

**Centrica Storage Limited (“CSL”)’s application to reduce the Minimum Rough Capacity and Additional Space for the 2017/2018 Storage Year (Amended in accordance with Annex 1, paragraph 2 of the Undertakings)**

*Final Application – 28 February 2017*



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## 1. Purpose of this document

Due to operational and safety issues it has become clear that Rough is not able to physically support the volume of capacity it is obliged to offer for sale under the Rough Undertakings<sup>1</sup> (455 million Standard Bundled Units (**SBU**s) (the Minimum Rough Capacity (**MRC**) and 1.534TWh of Additional Space (**AS**)). As a consequence, CSL considers these circumstances 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 (**Obligated Capacity**).

Pursuant to paragraph 2.10 of the Undertakings, CSL is entitled to apply to Ofgem to adjust the Obligated Capacity where there has been, or may be expected to be, a substantial change in Rough's physical capabilities. One of the requirements of such an application is that an appropriate market consultation process is conducted "*whereby Market Participants can provide their views on CSL's application and whether Ofgem should approve it*".

On 15 December 2016, CSL launched a consultation on its application to reduce the MRC and AS for the 2017/2018 Storage Year (**December 2016 Consultation Document**). At that time there was significant uncertainty regarding Rough's expected physical capabilities for the 2017/2018 Storage Year. To address this uncertainty, CSL consulted on four different scenarios for Rough's physical capabilities and the volumes of MRC and AS CSL considered it should be required to offer under those different scenarios.

On 16 February 2017, CSL determined that based on the results of the calliper survey and well testing program, and following a review with its independent technical advisers, that the uncertainties associated with emerging well failures, plus the age and condition of the assets, meant CSL was not currently in a position to offer injection services for the storage season 2017/18<sup>2</sup>. Further, CSL expects that it will take in the order of 2 months following completion of the well testing program to assess the results and determine whether injection operations can be safely re-instated (and, if so, within what timeframe).

On this basis, CSL has modified its original consultation to remove all but the actual operational condition of Rough as now understood; namely, having no wells available for injection before 16 May 2017 (this was Scenario 1 in the December 2016 Consultation Document). As set out in Section 7 of the December 2016 Consultation Document, under this scenario CSL has proposed that the Obligated Capacity should be set to 0 (zero) SBUs and 0 (zero) TWh of AS. CSL identified 15 May 2017 as the last date on which CSL could return to injection operations and still offer capacity in SBU form (see Section 8.1 of the December 2016 Consultation Document).

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<sup>1</sup> See Section 4 for the background to the Rough Undertakings

<sup>2</sup> See REMIT bulletin 2017-23A (<http://www.centrica-sl.co.uk/regulation/remit/2017-23a>)

This Application Document updates and modifies the December 2016 Consultation Document as contemplated in Section 2 of that document and constitutes CSL's final Application to adjust the MRC and AS in accordance with Annex 1 and Annex 11 of the Undertakings<sup>3</sup>. In accordance with Annex 1 paragraph 2 of the Rough Undertakings, CSL has proposed to Ofgem (and Ofgem has accepted) that this is a non-material change to the December 2016 Consultation Document on the basis that CSL's final proposal is simply the implementation of Scenario 1 in that document. This final Application Document demonstrates that the Maximum Technical Storage Capacity of space in Rough which can be calculated as at 28 February 2017 is 0 (zero) TWh<sup>4</sup>. This final Application Document implements CSL's proposed and published methodology for converting Rough's Maximum Technical Storage Capacity into a volume of MRC and AS. The approach to determining the Maximum Technical Storage Capacity and converting this into MRC and AS is unchanged from that set out in Sections 7 and 8 of the December 2016 Consultation Document.

## **2. Approach to the final application**

CSL has set out below, each of the Undertakings requirements relating to the application process and explained how each has been addressed.

### *2.11(a) Identify the substantial change in Rough Capacity and the reasons for it*

In Section 5 of this document, CSL has set out a detailed explanation for the change in Rough Capacity for the 2017/2018 Storage Year, together with CSL's response to the emergence of those issues and the operational and financial impact on CSL and its customers.

### *2.11(b) Identify the proposed MRC and AS for the next Storage Year and demonstrate the sum of the varied MRC and AS is at least the Maximum Technical Storage Capacity of Space in Rough which can be calculated in advance of the Storage Year*

In Section 7 of this document, CSL explains the Maximum Technical Storage Capacity in 2017/2018 and how this should be converted into volumes of MRC and AS.

