

## Centrica Storage Limited and Centrica plc – Notice of decision to review the ‘Rough’ undertakings

### Introduction and statutory duties

1. The Competition and Markets Authority (CMA) has decided to conduct a review of the undertakings given in December 2003 by Centrica Storage Limited (CSL) and Centrica plc (Centrica), and amended on 3 April 2006 and on 5 March 2012, in relation to the completed acquisition by Centrica of Dynegy Storage Limited and Dynegy Onshore Processing UK Limited (‘the ‘Rough’ undertakings’).<sup>1</sup>
2. Rough is a gas field in the North Sea used to store gas in the summer and deliver it in winter when the gas is needed to help meet higher demand. It is an important part of the UK’s gas storage infrastructure and capacity.
3. CSL and Centrica, by reason of a change of circumstances, are seeking a variation to the undertakings. The CMA’s decision follows its consultation on whether to conduct a review and consideration of the responses to that consultation.<sup>2</sup>
4. The CMA has a statutory duty to keep under review undertakings made under section 88 of the Fair Trading Act 1973 (FTA) by virtue of Schedule 24 paragraph 16 of the Enterprise Act 2002, as amended by the Enterprise and Regulatory Reform Act 2013.
5. The CMA has set out in its published guidance, *Remedies: Guidance on the CMA’s approach to the variation and termination of merger, monopoly and market undertakings and orders* (CMA11),<sup>3</sup> that in launching a review, the CMA will consider its published prioritisation principles and whether there is a realistic prospect of finding a change of circumstances (CMA11, paragraph 3.10). The guidance reinforces the point that in doing so the CMA will apply its discretion in determining whether ‘a review should take place at a particular point in time’.

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<sup>1</sup> These undertakings can be viewed at: [Centrica review of undertakings \(OFT/CC\)](#).

<sup>2</sup> See: [Centrica Storage Ltd and Centrica plc – request to vary undertakings](#).

<sup>3</sup> See: [Remedies: Guidance on the CMA’s approach to the variation and termination of merger, monopoly and market undertakings and orders](#).

6. In this case we have received evidence, supported by public consultation responses, suggesting a change of circumstance and that a review meets our prioritisation principles.

## Background

7. In December 2003, the Secretary of State accepted undertakings from Centrica and CSL under section 88<sup>4</sup> of the FTA ('the original undertakings'), to take the action necessary to remedy or prevent the adverse effects specified in the Competition Commission's (CC) report.
8. In November 2005, Centrica requested a variation of the original undertakings in order to enable a minor group restructuring of the Centrica Group. After considering advice on the proposed variation prepared by the Office of Fair Trading (OFT), the CC accepted the variation, and the new, amended, undertakings ('the amended undertakings') came into force on 3 April 2006.
9. In April 2010, Centrica submitted a request to the OFT for a review of the amended undertakings as it believed they were no longer required. After considering the advice of the OFT<sup>5</sup> and reviewing the amended undertakings, the CC published a report proposing variations to the amended undertakings on 20 April 2011.<sup>6</sup> Centrica and CSL gave revised undertakings which came into effect from 5 March 2012.
10. Currently, the main provisions of the undertakings are that CSL will be maintained legally, financially and physically separate from all other businesses of Centrica and that CSL must:
  - (a) offer all Rough capacity for sale on a non-discriminatory basis;
  - (b) unless otherwise agreed with Ofgem, retain the Storage Service Contract for all sales of Rough capacity;
  - (c) unless otherwise agreed with Ofgem, sell Minimum Rough Capacity (MRC) in Standard Bundled Units (SBUs) comprising combined rights to fixed units of space, injection and withdrawal;
  - (d) sell the following 'obliged capacity' before the start of the Storage Year (May):

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<sup>4</sup> Section 88 of [the FTA](#).

<sup>5</sup> See: [Centrica review of undertakings \(OFT/CC\)](#).

<sup>6</sup> See the [Competition Commission's final report](#) (April 2011).

- (i) 455 m SBUs of MRC; and
  - (ii) at least 1.5 TWh of 'Additional Space';
- (e) not sell more to Centrica per year than a maximum 'specified capacity' of:
- (i) 25% of MRC; and
  - (ii) 1.5 TWh of Additional Space;
- (f) offer at least 20% of MRC (equivalent to 91 m SBUs) on annual contracts;
- (g) auction all unsold obliged capacity one month before start of the next Storage Year;
- (h) offer for sale capacity that becomes available during the Storage Year;
- (i) facilitate the efficient operation and development of a secondary market in Rough capacity;
- (j) disclose information on storage operations to all market participants simultaneously;
- (k) ensure that no commercially sensitive information arising from the operation of Rough is passed directly or indirectly to any business of either Centrica or any other member of the Centrica Group; and
- (l) provide sales and operational information to Ofgem and the CMA for compliance monitoring purposes.

## **The request to vary the undertakings**

11. In March 2015, following technical reports, CSL announced a decision to limit the maximum operating pressure in Rough. CSL is conducting further tests, but it considers that there is a risk it will be physically unable to meet the capacity sales requirements as set out in the undertakings for the 2016/17 Storage Year.<sup>7</sup>
12. CSL further submits that, as an ageing asset, the Rough storage facility's performance can be expected to become less predictable, increasing the

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<sup>7</sup> CSL therefore separately requested an indication of the CMA's approach to prioritisation of enforcement action if CSL were to undertake the compliance steps it identified for 2016/17. See: letter dated 18 September 2015: '[Indication of the CMA's prioritisation principles in relation to the Undertakings](#)'. The CMA published a response to this request, indicating that, provided the assumed facts set out in CSL's letter of 18 September 2015 were to continue to apply and the proposed actions set out in the letter were undertaken by CSL, CMA officials anticipate they would not recommend prioritising the taking of enforcement action. See: letter dated 22 September, '[Request for an indication of enforcement prioritisation](#)'.

potential for CSL to be physically unable to meet the undertaking's capacity sales requirements in future years. In its letter to the CMA of 18 September 2015, CSL provided further explanation of the changes to Rough's capacity.<sup>8</sup>

13. By reason of a change of circumstances, CSL is seeking a variation of the undertakings and it has also provided proposed changes to their wording.

