained high liquidity.

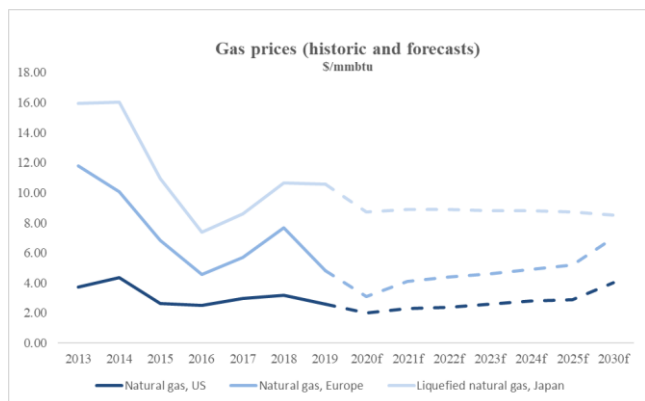
Most common spot reference price indices currently used are Henry Hub (main US gas hub), NBP/TTTF (main European gas hubs) and JKM (Platts LNG Japan/Korea Marker).



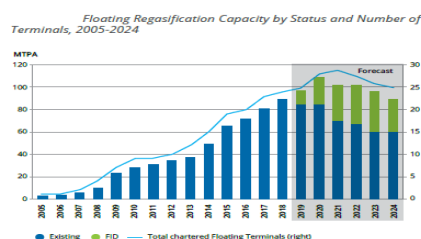
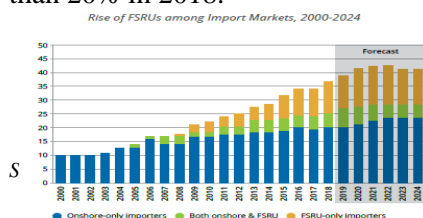
Source: Shell

FSRUs, which are more economical and flexible than onshore LNG regasification facilities, are adding to the fast growing LNG landscape. Given the increasing uncertainties surrounding the future of gas demand in a world where renewables and coal continue to provide stiff competition, development of the FSRU market has grown rapidly. FSRUs have a number of advantages over onshore import terminals: cheaper [REDACTED], twice as quick to delivery and flexible as the vessel can journey to other destination once it is not needed.

Source: World Bank (forecasts from April 2020)



There are currently 23 FSRU vessels in operation out of which 20 are operated as terminals with total active floating import capacity at 80.1 Mt per annum, 3 as LNG tankers and approximately 12 are under construction. The share of LNG deliveries to FSRU increased from below 5% in 2012 to more than 20% in 2018.



ANNEX 4 – Regulatory Annex

Gas Market Law and EU Directive

The law regulating the Cypriot natural gas market of 2018, which is presently in force⁷, adopts the important features of the EU's Third Energy Package that incorporates the legislative package for internal gas markets in the EU (Directive 2009/73/EC). The domestic natural gas law, among others, sets the rules for transportation, distribution, supply and storage of natural gas. In addition, it sets out the rules on the organisation and operation of the gas sector, market access, exploitation of the networks and the criteria and procedures for granting licences for the transport, distribution, supply and storage of natural gas. The Law also describes the tasks and responsibilities of CERA and fully defines the range of activities and its role.

As an emergent and isolated gas market, Article 49 of the EU Gas Directive (2009/73/EC) gives the right to Cyprus to derogate from specific articles of the Directive. In this context, Cyprus following relevant decision from the Council of Ministers on 05 June 2019 decided to:

- (a) proceed with the derogation from Article 9 of the Directive for the “Unbundling of transmission systems and transmission system operators” i.e. not separating the activities of the natural gas operators (distribution, storage, LNG etc.) from the activities of marketing and supply, with ownership unbundling.
- (b) proceed with an exemption from Article 36 of the Directive for major new gas infrastructure development i.e. exempting the Project from third party access.

This will allow the operation of the Project under a monopolistic regime (under the umbrella of state owned integrated gas company DEFA) for the first years of operation and aims at assisting Cyprus gas market in its transition in becoming functional and competitive. The criteria for such exemptions are as follows:

- the infrastructure must improve security of supply and boost competition in the gas market;
- the investment could not go ahead without the exemption due to the level of risk;
- the infrastructure must be owned by a legally separate firm from the system operator in whose system it will operate;
- users of the infrastructure must pay for access;
- the exemption does not harm the functioning of the EU's internal gas market or the transmission system to which the infrastructure is linked.

Natural gas market regulations are currently under development including a code for supply of gas defining the supplier-consumer relations and technical rules regulating connection and operation of all natural gas networks. The tariff methodology regulation has been issued by CERA in June 2019 (see below). Under the Gas Market Law, the CERA has to secure and establish the network codes, however it is the transmission system operator's obligation to prepare these and for the CERA to adopt them.

Role of the Regulator

The Cyprus Energy Regulatory Authority (CERA) was established in 2003 pursuant to the Law on Regulating the Electricity Market of 2003, which was enacted for the harmonisation of Cyprus law with the relevant EU directive on electricity. CERA was made responsible for regulating the natural gas market later in 2004 by virtue of the Natural Gas Market Law of 2004. CERA's roles include:

- Overseeing and regulate the market for the electricity and gas
- Ensuring effective and fair competition
- Protecting the interest of the consumers
- Ensuring safety, quality, competence, continuity and reliability.

⁷ The Regulation of the Gas Market Law was originally introduced in 2004 and amended by Laws 103(I)/2006, 199(I)/2006, 199(I)/2007, 219(I)/2012 and 148(I)/2018.

Role of DEFA

In November 2007 the Government of Cyprus established DEFA to facilitate the importation and distribution of natural gas to the Cyprus energy market. The council of Ministers of the Republic of Cyprus issued a decree dated 18/06/2008, which appoints DEFA as the sole importer and distributor of natural gas in Cyprus. Accordingly, and in line with the EU derogations, DEFA has the exclusive right to import and supply natural gas to consumers. More specifically, DEFA is responsible for the development of the gas market in Cyprus including (i) the purchase and import of natural gas, including LNG; (ii) the development and management of an LNG import terminal and gas transmission network; and (iii) the sale, distribution and supply of natural gas within the Cypriot market.

Before the start of commercial operations, DEFA will be established as a Public Law Entity (it is currently registered as a Limited Liability Company) and DEFA/ETYFA will need to secure licenses from CERA for:

- Ownership and Operation of Transmission System
- Ownership and Operation of Distribution System
- Ownership and Operation of LNG Facilities
- Ownership and Operation of LNG Storage
- LNG & natural gas supply.