### *2.11(c) Identify the proposed allocation between MRC and AS and the reasons for that allocation*

CSL addresses this issue in Section 7 of this Application Document.

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<sup>3</sup> For the purposes of Annex 1 and Annex 11, this final Application should also be considered as CSL's amended consultation document

<sup>4</sup> In accordance with Article 17 of the Gas Regulation (EC) No 715/2009, CSL considers that Rough's Maximum Technical Storage Capacity is zero, taking into account system integrity and operation

2.11(d) *Identify whether an adjustment of Specified Capacity in accordance with paragraph 3.6(a) is proposed in relation to the application and the reasons for it*

In Section 8.3, CSL proposes that there should be no substantive changes to the Specified Capacity restrictions as currently set out in the Undertakings.

2.11(e) *Provide any other relevant information*

Section 8 of this document sets out other relevant information concerning the application, in particular in relation to ensuring CSL's continued compliance with relevant provisions of the Undertakings.

### **3. Market participants' views on CSL's December 2016 Consultation Document and final Application Document**

As CSL considers that this final Application Document has not materially changed from the December 2016 Consultation Document, CSL is not seeking Market Participants' views on the modifications.

Pursuant to Annex 11 of the Undertakings, CSL received responses to the December 2016 Consultation Document from 6 Market Participants.

CSL has reviewed these responses and notes that no market participants questioned the desirability of ensuring the Obligated Capacity is aligned with Rough's physical capabilities. However, a number of responses did highlight the need for greater certainty regarding Rough's expected capabilities ahead of the 2017/2018 Storage Year. CSL considers it has now provided this certainty through the publication of its REMIT bulletin 2017-23A on 16 February 2017.

Annex 1 provides a summary of issues raised by Market Participants and CSL's response.

If you have any questions on the final Application Document, please contact Antony Miller ([Antony.Miller@centrica-sl.co.uk](mailto:Antony.Miller@centrica-sl.co.uk) or +44 (0) 7557611924).

If you have any questions for Ofgem, please contact Ed Freeman ([Edward.Freeman@ofgem.gov.uk](mailto:Edward.Freeman@ofgem.gov.uk) or +44 (0) 207 901 3121).

#### 4. Final Application Document

In 2003, following CSL's acquisition of the Rough Gas Storage Facility (**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>5</sup> varied the Undertakings in 2006, 2011 and 2016.

Pursuant to the Undertakings, CSL is required to offer for sale the Obligated Capacity ahead of each Storage Year. The Obligated Capacity is currently 455 million SBUs 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 3,500psig without further testing of the integrity of the wells. The specific concern related to the calculation of the Maximum Allowable Annular Surface Pressure (**MAASP**). This resulted in CSL placing a pressure limit of 3,000psig for operating Rough's wells and gaining the Oil and Gas Authority (**OGA**)'s consent to store gas lower in the reservoir<sup>6</sup>. Further, CSL commenced a testing program (**Well Testing Program**) to verify which wells could safely be returned to operating pressures of 3,500psig.

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.

Since that time, CSL has continued its Well Testing Program and undertaken a range of other activities to enhance its understanding of the integrity of the Rough well stock and offshore installations. In relation to the well testing results, 6 of 14 wells have failed the pressure test and other issues have been identified with 3 wells. In addition, CSL has further developed its understanding of the integrity of the Rough assets. Given the uncertainties associated with the differing failure modes of the wells, plus the age and

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<sup>5</sup> From 1 April 2014 the Competition and Markets Authority took over many of the functions of the Competition Commission (CC), including responsibility for keeping the Undertakings under review

<sup>6</sup> From between -50bcf and 115bcf instead of -35bcf and 115bcf

condition of the assets, CSL has determined that it cannot offer injection services for the storage season 2017/18 at the present time. CSL intends to conclude the Well Testing Program and will then analyse all test results to determine whether further works are necessary in order to re-commence safe injection operations (and if so, the timeframes for completing these works)<sup>7</sup>. These issues are discussed further in Section 5 of this document.

