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for energy consumers

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## **Review of the Rough Undertakings given by Centrica Storage Limited and Centrica – Ofgem response to Provisional Decision**

Ofgem welcomes the opportunity to comment on the CMA's provisional decision to vary the Rough Undertakings. This would introduce an adjustment mechanism to allow Centrica Storage (CSL) to apply for a change in their capacity sales obligations if Rough's capabilities significantly change. In this letter we set out some detailed comments on the issues highlighted in the CMA's provisional decision.

### **Change of circumstance**

The CMA has provisionally found two changes of circumstance. The first is the current need to operate Rough at a significantly reduced pressure, which has affected CSL's ability to offer the capacity it is obliged to for the 2016/17 Storage Year. The second is that as Rough ages its performance may become increasingly unpredictable, which may affect CSL's ability to offer the capacity they are required to in the future.

We generally agree that the current technical issue and reduction in Rough's capacity due to ageing of the asset could represent a change in circumstances at Rough. However, at the present time it is difficult for us to conclude with certainty that ageing will necessarily lead to deterioration in future performance.

In this regard, if ageing or other factors do result in changes to capabilities, we recognise that the current capacity obligations may not be appropriate. At this time, we have not formed a view on the extent to which the current issue would be a reason to justify changing capacity sales obligations; though we agree it would likely be an appropriate trigger to consider whether such a change should be made.

### **Alternative approaches to addressing the changes in circumstance**

The CMA has focussed on options designed to address issues that affect CSL's ability to deliver capacity in future years, while not addressing mismatches that occur within year. We agree with this approach in drawing a distinction between CSL's regulatory obligations before capacity is sold, and their commercial obligations to their customers once capacity has been sold. CSL's contractual mechanisms are designed to manage their commercial exposure to their customers once capacity has been sold. We agree that a mechanism to change undertakings obligations should only be used to address issues that affect capacity which has not yet been sold.

## **The proposed adjustment mechanism**

The CMA has proposed to vary the undertakings to introduce a mechanism to adjust the Obligated Capacity of the undertakings. This would allow CSL's capacity obligations to be varied if appropriate in response to changes in Rough's capabilities. A mechanism such as this has the advantage of providing clarity to all market participants while minimising administrative burden on regulators and CSL, as adjustments to these obligations could be made without a full review of the undertakings. As a result, we are supportive of the CMA's provisional decision to introduce such a mechanism. We comment on some of the specific details of the design of the adjustment mechanism below.

### *Decision maker*

The CMA has provisionally decided that Ofgem should act as decision maker for the adjustment mechanism. We can confirm we are content to take on this role for a mechanism that functions as set out in the provisional decision.

### *Triggering the mechanism, the evidence required and consideration of changes*

The CMA has provisionally decided that either Ofgem or CSL could trigger the mechanism. We agree with this approach, as it will help ensure confidence that the mechanism will be triggered where appropriate. We think it is important that this mechanism is only used in exceptional circumstances, where other routes are not sufficient for CSL to address an issue that has had a substantial impact on Rough's capability. We do not envisage that this mechanism would be used regularly.

The CMA has provisionally decided that the undertakings should not be amended to include a principle that CSL is only obliged to sell capacity that can be physically backed by Rough. We are supportive of this approach, as there may be circumstances (such as a minor change in capabilities) where it would be appropriate for CSL to be obliged to sell more capacity than they are able to physically back. In addition, as CSL currently sell capacity that is not always physically backed, introducing such a principle could imply that the mechanism should be triggered even if no change to Rough's capabilities has occurred.

The CMA's general principle is that the onus should be on CSL to demonstrate that a change has occurred and had a substantial impact. The CMA also thinks that CSL should be required to demonstrate that the proposed adjustment does not leave Centrica better or worse off relative to the current undertakings. We agree that the burden of proof should rest with CSL.

The CMA proposes that an independent third party should be appointed to verify CSL's assessment and proposals. We support this approach as it will provide independent assurance on the application and should allow for a faster decision making process. The CMA has also provisionally decided that additional assurance on Rough's capabilities should be provided as part of their current annual injection report. We agree that this would be a good addition to the current report.

### *Consultation and timings*

The CMA has proposed that, by default, CSL should conduct a consultation on their proposed adjustments to capacity obligations, as part of the process of using the adjustment mechanism. We agree with this approach, as third party views on the proposed adjustment and its impact will be an important input into decisions on the adjustment mechanism.

The CMA has provisionally decided that Ofgem's decision on the adjustment mechanism should not be subject to a month's time limit, as proposed by CSL. We agree with this approach, as these issues could be complex and require longer consideration. In line with

good regulatory practice, we would aim to respond to any request from CSL as soon as reasonably practicable.

*Other issues arising from the adoption of the mechanism*

The CMA has provisionally decided that the definitions of specified, obliged and incremental capacity should be adjusted. This would provide a baseline level of capacity sales, set based on Rough's historical performance before CSL made significant investments in Rough's capability. When sales are below this baseline, Centrica's access to incremental capacity would be restricted. We support this approach, as it provides an incentive on Centrica and CSL to make appropriate investments in Rough to restore capability if economic to do so.

**Monitoring and compliance**

The CMA has proposed changes to monitoring and reporting requirements to provide additional information on capacity sales. We agree that this will improve clarity of information and ease of compliance monitoring. CSL suggested that some monitoring, reporting and publication obligations could be removed. We agree with the CMA's provisional decision that these changes should not be made where they result in additional information being provided to the market beyond that which would be provided without these requirements.

CSL has also proposed changes to recognise Centrica group's centralised compliance function, which the CMA has provisionally decided to make. We think these changes are appropriate, provided sufficient safeguards are in place to protect commercially sensitive information.

**Other changes**

We are supportive of the CMA's provisional decision to amend the undertakings to update definitions and references, including changes to the definition of the gas day, references to the OFT, Centrica business units and named individuals.

We remain committed to providing ongoing advice and support to the CMA as this review process is finalised. If you have any questions about this response, please contact my colleague Thomas Farmer [REDACTED] in the first instance.

Yours sincerely

**Frances Warburton**  
**Partner, Energy Systems**