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Dear Rochelle

Centrica's completed acquisition of Dynegy Storage Limited and Dynegy Onshore Processing UK Limited

Thank you for the opportunity to respond to the above consultation. We believe that the issue of gas storage is critically important for the UK as we move to an era of import dependency and a growing deficit of sufficient swing production to meet UK peak day requirements. BP hopes that the consultation will present an opportunity for the Industry to address the specifics of the acquisition and also to engage in a wider debate on storage and flexibility services.

In view of the nature of Centrica's business interests in the UK we believe that this proposal raises a number of important issues of concern. The scope of Centrica's activities, particularly its gas supply position, means that the proposal must be considered holistically and not viewed as an isolated acquisition of storage assets. For example, an issue for Ofgem needs to be the potential impact of this acquisition on the competitiveness of the domestic gas supply market. We are reassured that Ofgem has recognised the conflict between Centrica's ownership of Rough and Morecambe gas field and the potential impact which this might have on the provision of flexibility services to the wider market. We look forward to your analysis of the injectability of Rough and the ability to swing down at the beach.

BP is confident that Centrica has the commercial and technical expertise to manage the Rough facilities in a safe and proficient manner but believe that there are potential conflicts with their other business activities. All existing and prospective users of Rough require assurance that they will continue to have access to storage on a fair and non-discriminatory basis and that there will be full legal and operational separation of the new entity.

<u>Rough Storage</u>

Rough is, and will remain, the provider of the majority of the UK's seasonal storage capacity. Whilst we are starting to see a number of new storage products and services being developed none of these is sufficiently material to challenge the key position enjoyed by Rough.

It is doubtful that the Rough facilities will face competition from any new UK seasonal storage sites for some time. One major reason for this is the cost of developing new facilities. It is estimated[1] that the capital costs incurred at Rough have been in the order of ~ £750 million plus the very significant additional costs of “cushion gas”. It is unlikely therefore that many players would currently undertake such an investment, to convert depleted fields, on the basis of a perception of future and seasonal spot price variations.

In view of the pivotal position that Centrica will enjoy it is imperative that the acquisition of this asset in no way dilutes the level of protection currently offered to users. Indeed there are strong arguments to support the view that the Undertakings currently in place with Dynegy should be reviewed, strengthened and extended.

In the event that Centrica is unable to agree to specific undertakings to protect users then we believe that the matter should be referred to the Competition Commission.

We are very concerned to note that Centrica proposes to reserve, for its own use, between 25 and 30 % of total Rough capacity[2]. We do not believe that any user should enjoy *any* preferential access to these storage services. On the contrary, we believe that any user should be required to participate, along with others, in transparent and non-discriminatory auctions as the primary method of capacity release and that the rules for those auctions should only be modified with the agreement of Ofgem and after discussion with service users.

However, we do not believe that Centrica should be constrained from developing a wider range of storage products and services to meet the future needs of their storage customers. BP would welcome the opportunity to discuss the development of new services and to understand what plans Centrica might have to develop the capability of Rough to further improve rates of injectability and deliverability.

We are pleased to note that Ofgem has identified the need to conduct a general review of the competitiveness of the gas storage market, and its ongoing regulation, during 2003. The existing undertakings expire at the end of the storage year beginning on 1 May 2003 and, as we have indicated, we do not believe that the storage market will have developed sufficiently in a competitive manner to obviate the need for further undertakings to be established beyond that date. It is vital therefore that Ofgem initiates the storage review <u>early</u> in 2003 in order to lessen any uncertainty for users beyond the end of April 2004.

Over recent months there has been lengthy debate within the Industry about **‘title to gas in store’**. Whilst the issue remains unresolved; we believe that Centrica is sympathetic to the concerns of users and would therefore be keen to seek a speedy and mutually satisfactory resolution to the matter.

As Ofgem will be aware, the concern arises from the fact that under the standard storage contract, which all storage users have to sign, the operator of the facility is given title to the gas while it is in storage. They are then obliged to return that gas in accordance with the user’s nominations. The concern has been that in the event that the storage operator encounters financial difficulties then a liquidator or administrator appointed could exercise its rights to ignore the contractual obligation to return the gas and may sell the gas to third parties.

We would like to see a commitment from Centrica that all future storage contracts will be restructured so that their customers take title to their gas while it is in storage.

<u>Information.</u>

The scope of Centrica’s commercial activities re-inforces our view that it is essential that there is full operational separation of both its Storage and Onshore processing businesses from the rest of its businesses.

This is to provide assurance to users of those services that none of Centrica’s other entities will have access to commercially sensitive information and will not then be in a position to exploit or abuse a privileged and advantaged position.

Whilst we recognise that Centrica will be subject to general Competition Law in their activities, we would like some specific response from Ofgem as to how they intend to monitor Centrica’s behaviour on an ongoing basis in this regard.

[1] Wood MacKenzie data
[2] Appendix 1Centrica’s views. Ofgem consultation. December 2002

We hope you have found our response to be of assistance in this matter and would be pleased to discuss the issues further.

Yours sincerely

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