Development of the Natural Gas Market

Once the Project will be operational, DEFA intends to make additional gas sources available to the wider power sector by constructing a gas transmission line to connect EAC's two other existing power stations and future independent power producers (IPPs). The Project is the first step of the establishment of an integrated storage, transmission and distribution system for natural gas in the country to extend its use beyond the power sector to the industrial, transportation and petrochemical sectors.

Natural Gas Pipeline Network

As part of efforts to secure an uninterrupted supply of natural gas, DEFA appointed an external advisor (Gas Natural Fenosa) in 2010 who completed a feasibility study in 2012 - which was subsequently revised in 2017- for the development of the transmission and distribution natural gas pipeline network. The feasibility study includes various studies in connection to gas demand, route selection, network sizing, as well as a preliminary EIA and Risk Assessment and Economic and Financial Analysis that serves as the basis for the development of the Cypriot natural gas network.

Phase A of the project considers the construction of a natural gas network comprised three pipelines that will supply the three power stations of EAC (Vasilikos, Dekeleia and Moni) as well as the three licensed Independent Power Producers (IPPs). This first network will serve as the backbone for the development of future network in the cities and industries and is estimated to have a total length of 80km. The initial cost estimate for Phase A is approximately EUR 70m and the project has already secured sponsorship of EUR 10m by the EU under the European Economic Recovery Plan.



Selected gas transmission route, *source : DEFA*

CYnergy Action

CYnergy is a project co-financed by the EU's Connecting Europe Facility launched in 2017. It is a collaboration of energy, transport and finance experts as well as public and governmental institutions of Cyprus and Greece. This initiative provides a holistic approach towards the establishment of a gas supply system on the island of Cyprus, as well as an approach towards the optimization of the upstream and downstream natural gas supply chain. The proposed action is linked to the Project of Common Interest (PCI) 7.3.2 promoting the development of a LNG Storage Facility in Cyprus and to the TEN-T Orient/ East-Med Core Network Corridor and the complete Core and Comprehensive Port and Road Network of Cyprus.

More specifically, it aims to achieve the optimisation of the downstream and upstream gas facilities through five proposed approaches:

- exploration of the options for the main natural gas supply, storage, trade and distribution for Cyprus;
- exploration of the possible complementary patterns in supply, storage, trade and distribution of gas;
- possible development of a secondary LNG intramed market utilising small-scale LNG bunkering vessels;
- investigation of the possible development of a complementary CNG waterborne supply chain;
- development of dedicated implementation plans per sector explored.

Open Season & Market Test Process

DEFA has submitted proposals for open season general rules, which are currently under review by the regulator. These rules will determine the gas demand allocation per end consumer and year as well as the spatial requirements that are necessary for future decisions regarding the development of additional facilities, incl. the gas pipeline network.

More specifically, open season general rules will regulate (a) the allocation of costs / gas to the new entities using the LNG termination; (b) the reallocation of costs / gas if a user(s) wishes to increase, decrease or eliminate its share of the gas supplied from the LNG terminal; (c) the reallocation of costs / gas to prevent market abuse by a user(s). It is expected that the new customers will be signed up using a two-stage process:

- a non-binding express of interest (EoI); and
- final gas allocation commitments.

Tariff Methodology

Background

CERA, following the decision of Council of Ministers on 18 May 2017 according to which the Minister of MECI was authorized to instruct DEFA to tender for long-term supply of LNG for electricity generation purposes and to find a strategic investor for the construction and the subsequent operation of the Vasilikos FSRU, decided to lay down the ***basic principles of the pricing methodology for LNG facilities*** to be used in the setting of the regulated tariffs for the use of LNG facilities. This methodology was used for the LNG regasification CEF Energy proposal.

Subsequently, in January 2019, CERA with the support of external advisors and EU technical assistance proceeded to the development of the first draft on tariff methodology regulation for natural gas that set out ***the pricing methodology for each core regulated activity in the natural gas market***, namely the transport, distribution, LNG facilities, storage as well as the supply of natural gas tariffs. This was later published to the Official Government Gazette in April 2019 and came into public consultation for industry experts and interested parties for a period of thirty days.

Ultimately, following the decision of Council of Ministers on 05 June 2019 and the derogations approved in light of the country's natural gas emergent market status, according to which (a) the supply of natural gas will be monopolistic and (b) DEFA will be the vertically integrated entity to own and manage all natural gas infrastructure in Cyprus, i.e. transmission and distributions networks – ***CERA issued the final “Statement on Regulatory Practice and Tariff Methodology for Natural Gas” on 14 June 2019.***

Basic Tariff Principles

The basic principles, on which the methodology is based for the calculation of regulated tariffs during the emergent market period, are the following:

- a common approach shall be followed with the same basic principles for the calculation of the recoverable revenue to apply for all gas infrastructures (LNG and storage facilities, transmission and distribution networks);
- a period of calculations and review adjustments of the costs of use to be enacted, in order to promote stability and predictability of monetary cash flows;
- the value of asset acquisition methodology to be used for the calculation of Regulated Asset Value Base (RAVB), given the initial development of natural gas infrastructure, whilst WACC to be used as a rate of return.
- the principal of financial neutrality of operators and the monopoly supplier to be applied, to allow for cost recovery plus a reasonably return.
- where is financially efficient, CERA would allow for external cost parameters integration to the recoverable revenue of operators and the supplier, to ensure the competitiveness of gas against alternative fuels;
- subsidies cannot bring profits to its beneficiaries – therefore the rate of return of the said investments is nil, while depreciation relating to the part of subsidies cannot be included in the recoverable revenue;
- accounting and operating decoupling rules of the monopoly supplier to be fully implemented, so that both the costs and revenues of the activities as operator are recorded separately from those arising from activities as supplier;
- as the emergent status lasts, the monopoly supplier will be the only who will incur the cost of for the use of transmission, distribution, storage of gas and LNG, to be accounted for on an annual basis and included in the recoverable supplier costs, through supply tariffs, upon CERA approval.