On this basis CSL has amended its application to Ofgem, to propose that:

- (i) the Obligated Capacity (MRC and AS) for the 2017/2018 Storage Year be set at 0 (zero) SBUs and 0 (zero) TWh of AS based on Rough’s projected physical capabilities known ahead of the 2017/2018 Storage Year; and
- (ii) there is no change to the Specified Capacity. Specifically:

Centrica will be permitted to purchase up to 25 per cent of the MRC and up to 1.534TWh of AS	Equates to 0 (zero) SBUs and 0 (zero) TWh of AS (as CSL is not proposing to offer any AS)
CSL does not propose any change to the requirements of paragraph 3.3(c) of the Undertakings and therefore Centrica will be prohibited from purchasing Incremental Capacity ahead of the 2017/2018 Storage Year until CSL has made available no less than 34.7TWh of space for the 2017/2018 Storage Year	Equates to 0 (zero) TWh as CSL will not be offering any capacity ahead of the 2017/2018 Storage Year
CSL does not propose any change to the requirements of paragraph 3.7 of the Undertakings and therefore Centrica will be permitted to purchase up to 100 per cent of Rough Capacity sold within the 2017/2018 Storage Year	Centrica will be entitled to make offers for and purchase any Further Additional Space and Incremental Capacity CSL is able to make available during the 2017/2018 Storage Year via CSL’s objective, transparent and non-discriminatory sales process

CSL has prepared its final Application in accordance with paragraph 2.11 and Annex 11 of the Undertakings. The modification to the December 2016 Consultation Document as the basis for CSL’s final Application Document has been completed in accordance with Annex 1, paragraph 2 of the Undertakings.

<sup>7</sup> See REMIT bulletin 2017-23A (<http://www.centrica-sl.co.uk/regulation/remit/2017-23a>)

In accordance with both the requirements and process set out in Annex 11 of the Undertakings, CSL has appointed Axis Well Technology Limited (**Axis**) and Genesis Oil and Gas Consultants Ltd (**Genesis**) to act as Advisers to Ofgem. CSL has provided technical information supporting the modifications to its application to both Ofgem and the Advisers. The function of these Advisers is to advise Ofgem on the merit and accuracy of CSL's final application, which CSL understands they have performed and will continue to perform in light of this Application Document.

## **5. Identifying the substantial change in Rough Capacity and the reasons for it**

In the December 2016 Consultation Document, CSL provided some background regarding:

- (i) the Rough Gas Storage Facility;
- (ii) the limitation on Rough's maximum operating pressure in March 2015 and CSL's response to those issues;
- (iii) "further issues" with the wells that CSL had identified during its Well Testing Program;
- (iv) the impact on asset capabilities associated with the withdrawal of Cushion Gas;
- (v) the impacts of the permanent withdrawal from service of the 47/8A installation; and
- (vi) other uncertainties associated with the modes of the well failure and integrity of the topside equipment that may result in CSL determining that it is unsafe to return Rough to injection operations.

Below, CSL explains the basis for its decision that, as a reasonable and prudent operator, it cannot safely return to injection operations prior to 16 May 2017<sup>8</sup>.

### **5.1. Summary of the factors that resulted in the substantial reduction in Rough Capacity for 2017**

In its December 2016 Consultation Document, CSL set out a number of changes to Rough's characteristics that substantially reduced its operating capabilities in the 2017/2018 Storage Year such that the Obligated Capacity is no longer aligned with these capabilities. Specifically, the changes are:

- (i) at a minimum, wells B11, B3<sup>9</sup> and C6 will be unavailable for injection and withdrawal operations;

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<sup>8</sup> CSL identified 15 May 2017 as the last date on which CSL could return to injection operations and still offer capacity in SBU form (see Section 8.1 of the December 2016 Consultation Document)



- (ii) well C12's<sup>10</sup> withdrawal performance has been significantly reduced;
- (iii) the production of Cushion Gas over the years has substantially changed Rough's operating envelope;
- (iv) CSL has permanently withdrawn the 47/8A installation (and its 6 wells) from service; and
- (v) there are a range of other operational uncertainties affecting the Facility that may limit Rough's injection and/or withdrawal capabilities. These include the outcome of the Well Testing Program and the uncertainties associated with operating an aging asset.

Since the publication of the December 2016 Consultation Document, CSL has:

- (i) conducted pressure tests on a further 6 wells with 4 failing those tests;
- (ii) not been able to conclusively ascertain the mode of failure in all cases for the wells which failed the pressure test; and
- (iii) continued to develop its understanding of the condition of the Rough assets.

