

**OFGEM DECISION LETTER No. 0580**  
"Responsibilities following the Appointment of a Supplier of Last Resort"  
Version 1.0

To:

Transco, Shippers & other interested parties

Direct Dial: 020 7901 7052  
28 January 2003  
Your Ref:  
Our Ref: IO/JR/2401

Dear Colleague,

**Re: Modification Proposal 0580 'Responsibilities following the Appointment of a Supplier of Last Resort'**

Ofgem has considered the issues raised in modification proposal 0580 "Responsibilities following the Appointment of a Supplier of Last Resort" and has decided to direct Transco to implement the modification. Ofgem believes that the modification will better facilitate the relevant objectives of Transco's Network Code (NWC). This letter explains the background to the modification proposal and gives Ofgem's reasons for making its decision.

**Background to the proposal**

Under current NWC rules, the shipper of a Supplier of Last Resort (SoLR) appointed by Ofgem does not assume financial responsibility for energy balancing and transportation charges until the supply points become registered to it on Transco's Site and Meters database. Because of the constraints of Transco's UK Link system, in the case of the failure of a large supplier the time taken to transfer the portfolio using existing Supply Point Administration processes could be considerable. Until transfer of all supply points has been completed, Transco would be exposed to any non-paid transportation charges and the shipping community would be exposed to any non-paid energy balancing charges.

Although under current NWC rules the SoLR's shipper would not be financially responsible for transportation and energy balancing until supply point registration had taken place, the SoLR would be entitled to bill the customers of the failed supplier on deemed contract terms from the date of SoLR appointment. Transco and shippers have concluded in industry meetings that it is therefore appropriate for the SoLR's shipper to assume responsibility for transportation and energy balancing charges from the date of SoLR appointment as opposed to the date of supply point transfer.

On 11 November 2001 BGT raised modification proposal 0503 'Network Code Implications of the Appointment of a SoLR'. The modification established the NWC SoLR Review Group to consider the consequences of the appointment of a SoLR under existing NWC rules, including the issue of financial responsibility.

On 15 January 2002 Transco submitted modification proposal 0524 'Shipper Responsibilities in the Event of the Appointment of a Supplier of Last Resort'. This modification addressed the issue of financial responsibility, and stated that until supply point transfer had taken place, Transco would act as agent for the terminated shipper's account on behalf of the SoLR's shipper. On 6 June 2002, Ofgem rejected modification 0524 on the grounds that Transco and shippers had not fully investigated all of the options for dealing with the appointment of a SoLR.

Transco proposed modification 0580 on 23 August 2002. The modification addresses similar issues to modification 0524, but presents a different solution for dealing with the existing problems.

### **The Modification Proposal**

Modification 0580 proposes that responsibility for energy balancing and transportation should transfer to the shipper of the SoLR with effect from the date of SoLR appointment. From this date, the shipper would incur energy balancing and transportation charges for the failed supplier's portfolio.

The modification proposes that in order to manage energy balancing actions between the date of the appointment of a SoLR and the completion of the portfolio transfer, the failed shipper's account would be made available to the new shipper. This solution would permit one new shipper to manage the portfolio of the failed shipper until all supply point registrations had been completed.

The modification also proposes that Transco will undertake a review of the energy balancing and transportation credit arrangements of the new shipper in light of its increased portfolio, and will advise of any new credit arrangements that would need to be put in place. The new shipper would be given 14 days to put new arrangements in place.

### **Respondents' Views**

Representations were received from six shippers. Respondents were generally supportive of the modification, but raised a number of concerns. These are set out and addressed below.

#### **1. Modification does not support the appointment of more than one SoLR**

The principle concern of shippers was that the modification proposal does not make arrangements to support the scenario of more than one shipper taking responsibility for the supply points of the failed supplier. (Ofgem understands, however, that this only applies to supply points registered on the Sites and Meters database; the modification proposal would support the appointment of separate SoLRs for any supply points registered to the failed shipper on the Unique Sites Database.) In its Final Modification Report Transco outlines the reasons why the proposed solution would not support more than one shipper taking responsibility for the supply points of the failed supplier.