Operator Revenues Allowed

CERA shall approve the operator revenues allowed, in accordance with the periodic regulatory review, for each of the activities of the ownership and management of the transmission, distribution, storage system, LNG facilities and/ or a combination of the above. The regulatory control period for every regulated operator activity shall be as follow:

Parameter description	Value
Duration of regulatory control period for the Transmission System	5 years
Duration of regulatory control period for the Distribution System	5 years
Duration of regulatory control period for the LNG facility	10 years
Duration of regulatory control period for the storage facility	5 years

The revenues allowed for each regulated activity shall include a capital and operating component as follows:

- **The capital component** of allowed revenues which shall include the allowed return on the average RAVB and depreciation. The allowed rate of return of RAVB shall correspond to the WACC that will be determined within the framework of the periodic regulatory review by the regulator, on the basis of the actual data and it shall be a nominative return rate.
- **The operation component** of revenues allowed, which include expenses carried out by the regulated entity to carry out its daily business activities, including (a) the cost of

maintenance and management, advisory, legal services, insurance (b) gas consumed while the system operates, including losses and self-consumption, (c) spare parts and natural gas odorization; and (d) other opex (lease of buildings, self-supplied fixed assets, expenses for the commitment of gas system capacity etc.) which are directly spent and not capitalized according to the accounting rules.

Prior to the commencement of the regulatory period, the operators shall submit to CERA all necessary data for the determination of revenues allowed for each year of the regulatory control period. Following the initiation of the regulatory control period, CERA may review the revenues allowed for a year of the current control period only in the event of a deviation of revenues allowed which is greater than 10% for the year concerned. Any discrepancy shall be taken into account in the calculation of the revenue allowed for the following regulatory control period, referred in each year of period in a manner to be determined by a decision of CERA.

Revenues allowed and natural gas supply tariff methodology

The allowed supplier revenues will be regulated by CERA in a 5-year regulatory control period. The revenues allowed linked to the supply activity aims at the full recovery of the natural gas supply costs from final consumers, during the regulatory period, including the cost for the use of infrastructure and any deviations in the recovery of the annual supply cost (recoverable cost difference).

The annual supply cost will be the sum of (a) the annual cost paid by the supplier for the use of the gas infrastructure, (b) the cost of supply of natural gas from the respective supplier contracts, (c) the supplier's operating expenditures increased by the allowed cost margin in the commercial and accounting management services provided to clients (set at 2.00%) as well as (d) any recoverable cost difference calculated on annual basis and approved by CERA.

Final consumers will be classified in categories depending on their final use of natural gas and the distribution of the annual supply cost in supply tariffs per final consumer category will be based on the following principals:

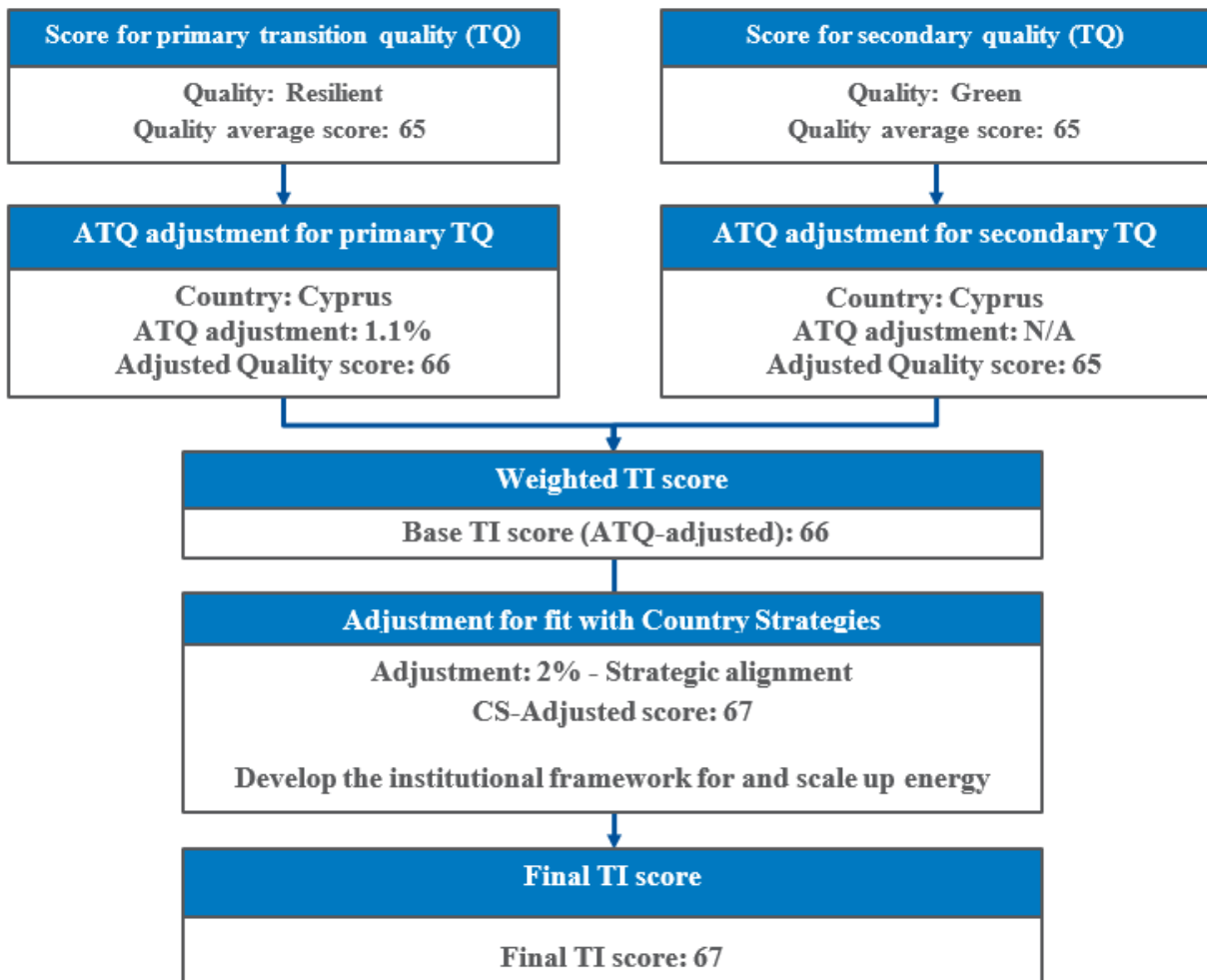
- Recovery of the cost from the use of infrastructure
- Equal treatment of consumers within the same category
- Competitiveness of natural gas against alternative fuels, in line with the principles of healthy competition.
- Consumer and environmental protection.