#### **5.1.1. Further pressure test results**

As at 15 December 2016 (the date on which CSL published the December 2016 Consultation Document), CSL had conducted calliper surveys on 19 wells and conducted pressure tests on 8 of these wells. During the course of this period of the Well Testing Program:

- (i) the results of the calliper surveys are typically positive and degradation has occurred at a slower rate than industry models at around 10-12 per cent with the exception of one well, C8, which shows localised corrosion greater than 40 per cent; and
- (ii) of the 8 wells that had been subject to calliper surveys and pressure testing:
  - (a) one well failed the pressure test at low pressures (C6);
  - (b) one well was found to have a leak in the primary barrier (B11);
  - (c) one well has a known primary barrier failure (B3); and
  - (d) one well has blockages which reduce its performance (C12).

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<sup>9</sup> As set out in Section 5.3 of the December 2016 Consultation Document, CSL considers that it may be able to return well B3 to operations at some point in the future. However, the necessary remedial works will not be possible within the calendar year 2017

<sup>10</sup> As set out in Section 5.4 of the December 2016 Consultation Document, CSL has as yet not been able to identify the specific cause of the reduction in capability and therefore cannot determine what remedial actions, if any, could return the well to its historic capabilities

Since 15 December 2016, CSL has performed a calliper survey on one further well and performed pressure tests on 6 further wells. During the course of this period of the Well Testing Program:

- (i) the results of the calliper surveys continue to be typically positive and degradation has occurred at a slower rate than industry models at around 10-12 per cent; and
- (ii) of the 8 wells that have been subject to calliper surveys and pressure testing:
  - (a) four wells failed the pressure test (C9, C3, C10 and C1);
  - (b) one well passed the pressure test but the plug cannot currently be removed (C2); and
  - (c) the issues affecting the Rough wells resulting in CSL considering them incapable of safe injection operations are varied and do not seem to follow a predictable pattern.

#### **5.1.2. Other integrity issues affecting the Rough assets**

The Rough assets have successfully operated significantly beyond their design life. However, as they age, the number of anomalies increases and the demand for inspection and maintenance increases. The general effect of age has been demonstrated:

- (i) during the work CSL performed as part of the 2016 jack-up campaign;
- (ii) in the results of the Well Testing Program;
- (iii) by the discovery of potential further integrity issues relating to the 47/8A platform as work has commenced to isolate its wells from the reservoir;
- (iv) through the draft findings of additional reports CSL has commissioned on specific aspects of the assets and their operation; and
- (v) in November 2016 as CSL conducted its assurance process ahead of re-commencing withdrawal operations.

Before re-commencing injection operations, CSL must complete an assurance process comparable to that process enacted before re-commencing withdrawal operations.

#### **5.1.3. Conclusion as to Rough's Maximum Technical Storage Capability**

CSL considers that the cumulative effect of the issues identified above means that CSL cannot permit injection operations to re-commence before 16 May 2017<sup>11</sup> and,

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<sup>11</sup> CSL identified 15 May 2017 as the last date on which CSL could return to injection operations and still offer capacity in SBU form (see Section 8.1 of the December 2016 Consultation Document)

consequently, the Maximum Technical Storage Capacity of space in Rough for the purposes of the Obligated Capacity should be considered to be zero.

## **5.2. The financial implications to CSL and its customers of having to manage a significant mismatch in Rough's physical capabilities and the Obligated Capacity**

CSL's decision to conduct the Well Testing Program was not driven by financial imperatives but was made by CSL, acting as a reasonable and prudent operator, and having regard to its obligation to ensure Rough continues to operate safely.

In the December 2016 Consultation Document, CSL set out the substantial costs to both it and its customers of being required to offer capacity which is not aligned with Rough's physical capabilities.

CSL estimated that offering the Obligated Capacity if CSL had 21 wells that were operating at levels of availability on demand of c.90 per cent would expose CSL to costs in the order of £12.3 million (see section 5.9.3 of the December 2016 Consultation Document for details). The purpose of these calculations was to demonstrate the potential costs to CSL of having to offer capacity in SBU form which was also in excess of Rough's physical capabilities.

