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Office of Gas and Electricity Markets  
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10 December 2002

Dear Rochelle,

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

Thank you for the opportunity to comment on the above acquisition. Statoil (UK) Limited (STUK) is responsible for the marketing of potential supplies of its parent company's Norwegian equity gas and the Norwegian State's equity gas in the UK market. Due to its size, proximity to Norway and its prospective gas supply shortfall in the next few years, the UK market is of great interest to us. Therefore STUK would like to make the following comments.

STUK agree that this acquisition is significant to the gas industry in the UK and the role that storage plays in that industry will be affected by this transaction. Storage is of key strategic importance in the UK in managing the potential shortfall of supplies. In this respect the fact that the Rough facility represents 85% of storage in the UK should ensure that, whoever the owner is, the appropriate regulatory safeguards are put in place to ensure that it is managed in a way that will promote competition.

It is STUK's opinion that there is unlikely to be a great deal of competition with Rough from other storage facilities. In fact the position of storage in the UK has changed little since the last review of storage by Ofgas in 1998 while current new storage facilities are small and do not perform the same functions as Rough; any new storage facilities are unlikely to be ready for some time to come. As such, while STUK do not object in principle to the purchase of Rough by Centrica, it would be appropriate that statutory undertakings are put in place in lieu of a referral to the Competition Commission and that these undertakings should be in place beyond the deadline for previous undertakings of 2004 and should be subject to a wider review of storage by Ofgem in 2003 which STUK would welcome.

The following sections below detail the main points of concern for STUK in the above acquisition.



## Position of Rough in UK storage market

STUK perceive that Rough has a unique position in the UK as a “long duration” storage facility, which was designed and built as an integral part of the supply demand match in the UK. As such is assumed that in order to achieve such a match this storage site would provide support in periods of sustained high demand.

Furthermore the main sources of competition for Rough storage do not provide the same service and it is significantly distinct from other forms of flexibility that ownership of a significant proportion of the facility should cause competition concerns. Rough provides a long duration service of up to 67 days withdrawal when the site is full. No other storage facility in the UK has similar capabilities as this. It provides a seasonal storage service, which enables users to physically manage their exposure to demand swings and gas prices across the year between winter and summer. Again although other sites can provide seasonal storage they tend to cycle more frequently and benefit from different usage patterns to Rough and are considerably smaller. As highlighted in the consultation document Rough makes up 85% of the storage market and STUK do not think that there will be any sites of significant size to challenge the dominance of this facility.

It would therefore seem suitable to ensure that any owner of this facility has appropriate statutory regulation, controls and monitoring in place until effective competition exists in UK long-term storage.

## Current Statutory Undertakings

The nature of the undertakings placed upon Dynegy Storage Limited in lieu of a referral to the Competition Commission covered the period up to 30 April 2004 placed certain restrictions on the operation of the site, as set out in the consultation document. STUK do not believe that these undertakings would be sufficient to ensure effective competition in the storage market.

Centrica are a significant player in many areas of the market, both in wholesale trading through Accord and BGT and in the supply market at both domestic and Industrial and Commercial level. Furthermore they have upstream resources including deliveries through the Barrow terminal, which provide substantial levels of swing. If they were to control 85% of the storage market under the terms suggested in the appendix of the consultation document there would be a perception that opportunities may exist to use this dominant position to influence the market, whether this is actually the case or not. STUK agree with Ofgem that the perception of dominance can deter competition in a market as much as actual conduct of market participants.

It is better, therefore, that preventative measures are in place to provide sufficient safeguards to competition and ensure market participants are comfortable with the rules governing access to storage and protecting those rights already held in storage.

As a basic opening provision STUK assert that the statutory undertaking that were in place for Dynegy should be transferred to Centrica storage. However given the different position, which Centrica holds in the market and the specific nature of the Rough facility further amendments should be made.



## Protection of Users and Operational information

As previously highlighted Rough occupies a particular role in the UK gas industry. Information about the activity of this asset and the requirements of those who use it is extremely sensitive information of a commercially important nature. As such it is essential that the Storage business should be legally, robustly and physically separated from any trading activity within the Centrica group. This would ensure that other companies using Rough storage and trading with Centrica companies need not be concerned about the information advantages which their counterparty may hold and protect their commercial positions with regard to the price at which storage is purchased and the nominations of gas from day to day.

## Continuation of controls after 2004

Competition in the storage sector has been very slow in starting and to date the number of new entrants in the storage market has been low, and of small volumes. Further additions are expected but again these sites will be small and of a significantly different nature to Rough. STUK are concerned that there is still limited competition for the services that Rough supplies and that there is little prospect of further competition in the future.

It must, therefore be concluded that any for of undertakings that are required of Centrica Storage should extend substantially beyond the end of the current period (April 2004), possibly subject to the review of the storage market which Ofgem have agreed to undertake in 2003.

## Centrica's access to Rough Storage

Centrica have confirmed that they currently contract for approximately 25% of the storage sold in Rough. Naturally these contracts should be honoured and under a fully separated company this would not be an issue, as any Centrica company would access storage on the same grounds as other users.

However, should Centrica wish to contract further for storage or when they renew their existing requirements, they should also be made to purchase it under the same standard terms as other participants through a standard storage contract. Centrica should be required to offer 100% of maximum physical capacity and compete on equal terms with all other parties interested in purchasing storage products.

## Maximum Physical Capacity

The definition of the maximum space in Rough has remained the same as that defined in the review of storage was undertaken in 1998. STUK think it is appropriate that Ofgem reassess the level of space available based on any changes to the usage pattern of the facility over the period of time since the last review was conducted to establish if this maximum capacity is still a valid figure or if it should be changed.

In conclusion STUK do not object to the purchase of Rough Storage facility by Centrica in principle, however, we feel that suitable undertakings as mentioned above should be put in place to ensure that competition in both storage and other markets is in no way affected by the transaction.



STUK trust that our comments will be given due consideration and should you wish to discuss any aspect of this response further please contact me on the above number.

Yours sincerely

Robert Cross  
Regulatory Affairs Manager



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