Annual supply cost is intended to be recovered through the regulated supply tariffs. Prior to the year in which supply tariffs will apply the supplier shall submit to CERA the annual supply cost as well as the intended supply tariff for each consumer category. The regulator will then decide whether to approve or propose amendments to the proposal as appropriate.

ANNEX 5 - EAC and DEFA Financial Highlights

[REDACTED]

ANNEX 6 – Transition Impact scoring chart



ANNEX 7 – Greenhouse gas emissions analysis

The Bank hired a consultant (RINA Consulting) to undertake an assessment of the GHG impact of the Project by looking at its impact in Cyprus on the various energy sources affected by the new gas supplies into the country, as well as the related supply chains. Similarly to the same analysis undertaken in the past for gas infrastructure projects (e.g. Southern Gas Corridor), the assessment is based on the following main assumptions:

Scenario analysis: The assessment has been carried out by comparing the broad market outcomes, energy trends and emissions in a suitable reference scenario (i.e. the evolution over time of the energy balances in absence of the gas supply from the Project) with the project scenario (i.e. same evolution but with the new gas supplies from the Project).

Energy demand evolution: The analysis focuses on the period 2022-2040. Different referenced sources⁸ have been used to set the anticipated evolution of the total energy demand in light of the probable impact of sustainable development and Paris Agreement existing and planned policies. These same sources provide a clear overview of the future demand for non-renewable energy sources and thus the possible scope for fuel replacement with LNG.

Sectors: The assessment primarily focused on the power sector and the Vasilikos area in particular as the gas will land in Vasilikos and the Project will be directly connected via pipeline to the existing Vasilikos power plant. Other gas users, the industrial sector and residential/commercial buildings, have also been taken into account in relation to the possible technical viability and cost competitiveness of fuel switch but also the residual share of demand not covered by renewable energy sources.

Origin of LNG: as per Annex 3, the LNG market is in continuous evolution and entails intercontinental flows and impacts. For simplicity, the assessment has considered three possible sources of LNG: 1) the global international market, 2) Algeria and 3) Egypt. The latter remains the most realistic option as Egypt's existing LNG infrastructure is expected to be physically linked to the offshore gas developments of Cyprus (Aphrodite) and Egypt is developing as a regional gas hub in the Eastern Mediterranean.

Extent of impacts: GHG emission have been calculated as the sum of demand-side GHG variations and supply-side GHG variations. The demand-side variations were determined by looking at the energy supply changes occurring at the points of final use of the natural gas. The supply-side variations depend on the above energy supply changes and represent the associated GHG emission variations along the supply chains of the fuels being replaced in comparison with the emissions of the LNG supply chain. In this regard, while data from the IPCC and other technical literature often provides a broad range of variations for the GHG emissions of different supply chains (e.g. long-distance supply by pipeline; LNG gasification and regasification terminals, geographic origin of the gas, etc.), the study always used realistically conservative assumptions.

Limitations: The scenarios analysis did not rely on new energy and market models developed by the consultant within the assignment, but rather relied on the results of existing models developed by the Government of Cyprus to develop its National Energy and Climate Plan as well as other reputable institutions (in particular the International Energy Agency, the EUCO27 study published by the EU Commission). Scope 1 emissions were derived from the currently available technical specification of the Project. Scope 2 and 3 categories of GHG emissions, as defined by the UNFCCC, were calculated and reported but second-order effects (such as reactions to the emission savings in the EU ETS) were not included in the analysis.

⁸ Among others: Cyprus Draft Integrated National Energy and Climate Plan for the period 2021-2030 formally published in January 2019; IEA Energy Balances for historical years for Cyprus; EU PRIMES EUCO27 scenario (E3Mlab & IIASA) for future energy trends in Cyprus.

Main results

The total supplies of LNG into Cyprus have been modelled as follows:

Million m ³ per year	2022	2030	2040
Power sector (of which Vasilikos TPP)	843 843	860 860	209 0
Other sectors	0	206	345
Total	843	1,066	554

The total GHG emission reductions are estimated to be around 0.6 MtCO_{2e} in 2022, when the Project start operations, slightly increase in 2030 to 0.8 MtCO_{2e} and then gradually decline to under 0.4 MtCO_{2e}.

	GHG emissions savings (tCO _{2e} per year)				Cumulative GHG emissions savings (MtCO _{2e} per year)
LNG source	2022	2030	2040	avrg	2022-2040
Global markets	347,000	453,000	210,000	337,000	6.4
Algeria	666,000	855,000	420,000	647,000	12.3
Egypt / Aphrodite	825,000	1,056,000	524,000	802,000	15.2
<i>Average</i>	<i>613,000</i>	<i>788,000</i>	<i>385,000</i>	<i>595,000</i>	<i>11.3</i>

The demand-side impacts are not influenced by the source of LNG and only depend on the national policies and market evolution which affect the demand for gas in the different sectors. Based on the National Energy and Climate Plan they are:

	Demand-side GHG emissions savings (tCO _{2e} per year)			
	2022	2030	2040	Avrg
Demand side (of which power sector)	780,000 780,000	1,001,000 824,331	498,000 200,261	760,000 601,440

The supply-chain impacts instead primarily result from the comparison of CO₂ and methane emissions along the LNG supply chain from the various geographical sources of the gas and the oil products currently being used in the country:

	Supply-side GHG emissions savings (tCO _{2e} per year)			
LNG source	2022	2030	2040	avrg
Global markets	- 433,000	- 548,000	- 288,000	- 423,000
Algeria	- 114,000	- 146,000	- 79,000	- 113,000
Egypt / Aphrodite	45,000	55,000	26,000	42,000
<i>Average</i>	<i>- 167,000</i>	<i>- 213,000</i>	<i>- 114,000</i>	<i>- 165,000</i>

Notably, while the supply chain emissions are generally higher for LNG than the oil it replaces, this is not the case if the gas comes from the nearest gasification plants in Egypt.

ANNEX 8 – Economic Assessment

Summary

The economic assessment concludes that the Project –a Floating, Storage and Regasification Unit and its associated infrastructure – would offer a positive benefit to society if implemented. It has the potential to significantly reduce electricity generation costs, entail environmental benefits in terms of GHGs and local air pollution and increase the security of electricity supply of Cyprus. This conclusion is robust to plausible sensitivity checks.