CSL does not expect to be able to determine whether it will be feasible to re-commence injection operations until 30 June 2017. In these circumstances, if CSL were to sell SBUs or injection capacity under the terms of the SSC ahead of the 2017/2018 Storage Year, such capacity would not be asset-backed (certainly between 1 May and 30 June 2017 and possibly after 30 June 2017) and CSL would not be capable of performing its obligations under the SSC and Security Trust Deed<sup>12</sup> to accept or deliver gas in accordance with customer nominations.

As a consequence, CSL would be required to cancel injection rights on every day that Rough was not available for injection. Under the SSC, this would result in customers with SBU bookings receiving no compensation for the first 15 days of the 2017/2018 Storage Year, and then receiving a refund of 20 per cent of the amount they paid for their SBUs on each additional day that injection was cancelled. If CSL were not able to re-instate injection operations at all, customers could potentially pay 80 per cent of the SBU purchase price and receive no physical storage capacity. In addition, these customers would not be certain of how much storage capacity they have during the Storage Year so they are also likely to face significant costs and risks associated with hedging their capacity booking.

As CSL cannot offer injection capacity with any volume of unbundled space that theoretically exists in Rough, such space is effectively inaccessible and CSL does not consider it appropriate to be required to offer it to customers under these conditions. A

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<sup>12</sup> [http://www.centrica-sl.co.uk/files/security\\_trust\\_deed\\_of\\_charge.pdf](http://www.centrica-sl.co.uk/files/security_trust_deed_of_charge.pdf)

number of the consultation responses received by CSL expressed the importance of CSL not being required to offer Rough capacity on a speculative basis, due to the potential costs to customers that booked the capacity and the impact that it might have on the wholesale market.

#### **6. CSL’s proposal for offering Rough Capacity for the 2017/2018 Storage Year**

Due to CSL being unable to re-commence injection operations before 16 May 2017, in accordance with its December 2016 Consultation Document, CSL is proposing that the Obligated Capacity be set to 0 (zero) SBUs and 0 (zero) TWh of AS.

Should CSL determine that it can, acting as a reasonable and prudent operator, re-commence injection operations during the 2017/2018 Storage Year, it will offer Rough Capacity as Further Additional Space, incremental space, incremental injection capacity or incremental withdrawal capacity. CSL will offer the available capacity in accordance with the Undertakings and the Gas Regulation<sup>13</sup> in both bundled and unbundled form.

#### **7. CSL’s proposed Minimum Rough Capacity and Additional Space**

As explained above, CSL has:

- (i) sought to demonstrate to Ofgem and its appointed technical Adviser (Axis), as at 28 February 2017, Rough’s projected Facility capability and availability for the 2017/2018 Storage Year based on all available relevant operational and well testing information; and
- (ii) on the basis that CSL cannot safely re-commence injection operations by 16 May 2017 and will not be able to determine if it can re-commence injection operations before 30 June 2017, Rough’s expected physical capabilities for the 2017/2018 Storage Year must be based on the zero well scenario (Scenario 1, summarised below).

<b>Number of Wells</b>	<b>SBUs</b>	<b>Additional Space</b>
0	0	0

As set out in the December 2016 Consultation Document, under this scenario CSL does not incur any financial risk associated with deliverability or injection support (depending on how it manages existing capacity bookings for the 2017/2018 Storage Year). Should CSL have capacity within the Storage Year it will be offered as bundled and unbundled volumes which are aligned with Rough’s expected capabilities.

Since publication of REMIT bulletin 2017-23A, CSL has commenced negotiations for the mutual release of rights and obligations associated with 2017/2018 SBU bookings acquired ahead of that bulletin.

<sup>13</sup> Gas Regulation (EC) No 715/2009

## **8. CSL's regulatory obligations**

### **8.1. Requirement to sell capacity ahead of the Storage Year**

The Undertakings require CSL to offer for sale all Rough Capacity for each Storage Year, and the sum of the MRC and AS will be at least the Maximum Technical Storage Capacity of space in Rough which can be calculated in advance of the Storage Year, (but not more than 31.834TWh).

As set out in the December 2016 Consultation Document, CSL considers that if it is incapable of re-commencing injection operations before 16 May 2017, the Maximum Technical Storage Capacity of space should be considered to be 0 (zero) TWh. As demonstrated above, CSL has determined that it is not capable of re-commencing injection operations before 16 May 2017. On the basis that Ofgem accepts CSL's final application, CSL will have met the obligations of the Undertakings in relation to offering capacity ahead of the Storage Year.

