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Dear Frances

**Centrica Storage Limited (“CSL”)’s application to reduce the Minimum Rough Capacity and Additional Space for the 2017/2018 Storage Year**

In 2003, following CSL’s acquisition of the Rough Gas Storage Facility from Dynegy Group (**Dynegy**), Centrica and CSL gave undertakings (the **Undertakings**) to the Secretary of State for Trade and Industry pursuant to the Fair Trading Act 1973. Pursuant to the Enterprise Act 2002, the Competition and Markets Authority<sup>1</sup> varied the Undertakings in 2006, 2011 and 2016. Pursuant to the Undertakings, CSL is required to offer for sale the Minimum Rough Capacity (**MRC**) and Additional Space (**AS**) ahead of each Storage Year (the MRC and AS are, together, referred to as the **Obligated Capacity**). The Obligated Capacity is currently 455 million Standard Bundled Units (**SBU**s) and 1.534TWh of AS.

Paragraph 2.10 of the amended Undertakings permits CSL to apply to Ofgem to adjust the amount of capacity CSL is required to sell ahead of the Storage Year on the basis that *“there has been, or may be expected to be, a substantial change in Rough Capacity which may be expected to affect the next, or subsequent Storage Years”* (the **Adjustment Mechanism**).

In 2015, CSL identified that there were risks associated with continuing the operation of Rough’s wells at pressures of 3500psig without further testing of the integrity of the wells. This resulted in CSL placing a pressure limit of 3000psig for operating Rough’s wells and gaining the Oil and Gas Authority (**OGA**)’s consent to store gas lower in the reservoir<sup>2</sup>. Further, CSL commenced a testing program (**Well Testing Program**) to verify which wells could safely be returned to operating pressures of 3500psig.

Between March 2015 and July 2016, CSL conducted calliper runs on 19 wells and pressure tests on 8 wells.

In July 2016, in the course of the Well Testing Program, CSL identified potential risks with the wells which resulted in CSL suspending all injection and withdrawal operations. Although CSL later identified that gas could be withdrawn from Rough safely, it determined that, based on the information currently known and mitigations in place, it could not reinstate injection until all wells had been tested.

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<sup>1</sup> From 1 April 2014 the Competition and Markets Authority took over many of the functions of the Competition Commission (CC), including responsibility for the keeping the Undertakings under review.

<sup>2</sup> From between -50bcf and 115bcf instead of -35bcf and 115bcf

Looking forward to the 2017/2018 Storage Year, owing to these operational and safety issues, it has become clear that Rough is not able to physically support anywhere close to the volume of capacity it was assumed to be capable of supporting when the obligations to sell capacity were incorporated in the Undertakings. As a consequence, CSL considers these circumstances should entitle it to seek a reduction in the volume of MRC and AS it is obliged to sell ahead of the 2017/2018 Storage Year.

In accordance with paragraph 2.10 and Annex 11 of the Undertakings, CSL has attached the following documents in support of its application to adjust the MRC and AS for the 2017/2018 Storage Year:

- 1 CSL's formal application document, setting out CSL's proposed adjustment to the Obligated Capacity; and
- 2 A non-confidential version of CSL's formal application for the purposes of facilitating a market consultation on CSL's proposed adjustment.

CSL considers that the information provided in these documents, combined with information provided separately to Ofgem and the independent expert Advisers CSL has appointed on Ofgem's behalf are consistent with the requirements of paragraphs 2.10, 2.11 and Annex 11 of the Undertakings.

In developing its application, CSL has acknowledged that, since 2002 when it acquired Rough, there has always been some degree of shortfall between Rough's physical withdrawal capabilities and the withdrawal rights associated with its regulatory obligation to sell the MRC. This is because Rough's previous operators had sold 28bcf of cushion gas which meant that, at the time CSL gave the Undertakings, Rough was already incapable of physically delivering the 455 million standard bundled units of 1kWh/day of withdrawal, 66.593407kWh of space and 0.351648kWh/day of injection. While CSL accepted that risk 13 years ago; this mismatch between Rough's physical capabilities and CSL's regulatory obligations is no longer manageable. This is primarily due to the increased magnitude of the mismatch and Rough's advanced age and the operational uncertainties accompanying this.

As set out in CSL's application (and in recognition of this historical discrepancy), CSL has sought to substantially re-align its obligation to sell the MRC with Rough's physical capabilities whilst retaining some risk and cost in managing a residual mismatch. CSL considers its proposed adjustment to the Obligated Capacity strikes a reasonable balance between the interests of market participants in ensuring the maximum technical capacity of Rough is offered to the market and the risk and costs CSL should be required to take on in offering that capacity.

In accordance with paragraph 2 of Annex 11 of the Undertakings, CSL is proposing to conduct a consultation in accordance with the approach and process set out below in order to give Market Participants the opportunity to provide their views on CSL's application and whether Ofgem should approve it.

CSL's consultation document will set out the methodology by which Rough's physical capability can be projected and a methodology by which this projected physical capability can be converted into MRC and AS.

CSL will set out a range of scenarios reflecting the proposed methodologies. These scenarios are primarily based on the availability of Rough's wells for injection and withdrawal. They also include one scenario where there are no wells available for injection and withdrawal (based on well test results or due to other operational risks identified and verified which mean that CSL as a prudent operator cannot recommence physical injection operations at the start of the 2017/2018 Storage Year. This is discussed further in section 5.7 of the application).

These scenarios will form the basis of how CSL will offer Rough's physical capabilities in 2017/2018. CSL will provide the market and Ofgem with specific information about Rough's expected capabilities on or before 28 February 2017 which will constitute a non-material amendment to CSL's application.

The process and timings for the market consultation are as follows:

- 1 CSL will announce the consultation on its website and CSL's STORIT system;
- 2 The consultation will run for a period of five weeks from 15 December 2016 until 20 January 2017;
- 3 Market Participants can provide written submissions to CSL or directly to Ofgem (CSL will provide Ofgem with all submissions that CSL receives);
- 4 Ofgem is not required to make a decision on CSL's application within a specified time period, however, CSL is seeking a decision no later than 10 March 2017 to enable CSL to offer the Obligated Capacity in the manner contemplated in the Undertakings; and
- 5 Once the Obligated Capacity has been formally set, CSL will promptly (within five working days) post details on its website and STORIT and will offer any unsold Obligated Capacity in accordance with the Undertakings.

CSL intends to formally commence the consultation process on 15 December 2016 subject to any direction from Ofgem concerning the consultation process and timing.

Should you or your team require any further information regarding this application, please direct your enquiries to Antony Miller ([antony.miller@centrica-sl.co.uk](mailto:antony.miller@centrica-sl.co.uk))

Yours sincerely



Greg McKenna  
**Managing Director**