The assessment compared these outcomes with those that could be obtained through other energy infrastructure options available to Cyprus. Based on our assessment, the highest benefits to society are in a scenario in which the Project is combined with an interconnector alongside an enhanced roll out of renewable generation. In the scenario where these infrastructure options are deployed together, the Project is utilised less but overall generation costs are lower, emissions reductions are higher and there is enhanced security of supply.

Given the short lead time of the Project, reduced generation costs and emissions savings can be delivered from 2022, while the interconnector is assumed to come online not earlier than 2025. The assessment shows that even if the Project was retired when the interconnector comes online, the economic value of its benefits would warrant investment. In practice, the implementation of the Project offers insurance against a delay in the interconnector.

The risk of the locking-in of fossil fuel infrastructure in the medium and long term are considered low. Comfort is taken for three reasons: first, the Cypriot electricity system is covered by the EU-Emissions Trading System (ETS), which is the key EU instrument to cost-effectively deliver an electricity system consistent with EU climate change ambition. Second, it is likely that some gas generation will be required even in 2040 to support the cost-effective implementation of renewables. Third, the Project could support the use of low-carbon gas in the form of synthetic methane should it become economically viable in the long term, although this is not expected to be the case in coming decades.

Background

The Energy Sector Strategy 2019-2023, approved by the Board of Directors on 12 December 2018, stipulates that from 1 January 2019, an economic assessment will be conducted for prospective investments whose annual direct greenhouse gas (GHG) emissions are deemed to be significant. The assessment applies where investments GHG emissions exceed 100,000 tonnes of carbon dioxide equivalent (CO₂e) in absolute terms and/or 25,000 tonnes of CO₂e relative to a baseline. A publicly available methodology for the economic assessment of EBRD projects with high GHG emissions guides this process. In line with current EBRD and multilateral development bank (MDB) practice, the thresholds above are based on a project's "Scope 1" (direct) and "Scope 2" (indirect or electricity) GHG emissions. However, as the EBRD is keen to consider the upstream or downstream impact of its projects, the methodology foresees that Scope 3 GHG emissions may be taken into consideration in some infrastructure investments, where these are significant. This is the case of this Project, where GHG mostly relate to the use of gas that the investment facilitates. Thus management has decided to undertake the assessment on this basis.

The purpose of the economic assessment is to provide an additional piece of information that supports the final decision around the Project. In particular, it focuses on its merits from a social perspective, including environmental externalities.

Outline of approach to economic assessment

Cyprus is a small energy system, isolated in terms of energy infrastructure. The electricity sector in Cyprus is characterised by its high cost, reliance on oil imports from Greece and Israel (which make up around 90% of current electricity generation) and high GHG and local air emissions.

Outside electricity, energy demand in Cyprus (for industry, buildings and transport) is also heavily reliant on imported oil. The need for a change in the energy system is widely acknowledged, partly driven by EU policy around energy, GHGs and air pollutants.

The objective of the Project is to build a Floating, Storage and Regasification Unit and its associated infrastructure. It is envisaged that the gas provided by the Project will be mainly used for power generation at the Vasilikos power station, which is “dual fuel” and therefore can switch between oil and gas as a generating source. It could also facilitate gas use elsewhere in Cyprus, subject to investment in supporting infrastructure (e.g. to the Moni power plant). The Project is “non-marginal” in that it is large enough to transform the electricity sector of the island and therefore the assessment focuses on the role of the Project in the context of different evolutions of the whole electricity sector in the period up to 2040. The assessment should not be read as a proposal for an energy sector strategy for Cyprus.⁹

There are a number of future electricity infrastructure options available to Cyprus. This includes some combination of gas infrastructure (which the Project facilitates), an electricity interconnector, and the build out of renewables. The starting point for the EBRD assessment was the Cyprus draft National Energy and Climate Plan ([NECP](#)) published in January 2019 which represents the current stated position of the country in terms of future ambition of its energy sector to 2040. Another key source is the [energy system modelling](#) developed by the EU, showing a 2021-2030 scenario in each member state to achieve EU energy policy objectives of at least 32% renewable energy in the EU energy mix and an improvement in energy efficiency of 32.5%. (known as the EUCO3232.5 scenario).¹⁰

Against this context, five scenarios have been assessed (depicted below):