In relation to offering all capacity within the Storage Year, if CSL determines that it can safely re-instate injection operations within the 2017/2018 Storage Year, it will offer all available capacity using its established processes for offering capacity within a Storage Year. These processes include informing all market participants that CSL is offering capacity via news bulletins published on its website and publications on STORIT. Subject to being signatories to the SSC and meeting credit and compliance requirements, all market participants are capable of bidding for offered Rough Capacity.

### **8.2. Ensuring CSL is able to offer 20 per cent of the MRC on annual contracts**

Paragraph 2.2(a) of the Undertakings requires CSL to offer for sale at least 20 per cent of Minimum Rough Capacity on annual contracts. As 20 per cent of 0 (zero) SBUs is 0 (zero), provided Ofgem accept CSL's amended application, CSL will be compliant with this requirement.

### **8.3. Limit on maximum volume sold to Centrica Group**

As set out above (Section 4) CSL is proposing that no changes should be made to the provisions of the Undertakings in relation to the capacity that can be sold to the rest of Centrica for the 2017/2018 Storage Year.

To the extent that Centrica has capacity bookings for the 2017/2018 Storage Year, CSL intends to negotiate the mutual release of rights and obligations associated with that capacity. Thus, Centrica will be entitled to 0 (zero) per cent of the MRC and will hold 0 (zero) per cent of the MRC. As part of the reporting requirements of the Undertakings, CSL must confirm to Ofgem the total 2017/2018 storage capacity held by Centrica Group as at 30 April 2017.

CSL is not proposing any changes to the Specified Capacity of Incremental Capacity. This means that Centrica will be permitted to purchase up to 100 per cent of Rough

Capacity sold within the 2017/2018 Storage Year. CSL considers that given the uncertainty associated with the amount of capacity CSL may be able to offer within the 2017/2018 Storage Year that placing ex ante limits on the amount of capacity CSL can sell to Centrica is likely to be counter-productive by artificially limiting potential demand for that capacity which could in turn result in underutilisation of the available capacity.

CSL notes that it is subject to the requirements of the Gas Act 1986, Gas Regulation and the Undertakings which require CSL to offer all Rough Capacity via an objective and transparent allocation process whereby capacity is offered and sold on non-discriminatory terms. This means that CSL must ensure all eligible Market Participants can bid for any capacity CSL can make available within the 2017/2018 Storage Year. Further, CSL must provide sales reports to Ofgem setting out all bids and offers for Rough Capacity<sup>14</sup>. This allows Ofgem to scrutinise the behaviour of both CSL and Centrica in relation to the allocation of Rough Capacity.

#### **8.4. Compliance monitoring**

To address any concerns Market Participants may have regarding access to Incremental Capacity CSL is able to release in the 2017/2018 Storage Year, if Ofgem accept CSL's application, CSL also intends to provide additional ex post reports to Ofgem detailing Centrica's capacity purchases for the 2017/2018 Storage Year. These reports will be updated within 10 Working Days of Centrica purchasing firm capacity with a duration of more than one day.

CSL will also provide Ofgem and the CMA with an annex to its compliance report for Compliance Year ending on 31 August 2017 setting out:

- (i) total SBU and AS sales;
- (ii) release and sales of strips of Incremental Capacity (including maintaining separation of information on asset changes from those managing CSL's hedging program); and
- (iii) compliance with reporting requirements for CSL sales to Centrica.

CSL notes that under paragraph 9 of the Undertakings, CSL is required to submit an independently verified injection and capacity report covering the 2017/2018 injection season. This provides market participants with additional comfort that CSL is making Rough's maximum storage capacity available to the market.

#### **8.5. Other Undertakings compliance requirements**

CSL has reviewed the compliance and reporting requirements in the Undertakings in light of this final application to consider whether they need to be adjusted or supplemented. CSL has not identified any necessary adjustments or inconsistencies.

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<sup>14</sup> See paragraph 10.1 of the Undertakings

As set out in Section 8.4, CSL is proposing to undertake additional reporting obligations if Ofgem approve its application.

#### **9. Application process and next steps**

The Undertakings do not specify a timeframe for Ofgem to reach its decision regarding changing the Obligated Capacity. However, CSL is seeking Ofgem's decision by 10 March 2017.

Following notification from Ofgem of its decision regarding this application, CSL will promptly (within 5 working days) post the details of the decision on the CSL website and issue a statement announcing Ofgem's decision on STORIT.