In the event of the failure of a gas supplier, Ofgem has powers to appoint more than one SoLR to the customers of the failed supplier. Given the constraints of this modification proposal, in the event of future supplier failures, Ofgem would need to carefully consider the impact of the appointment of more than one SoLR. However, in some circumstances it may not be realistic to appoint a single SoLR to take responsibility for all affected supply points. Ofgem would not want

a SoLR appointment to create operational or financial problems for the SoLR or its shipper, and so, in certain circumstances, the appointment of multiple SoLRs may be necessary.

Shippers generally supported implementation of the modification as they felt that it was a preferable option when compared to existing NWC arrangements. Ofgem shares this view, but considers it vital that Transco and shippers work to develop suitable arrangements to ensure that processes are in place to deal with more than one shipper taking responsibility for the portfolio. During meetings of the 'Expert Group' that supported Ofgem's SoLR Test Exercise, the industry stated that it believed further work was needed to enhance post-SoLR appointment processes, and established an informal group to consider issues. Ofgem believes that Transco and the industry should use this group and the Transco NWC SoLR Review Group established by modification proposal 0503 to further consider and develop suitable arrangements.

2. Modification does not cover the scenario of a shipper failure where the supplier does not fail, or the scenario of a supplier failure where the shipper does not fail

Shippers raised concerns that the modification proposal would only work where both a supplier and its shipper(s) failed simultaneously.

In the event of a shipper-only failure, Transco has the option to call upon the undertakings given by the solvent supplier(s) under standard condition 22B of the gas supply licence. This would cover transportation and energy balancing charges and would incentivise the supplier(s) to quickly make new shipping arrangements. There is no provision for Ofgem to appoint a 'shipper of last resort'.

In the event that a supplier, but not its shipper, fails, Ofgem has the power to appoint one or more SoLRs to the failed supplier's customers and to issue a direction to the shipper under standard condition 12 of its shipping licence. This condition requires the shipping licensee to either facilitate the commencement of supply by the SoLR to the supply points, or facilitate the making of arrangements by the SoLR's shipper for the conveyance of gas to the supply points.

Given these provisions, Ofgem believes that appropriate arrangements are in place to cover the scenarios highlighted by respondents.

3. Use of bulk transfer mechanism

A shipper stated that in recent weeks Transco has effected a bulk transfer of supply points from separate shipper accounts to a single shipper account, and queried whether this functionality could be utilised in a SoLR situation.

Transco has already developed a bulk transfer mechanism, although Ofgem understands that only a small number of shippers have developed systems that would allow them to use it. In any event, the bulk transfer mechanism is still constrained by the system traffic constraints of the UK Link system. Ofgem urges suppliers to consider the usefulness of the bulk transfer mechanism and to work with shippers to ensure that they can take advantage of the mechanism if appropriate. Where suppliers feel that the current functionality of the bulk transfer mechanism is deficient, suppliers, shippers and Transco should consider what improvements could be made.

4. Information to be provided by Transco to the incoming shipper

A shipper queried the information about the failed supplier's shipper's account that would be made available to the SoLR's shipper. The shipper asked whether it would broadly equate to the information provided by Ofgem as part of the SoLR test exercise that took place in September 2002.

In the event that Ofgem needs to select and appoint a SoLR(s), high-level aggregate information about the failed supplier's portfolio and consumption would be provided to potential SoLRs in order for them to make a decision about whether to volunteer for the role of SoLR.

Upon selecting and appointing a SoLR(s), Ofgem would provide all of the information it had about the failed supplier's portfolio to the relevant SoLR(s), including individual customer information where this has been obtained by Ofgem from the failed supplier.

This information is separate from the information that would be made available to the SoLR's shipper once Transco had assigned new security IDs under the process detailed in the modification. This information is defined in the legal text accompanying the modification as 'relevant information (including, but not limited to, Protected Information) relating to the Terminated Supply Meter Points to which the Discontinuing User would have had access through UK Link immediately prior to the User Discontinuation date'.

5. Timescales for putting new credit into place

A shipper stated a concern at the length of time afforded to the SoLR's shipper to make arrangements to put into place any necessary increased transportation and energy balancing credit cover. The shipper said that 14 working days could mean that 17 calendar days elapsed before the situation was resolved.