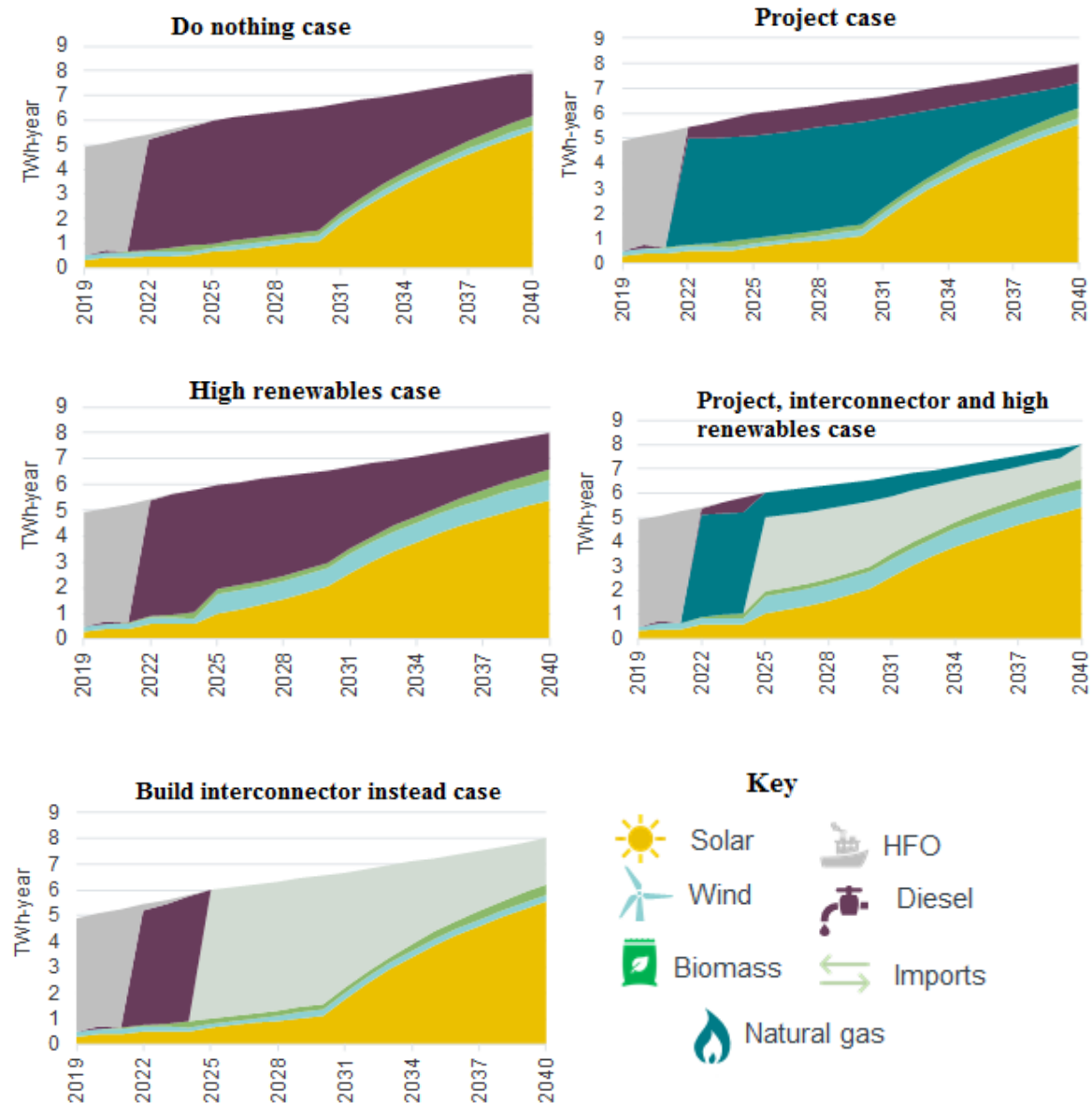
- “*Do nothing case*” – the Project is not built and Cyprus remains isolated in energy infrastructure terms, with continued reliance on oil fired power and an increase in renewables up to 77% of the generation mix in 2040, in line with the NECP.
- “*Project case*” – the Project is built and operational in 2022, resulting in gas use in the relevant power plants; renewables increase up to 77% of the generation mix in 2040, in line with the NECP.
- “*High renewables case*” – the Project is not built and Cyprus remains isolated in energy infrastructure terms but aggressive implementation of renewables takes place (from 2021, the EUCO32 renewables levels for Cyprus are brought forward by 5 years and by 2040 renewables reach 82% of the generation mix.)
- “*Build interconnector instead case*” – this scenario assumes the construction of an interconnector between Greece and Cyprus becoming operational in 2025, combined with an increase in renewables to 2040 in line with the NECP (thus 77% of the mix). The Project is not built.¹¹
- “*Project, interconnector and high renewables case*” – the Project is built and operational in 2022, the interconnector is built and operational in 2025, aggressive implementation of renewables takes place (82% of the mix in 2040).

⁹ The assessment considers the use of gas only in the electricity sector and the Vasilikos area. There is potential gas could be used in the existing Moni dual-fuel power station (12km from Vasilikos) and/or a new licenced gas power plant in Moni. Doing so would require building a pipeline or designing an inland LNG transport of gas from the Project or Vasilikos to Moni. Although it is technically possible and might be economically feasible these were not considered in this assessment as were not explicitly modelled in the NECP. There is also potential to use gas in energy intensive industry and in transport (particularly in heavy trucks) but these were not considered in this assessment. Lastly, there is potential too to use gas for heating and cooling however this would require investment in a new distribution network which is unlikely to be a cost-effective solution for Cyprus where heating demand is low and where penetration of solar water heating is already installed in around 80% of homes.

¹⁰ Environmental and financial data for the Project have been taken from the Environmental and Social Due Diligence (ESDD), Technical Due Diligence, Financial Due Diligence and an assessment of the Projects GHG emissions. Other core input assumptions include technology costs (Frontier Economics, NECP and ENTSO-E TYNDP), fuel costs (NECP and the International Energy Agency) and efficiencies of existing power plants (Electricity Authority of Cyprus).

¹¹ We have considered the Greece to Cyprus portion of the EuroAsia interconnector in our main scenarios and allocated 50% of the cost to Cyprus for the construction. There are a variety of sources of interconnection as part of the EuroAsia and EuroAfrica interconnector (e.g. Egypt or Israel) but for simplicity we have focused on this portion only.

Generation mix under different scenarios (2019-2040)



Note: there are small amounts of light fuel oil, pumped hydro and lion batteries but these are relatively low and cannot be observed.

The assessment compares the costs and benefits of the different scenarios compared to the “do nothing case.”¹² Other relevant factors are also considered for each scenario: potential for lock-in to high-carbon infrastructure, stranded asset risk and the overall technical performance of the grid (measured in terms of reliability, flexibility and security of supply).¹³ Furthermore, we considered the role of the Project in an electricity system which is likely to meet the longer term EU climate ambitions in 2030 and beyond.

¹² The assessment is undertaken from a social perspective, which has several features. These include the use of a social discount rate applied to all economic values (6%; rather than a “private” discount rate that is normally equated to cost of capital) and the use of input values that reflect market prices in the absence of distortions (for example, estimated gas prices based on values in traded markets).

¹³ The assessment has built a simplified model of the entire Cypriot electricity sector by assessing overall electricity capacity and subsequently final generation. We have adjusted each scenario to ensure the overall reliability and flexibility of the grid is equal to the “do nothing case.” Security of supply has been assessed outside the model. We have held electricity demand constant across all scenarios.

The main environmental externalities incorporated in the assessment are:

- GHG emissions. To ensure the approach is comprehensive, the assessment takes into account all of the GHG emissions associated with each scenario. This includes those upstream, e.g. extraction and transport of gas from the nearby Aphrodite gas field and electricity mix in Greece for the scenarios with an interconnector. While GHG emissions in the electricity sector are covered by the EU Emissions Trading Scheme (EU ETS), for the purposes of this assessment “shadow” carbon prices recommended by the High Level Commission on Carbon Prices have been applied to all GHG emissions.¹⁴
- Local air pollutants: sulphur dioxide (SO₂), nitrogen oxides (NO_x) and large particulates (PM₁₀). The pollutants have also been estimated for imported electricity. These emissions have been valued based on a 2011 European Environmental Agency study.¹⁵

A sensitivity analysis has been undertaken on the “critical” variables to test robustness of results.

Results

All of the counterfactuals considered deliver a net economic benefit relative to the “do nothing case.” This is explained by two factors: (1) generation savings linked from switching away from oil-fired power plants (which in 2030 under the base case would have a marginal cost of around EUR 155 per MWh); and (2) avoided emissions from both GHGs and local air pollutants.