## **Annex 1: Summary of responses to CSL's 15 December 2016 Consultation on reducing the Minimum Rough Capacity and Additional Space**

On 15 December 2016, CSL launched its consultation on its application to reduce the Minimum Rough Capacity and Additional Space for the 2017/2018 Storage Year. The consultation closed on 27 January 2017.

CSL invited Market Participants to give their views on matters such as:

- (i) whether CSL's proposed approach to setting the MRC and AS is reasonable in light of all the circumstances surrounding this application;
- (ii) whether CSL's approach to offering the Maximum Technical Capacity of Rough (i.e. pre-withdrawal) is an appropriate basis for maximising the number of SBUs it can offer ahead of the Storage Year;
- (iii) CSL's proposed allocation of technical capacity between MRC and AS based on the scenarios set out in the December 2016 Consultation Document; and
- (iv) Market Participants' appetite for buying injection and space capacity without corresponding withdrawal capacity.

Four market participants responded directly to CSL on this consultation. In line with the requirements of Annex 11 of the Undertakings, CSL provided these responses to Ofgem promptly following the closing of the consultation. In addition, Ofgem provided CSL with two further responses it had received directly from market participants.

The following provides a summary of comments CSL received and CSL's response.

### **(i) *Whether CSL's proposed approach to setting the MRC and AS is reasonable in light of all the circumstances surrounding this application***

Respondents were generally supportive of the MRC and AS being reduced to align with Rough's technical capacity. A number of respondents noted that it was important that it was important for the wholesale gas market that the capacity that CSL be obliged to sell is based on a complete understanding of the state of Rough's expected capabilities for the 2017/2018 Storage Year, rather than based on predictions that could result in potentially inflated estimates of Rough's expected capabilities. For example one respondent stated:

*'We accept the arguments supporting CSL's proposal to set the Obligated Capacity (MRC and AS) for the 2017/18 Storage Year based on Rough's projected physical capabilities, including the expected outcomes of its Well Testing Programme... However, we suggest that an alternative cut off date is considered for projecting Rough's physical capabilities [closer to the start of the Storage Year]... This would allow CSL to obtain more reliable inputs for the*



*'Rough Forecast Tool' and to produce more credible projections of Rough's physical capabilities'*

Another commented that:

*'Information provided should on future available storage capacity [from Rough] should be realistic and not seek to be reassuring, as overly optimistic assumptions might distort the price and volatility expectations'*

In contrast, three respondents considered it important that CSL inform the market of Rough's expected physical capabilities and amount of capacity it expects to offer as soon as possible, and *'well in advance of the Storage Year'*.

### **CSL's response:**

CSL considers that its final Application struck the balance between the need to wait for the best possible information about Rough's operational status and the need to allow sufficient time to offer available capacity to market participants in accordance with the Undertakings. CSL considers that its REMIT notification 2017-23A on 16 February 2017 provided clarity to the market that CSL could not re-commence injection operations before 16 May 2017, the date CSL considered was relevant for setting the MRC to zero SBUs.

#### **(ii) *Whether CSL's approach to offering the Maximum Technical Capacity of Rough (i.e. pre-withdrawal) is an appropriate basis for maximising the number of SBUs it can offer ahead of the Storage Year***

A number of respondents commented on the importance of maintaining the relationship between Rough's technical capabilities and the volume of capacity CSL is obliged to offer. For example, one respondent commented that:

*'It is important to ensure that CSL is not driven by regulatory oversight to set a Storage Year 2017/18 MRC which is over-ambitious relative to the uncertain technical capability of the asset, since this would perpetuate an undue level of risk to the business and its customers. It would also send misleading signals to the wider wholesale gas market.'*

Only two respondents commented directly on the use of pre-withdrawal, one respondent noted that they would *'like to better understand "pre-withdrawal"... as depending on scale, this could have operational impacts upon linepack and daily balancing'*.

Another respondent stated that they:

*'do not have any objections to CSL adopting the 'pre-withdrawal' approach to managing the Rough envelope so that a larger number of SBUs could be*

*provided to its customers. In our view, such an optimisation of Rough's capabilities reflects an efficient approach to operating a gas storage facility.'*

**CSL's response:**

CSL considers that these responses can be seen as broadly supportive of CSL's proposed methodology for maximising the volume of capacity it offers in SBU form, had CSL determined that it was possible to re-commence injection operations before 16 May 2017.