Ofgem believes that the proposal as drafted is sufficient. When selecting one or more SoLRs, Ofgem would ask potential SoLRs about their shippers' abilities to meet additional credit requirements, and would not want to appoint a SoLR whose shipper would be unable to cope with the increased portfolio. The SoLR's shipper must put in place the requisite security as soon as reasonably practicable but in any event no later than 14 days after notification by Transco of additional security. A SoLR and its shipper would face many challenges, and Ofgem believes that any requirement to make new arrangements within a timescale shorter than 14 days would be unrealistic. The timescales proposed in the modification are in line with the equivalent requirements in the electricity Balancing and Settlement Code.

6. Process must ensure that the new User does not pick up outstanding debts

The modification states that the SoLR's shipper would be responsible for energy balancing and transportation charges for the portfolio of the failed supplier with effect from the date of appointment.

Shippers have identified concerns that it is not entirely clear how this process would work in practice. Transco and shippers must clarify the exact procedures to be adopted, and should use the industry post-SoLR appointment forum, the NWC SoLR Review Group and existing Transco work groups for this purpose.

7. Workability of the procedure

A shipper queried the workability of the proposed procedure, citing implications for file transfers, transfer of invoicing files and energy balancing payments/smearing as some of a number of uncertainties. In its Final Modification Report Transco reiterates that the aim of the proposal is to minimise community risk by establishing an accountable User for the portfolio. The modification provides the accountable User with an opportunity to balance the portfolio until supply point transfers are completed. Transco states that the issues highlighted by the shipper respondent should be raised in the appropriate fora, i.e. Supply Point and Billing Workstream, Billing Operational Forum or at the Energy Balancing Credit Committee. It is for Transco and shippers to discuss the issues in the above fora.

#### 8. Acceptance of shipper of SoLR

A shipper stated that it had concerns about confirmation of the SoLR's shipper to accept the SoLR's additional portfolio of supply points.

When selecting a SoLR(s), Ofgem's information request to potential SoLRs would ask each supplier to give details about the arrangements it had to enable it to ship gas to the customers of the failed supplier. The information request would also ask for information about how the gas would be sourced to supply the additional customers, and how the shipper would meet additional credit cover obligations. Ofgem would use this, and other information collected via the information requests, to select the most appropriate SoLR(s). Ofgem considers it a reasonable assumption that potential SoLRs and their shippers would discuss these issues prior to returning information request responses to Ofgem.

Copies of the draft SoLR information requests will be sent to suppliers on Ofgem's SoLR register at the end of January 2003 for comments, and can be obtained from Ofgem's Supplier/Shipper Failure team by other interested parties.

#### 9. Consent to release of information

A shipper stated a concern that the consent to release information on the failed supplier's shipper's portfolio cannot be assumed, and that it is in need of clarification. Ofgem believes that this is clarified in section 2.1.11 of the legal text accompanying the modification proposal, but would urge Transco and shippers to carefully look at any concerns they may have.

#### **Ofgem's view**

Ofgem agrees with the majority of shipper respondents that the modification will put into place arrangements for dealing with supplier failure that are more robust than the current arrangements under NWC. The modification gives the SoLR's shipper more control over the portfolio until all supply point transfers have taken place, and reduces the potential exposure to the rest of the shipping community.

Whilst the modification will introduce more robust arrangements than current NWC arrangements, the modification does not support the appointment of more than one shipper to take responsibility for the supply points of a failed shipper. In some circumstances, the appointment of multiple SoLRs and thus, potentially, multiple shippers may be necessary, and so it is vital that Transco and the industry work to develop arrangements to deal with this scenario. Ofgem also agrees with shippers that further clarification of operational procedures is required, and would urge shippers, potential SoLRs and Transco to use the industry post-SoLR

appointment forum, the NWC SoLR Review Group and other relevant Transco work groups for this purpose.

Ofgem believes that the modification proposal will better facilitate Transco's relevant objectives. In particular, Ofgem believes that the objective of securing effective competition between relevant shippers and relevant suppliers will be better facilitated as the risk to the shipping community from being exposed to excessive smearing charges will be mitigated. Supply and shipping industry participants will be more comfortable entering and participating in a market where such risks are mitigated.

### **Ofgem's Decision**

Taking into account the issues above, Ofgem has decided to direct Transco to implement modification proposal 0580. I hope that this letter clarifies the reasons for this decision.

Should you require any further information on this decision, please contact Fran Gillon (020 7901 7283) or James Richardson (020 7901 7027).

Yours sincerely,

**Iain Osborne**  
**Director, Supply**