The economic assessment shows that the “Project case” would deliver an overall net benefit when compared to a “do nothing case” - generating a net present value (NPV) of EUR 2.3bn in real terms. Significant savings would come from avoided GHG emissions (valued at EUR 0.3bn), avoided local air pollutants (EUR 0.6bn) and avoided generation costs (EUR 1.9bn), more than enough to offset the incremental costs to build and operate the Project (EUR 0.5bn). It is important to note local air pollution benefits of the Project are more significant than the GHG benefits.

The largest net benefit of the options assessed is seen in the “Project, interconnector and high renewables case” with an NPV of EUR 3.3bn. This case results in the removal of diesel generation from 2025 onwards (in the Project case, diesel is still used in the Moni power plant), and the lower overall generation costs from the interconnector. In this scenario, the use of gas in the generation mix is significant between 2022 and 2025; once the interconnector is operational, the Project operates at lower load factors. This is because, on average, the marginal cost is lower for electricity provided by the interconnector (although in some hours of the year gas fired generation would be cheaper and therefore would be used instead of electricity from the interconnector).

Furthermore, the assessment shows that building out renewables only (high renewables case) delivers a lower economic benefit (EUR 1.1bn) than the Project case under central assumptions. In this scenario, as renewables are being installed, oil and diesel are still used in the generation mix even in 2040. In addition we note that while a renewables share of generation of above 82% may be feasible, it would still require significant investments in grid infrastructure and other operational measures which have not been valued in this assessment and which would likely reduce the economic benefit.

The option of building an interconnector instead of the Project yields a slightly higher net benefit of EUR 2.6bn under central assumptions. This is driven by higher economic savings due to avoided generation costs, partly because overall electricity provided by the

¹⁴ The High Level Commission on Carbon Prices have a range of USD 40-80 (~EUR 37-74) per metric ton of CO₂e in 2020 rising to USD 50-100 (~EUR 46-92) per metric ton of CO₂e by 2030. Beyond 2030 the prices will be increased by 2.25% per year. The lower end of the range has been applied in the scenarios. All values are in real terms and in constant 2017 prices.

¹⁵ The EEA study attributes costs in constant 2017 prices for sulphur dioxide (SO₂) of 8,313 EUR/tonne; nitrogen oxides (NO_x) of 8,010 EUR/tonne; fine particulates (PM_{2.5}) 28,732 of EUR/tonne; and large particulates (PM₁₀) of 18,008 EUR/tonne.

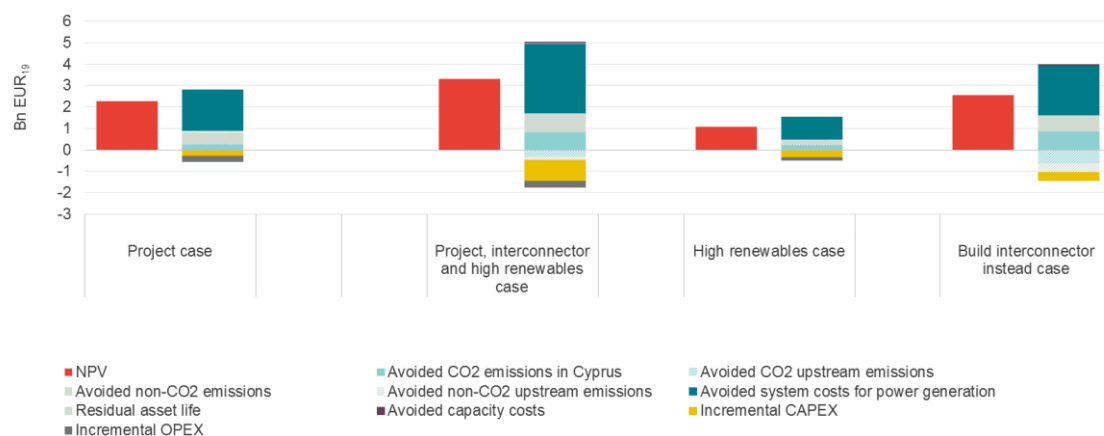
interconnector is cheaper than provision by gas, These lower generation costs more than offset the slightly higher emissions relative to the project case (both GHGs and local air pollution). However, investing in the interconnector *instead* of the FSRU delivers lower economic benefits than if they are built together. This is because shorter construction and planning lead times mean that electricity cost reductions and emissions savings can be delivered quicker with the FSRU from 2022 than with an electricity interconnector, which has been assumed to come online in 2025. Any delay in the construction of the interconnector would increase the attractiveness of the proposed Project, i.e. a two year delay results in an economic benefit equal to that of the Project case. Importantly the assessment does not reflect security of energy supply considerations – reliance on a single electricity interconnector with a still uncertain construction timeline exposes Cyprus to significant energy security risks in both the short and medium term, which accordingly challenges the viability of this scenario.

The conclusions above are robust to key sensitivities. These include the following insights:

- Applying carbon prices at the high end of the EBRD range amplify the benefits of different scenarios. Conversely, lower carbon prices also do not impact each scenarios NPV or relative ranking.
- The gas price series assumed (“medium” price scenario from the NECP) would have to be double for the Project to reduce the economic return to zero. This sits outside a plausible range.
- Results are not sensitive to assumptions around the availability of the interconnector to meet peak electricity demand.

Net economic benefit in billion Euros at constant 2019 values

Project case ¹⁶	Project, interconnector and high renewables case	High renewables case	Build interconnector instead case
2.3	3.3	1.1	2.6



Risk of lock-in to fossil fuel infrastructure from the Project

The Project is unlikely to be “stranded” in economic terms, even if the interconnector and high renewables are implemented according to the scenarios. This is because the economic payback of the Project under central assumptions is two years due to the avoided generation costs and emissions savings relative to the costs of the Project – and because part of the FSRU could be sold at a depreciated value at this point.

¹⁶ In the “Project case”, which is based on the envisaged generation mix under the NECP, diesel generation continues to play a role until 2040. We have analysed the economic benefit of gas from the FSRU replacing all diesel generation on the island. In this case, the net economic benefit is increased from EUR 2.3 to around EUR 3bn.

A more pertinent risk stems from the potential “lock-in” of fossil fuel infrastructure over the long term – and that investment in the Project will somehow inhibit achievement of the long run decarbonisation of the Cypriot electricity sector. To meet the EUs longer term climate ambition of net zero GHG emissions across all sectors by 2050 will mean that the utilisation of the Project must fall over time. This is because a significant share of unabated gas generation will not form part of any generation mix of consistent with the EU ambition.