**(iii) *CSL's proposed allocation of technical capacity between MRC and AS based on the scenarios set out in the December 2016 Consultation Document***

Only one respondent directly addressed this question. They noted that CSL's 'Capacity Model' is relatively new and therefore it would be important that CSL provide sufficient evidence to Ofgem that the model '*has been appropriately developed; does not contain errors; and can be reproduced*'. This respondent also considered that it was important that any capacity CSL determined could be offered based on asset capabilities (after 28 February) be offered to the market via an open and transparent process rather than treated as Incremental Capacity.

**CSL's response:**

CSL provided the Capacity Model and provided training to Ofgem regarding the development of the model and the key inputs and assumptions. Further, CSL sought to provide prompt responses to Ofgem's questions regarding the Capacity Model.

In relation to offering capacity within the 2017/2018 Storage Year, as set in Sections 6, 8.1 and 8.3 of this final Application, CSL has proposed that it will offer Incremental Capacity it determines it can make available using its established sales processes (CSL uses these process for all Rough Capacity) with additional reporting regarding any sales to the rest of Centrica. CSL notes that these established processes for offering capacity to the market have been subject to considerable scrutiny by the Competition and Markets Authority in both the initial review, which set the Rough Undertakings, and the subsequent reviews of the Undertakings in 2010/2011 and in 2015/2016. This should give the market comfort that CSL's arrangements for offering capacity whether ahead of, or during, the Storage Year is objective, transparent and non-discriminatory.

**(iv) *Market Participants' appetite for buying injection and space capacity without corresponding withdrawal capacity***

Only one respondent explicitly responded to this question stating that market participant appetite for injection and space without corresponding withdrawal capacity is relatively low.

**CSL response:**

CSL considers that this response is consistent with CSL's proposals put forward in its December 2016 Consultation Document and this final Application.

**(v) *Other comments and issues raised by Market Participants***

***a. Setting the MRC on an enduring basis***

Two of the respondents commented on the need to have an enduring approach to setting Rough's MRC and AS which could be applied for longer than one year, and which would not be subject to regular / annual changes.

**CSL response:**

CSL agrees that adjusting Rough's capacity should not be undertaken annually and that changes to Rough's MRC and AS would generally be enduring. However, in relation to the 2017/2018 Storage Year, the requirements of the Undertakings combined with the uncertainties of the Well Testing Program completion date and its likely outcomes left CSL with no option other than to apply for a change for the 2017/2018 Storage Year which would likely need to be revised for the subsequent Storage Year.

CSL also notes that the frequency of applications to Ofgem to adjust the MRC and AS will be a function of the asset's physical capabilities. As the Rough facility ages, the likelihood of substantial changes in its physical capabilities increases. CSL notes that there is a threshold requirement on CSL to demonstrate that the change in physical capabilities is substantial.

***b. Risk***

Five of the six respondents made reference to the role the Rough Storage Facility plays in the wholesale gas market. As set out in the responses above, these respondents considered that setting an Obligated Capacity that is not aligned with Rough's physical capabilities has the potential to generate unnecessary volatility in the wholesale gas market.

In addition to these general concerns for the wholesale market, one respondent also commented that Ofgem should not be seeking to set an Obligated Capacity based on

maintaining the level of asset risk (associated with deliverability support) that CSL was exposed to when the Undertakings were agreed in 2003. They stated that:

*'We note CSL's comment that Ofgem indicated its expectation for CSL to continue to accept a level of risk equivalent to that existing when CSL acquired the Facility in 2002. In our view, this is an unrealistic expectation as the gas market has changed significantly over the last fifteen years; therefore, to expect CSL to take on the same level of risk is hardly justifiable.'*

**CSL's response:**

CSL acknowledges the perception of market participants regarding the role of Rough in the wholesale market.

CSL agrees that it is not acceptable that CSL be required to take on deliverability support risk based on historic circumstances and also appreciated the issues raised by one respondent regarding compensation arrangements associated with capacity sold under the Storage Service Contract. CSL considers that, while issues around compensation are not directly relevant to the final Application or any adjustment to the MRC and AS, if CSL looks to launch new storage contracts in relation to future Storage Years, it will re-examine whether the allocation of risk in the Storage Services Contract remains appropriate in light of Rough's operational integrity.