## Consultation on whether to review

14. As set out in [CMA11](#), we sought views on whether the CMA should carry out a review in the light of the issues raised by the parties and CMA's [prioritisation principles](#). In particular we sought views on:
  - (a) whether the limit on the maximum operating pressure in Rough represents a change in circumstances in this market, such that the CMA should consider a review of these undertakings;
  - (b) whether we should prioritise this case for review; and
  - (c) whether this review should be carried out now.
15. The consultation commenced on 22 September 2015 and closed on 12 October 2015. We received responses from nine parties,<sup>9</sup> one of which acknowledged the invitation to comment but stated that it had no comments on the matter.
16. In response to the first question, of the remaining eight parties, seven considered that there was at least an indication that there had been a change in circumstances, such that a review was warranted. The other party did not address this question specifically.
17. In response to the second question, all eight parties considered that the CMA should prioritise undertaking a review.
18. In response to the third question, seven parties considered that the CMA should conduct a review now, with the remaining party making no specific comment on when the review should commence.
19. Some parties commented on the rationale and timing for a review. The points they made included the following:

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<sup>8</sup> Letter dated 18 September 2015: '[Application to the CMA for a variation to the Undertakings](#)'.

<sup>9</sup> Centrica Group (excluding CSL), CSL, Department of Energy & Climate Change, EDF Energy, Ofgem, Oil and Gas Authority, National Grid, Petronas Energy Trading Ltd, and SSE Hornsea Ltd.

- The CC in its 2011 review had determined that Rough continued to have market power in Great Britain's wholesale gas market and it follows that any significant reduction in Rough's physical capabilities constitutes a change in circumstances in the market.
  - The CMA should conduct the review as soon as possible, to ensure market certainty ahead of winter 2016 and beyond. The review should not, for example, wait for the results of CSL's current testing programme.
  - Commencing the review now maximises the possibility that the CMA Group can complete and implement the review before any potential breach of the undertakings crystallises.
  - Carrying out a review of the undertakings now (during a period when Rough's capabilities have been reduced) increases the likelihood of market participant engagement and participation.
20. Some parties also commented on the potential focus and issues a review might address. Their comments included that:
- any variation to the undertakings should ensure the primary and secondary markets remain competitive and not allow the Centrica Group to acquire proportionately more capacity than it is currently allowed to;
  - any changes should aim to maintain a level of restriction for Centrica equivalent to that currently in place, unless there is evidence to change this level;
  - the current limit on capacity is not necessarily an enduring one and uncertainty over the future changes in capability should be taken into account in any review;
  - any review of the undertakings should take into account the incentives to maintain and invest in Rough; and
  - any review should consider the implications for the gas transmission system and wholesale gas market.

## **Decision**

21. The responses to the consultation and our own assessment of the evidence presented to us, provide grounds for the CMA to consider there is a realistic prospect of finding a specific change of circumstances relating to the capacity

elements of the Rough undertakings.<sup>10</sup> However, we note that we have not received evidence of a wider change of circumstances – for instance in relation to competitive conditions in the wholesale gas market.

22. We have also considered the parties' request for a review in light of the CMA's [prioritisation principles](#). With regard to impact and strategic significance, Rough is the only long-term storage facility on the national transmission system and a strategically important asset.<sup>11</sup> The energy market is an area of strategic focus for the CMA. The risk that CSL will be physically unable to meet the capacity sales requirements in the undertakings for the 2016/17 Storage Year is also grounds for a review to be conducted now. The CMA concludes that these factors justify prioritising the resources for a review.
23. On the basis of the evidence available to us, our consideration of responses to our consultation and of the CMA's prioritisation principles, the CMA has therefore decided to conduct a review of the Rough undertakings. Given the respective roles of the CMA and Ofgem, as sectoral regulator, this review provides an opportunity to consider the monitoring and enforcement aspects of the undertakings.
24. As well as publishing this decision, the CMA will be informing relevant parties directly of this decision to commence a review.
25. The review of the undertakings will be undertaken by a group of CMA panel members, appointed by the CMA panel chair. The group of panel members will be advised by a case team of CMA staff. The CMA will also, as appropriate, seek the advice of Ofgem, the sector regulator of gas and electricity markets in the UK.
26. Further information on the process for conducting a review of an existing remedy is outlined in CMA11<sup>12</sup> and further information on the conduct of this review will be published on the [case page](#), which will be kept updated.

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<sup>10</sup> See [CMA11](#), paragraph 3.10, which identifies a relevant factor in whether the CMA prioritises opening a review is whether the CMA considers there is a 'realistic prospect of finding a change of circumstances'. This judgement is relevant to the prioritisation decision, the decision on whether there has in fact been a relevant change of circumstance is for the CMA group appointed to conduct the review.

<sup>11</sup> CSL reported turnover for 2014 of £149 million, with an operating profit of £29 million. See the [CSL website: Financial performance](#).

<sup>12</sup> [CMA11](#).