The risks of lock-in are considered low. This is for three reasons: first, an EU-ETS designed to support the achievement of carbon neutrality in Europe by 2050 should ensure the overall level of GHG emissions at the level of the EU, of which Cyprus is a part, will remain within required limits. As a practical consequence in the medium term it is likely to be cheaper to invest in additional renewables and related infrastructure, rather than to continue to use existing gas infrastructure.¹⁷ Second, it is likely that some gas generation will be required even in 2040 to support the cost-effective implementation of renewables. Third, the Project offers the option to be used for low carbon gas. The existing design of the Project could not support hydrogen but could be used to support synthetic methane in the future, though our preliminary assessment is that this is likely to remain more costly than importing gas even in 2050.

Relevant factors not captured in the assessment

There are crucial elements of the Project’s Transition Impact that could not be quantified due to methodological complexities. These relate to security of supply (around 90% of current electricity generation is from imported oil) and policy dialogue to support market competition. This is a limitation of the economic assessment.

The scenarios with the Project improve security of supply relative to the “do nothing case”. At present, most of the imported oil products are sourced from Greece and Israel and due to relatively small import volumes, Cyprus faces barriers in changing to other source countries. In contrast, LNG can be imported from a wide range of countries.

The scenarios with “high renewables” and “build interconnector instead” offer lower security of supply benefits. In the renewables case, while more renewables on the system reduce the need for oil imports, in the near term there is still reliance on Greece and Israel for oil. In the case of the interconnector, there is a risk that supply from the interconnector could be curtailed, so there is a continued need for reserve back-up generation from oil.

¹⁷ This is based on a simple assessment of the levelised cost of different technologies using the model produced. As noted, as higher levels of renewables enter the system further investment to ensure grid performance may be needed and these have not been assessed in detail here. However, this conclusion broadly concurs with leading assessments of the cost of electricity supply options (e.g. [IRENA](#)).

ANNEX 9 – Project Implementation

Procurement classification – *Public*

[REDACTED]. The Client has earlier experience in applying open international tendering procedures. ETYFA, with the support of DEFA personnel, managed the open tender process for the Project and will oversee the construction and operation of the Project according to the relevant laws and regulations of the Republic of Cyprus. The monitoring process will be carried out at the national level by the Project Steering Committee appointed by the Government of Cyprus and formed by representatives of Ministries and local and national institutions (including the Public Procurement Directorate) and at the EU level by the EU Innovation and Networks Executive Agency (INEA).

[REDACTED]. The Project will be procured under a single, comprehensive contract which includes design, procurement, construction, operation and maintenance of an FSRU to unload LNG from LNG carriers and offshore and onshore infrastructure, thus minimising the need to manage different interfaces under the Project.

The Contract conditions include clear responsibilities and liabilities for both parties. Key elements are enshrined in the Cyprus Procurement Law and implementing regulations.

Project implementation arrangements:

Procurement and implementation of the Project is under the responsibility of ETYFA, with the support of DEFA personnel.

During tendering ETYFA was supported by several operations, technical and engineering, legal and finance advisors and in particular Navigant (energy and financial advisor), DLA Piper (legal advisor), WSP (engineering advisor) and Rogan Associates (design and construction).

During Project implementation, the Project will be managed by an appointed Project Management Unit (PMU). The PMU will consist of dedicated personnel from ETYFA and DEFA and personnel from the external Owner's Engineer, to be appointed following a competitive tender procedure (launched in March 2020). This consultant will be in place to coordinate and support the company with all tasks relevant to project management and supervision and monitoring of the construction until project completion. This structure should strengthen project implementation ability within the Company and mitigate risks of project implementation delays.

A Lender's Engineer will be hired within the Project to monitor the Project implementation, including the Bank's disbursements. The Lender's Engineer will report to both EBRD and EIB on outcomes from Project monitoring throughout the implementation period (2020-2022) and the first two years of operation of the Project. It will provide quarterly reports to the Bank on the progress of the construction and participate in regular site visits.

Procurement arrangements:

As per the regulation establishing the CEF, procurement must be carried out by the EC or one of the relevant bodies in accordance with the EU and national public procurement principles. The Bank has reviewed the relevant public procurement laws and regulations of the Republic of Cyprus and the tender documents used for the Project and determined that the rules and procedures followed are fair and transparent and not discriminatory, and generally in line with the key principles of the EBRD PP&R and good international practice.

Thus an exception from the use of the Bank's PP&R, as envisaged under Clause 2.4 of the PP&R has been reviewed by FOPC on the 18th July 2019 (see FOPC Minutes at CS/FO/M/19-

33) and recommended for approval by the Board to allow the use of national procurement rules [REDACTED].

The Bank's Enforcement Policy will apply and the Bank's legal documentation will provide that EBRD loan proceeds will not be available for financing contracts with any entity appearing on the EBRD list of debarred entities.

Actual status of the LNG Import Infrastructure Tender and Contract execution:

The contract is being procured through a single stage open international tender. The tender notice was published in the EU Official Journal and in the Cyprus E-procurement system on 2 October 2018. Clarifications and a site visit took place in 4Q 2018 and the deadline for bid submission was set on 12 July 2019. Nine consortia have taken part in the bid process. Tender documents have been prepared using standard templates and have been approved by the Project's Steering Committee. Out of the three consortia submitting a proposal and by applying the evaluation criteria included in the tender documents, the tender process evaluation first ranked tenderer (being a consortium consisting of five members: China Petroleum Pipeline Engineering Co Ltd (CPP), Aktor SA (Aktor), Metron SA, Hudong-Zhonghua Shipbuilding Co. Ltd and Wilhelmsen Ship Management Limited) has been awarded with the Contract.

In December 2019, ETYFA required the consortium, in accordance with the tender rules, to remove Aktor [REDACTED]. The Contract was signed on 13 December 2019 with the Joint Venture of China Petroleum Pipeline Engineering Co Ltd and METRON S.A. Energy Applications, forming a consortium with Hudong-Zhonghua Shipbuilding Co. Ltd and Wilhelmsen Ship Management Limited. ETYFA issued the Notice to Proceed to the Contractor for the commencement of the works on 29th May 2020. . The construction period in the Contract is two years from the Notice to Proceed. [REDACTED].