

## **Supplier of Last Resort Test Exercise**

**A report into the lessons learned from testing  
procedures leading up to the appointment of a  
Supplier of Last Resort**

17 January 2003

## Summary

In the event of the insolvency of a gas and/or electricity supply licensee Ofgem has special powers to appoint one or more SoLRs to take over supply to the customers of the insolvent company. In December 2000, Ofgem initiated the 'Supplier/Shipper Failure' project. The project has considered many aspects of supplier and shipper failure, including a review and enhancement of Ofgem's procedures for dealing with such failures. Earlier this year Ofgem decided that it would be beneficial to carry out an exercise involving the industry in order to test part of these procedures.

This document reports on the planning, conduct and lessons learned from Ofgem's Supplier of Last Resort (SoLR) Test Exercise that was carried out from 23 – 25 September 2002. The exercise involved participants representing gas and electricity supply companies, electricity distribution companies, Transco, Elexon and an insolvency practitioner. The purpose of the exercise was to test Ofgem's procedures for the selection and appointment of a SoLR and the industry's procedures for responding to them.

Following the exercise, a number of lessons learned were identified by Ofgem and the Expert Group. These concerned information about the failed supplier's portfolio, the format and clarity of potential SoLR information requests, the timescales for potential SoLRs to respond to information requests, and Ofgem's policy on the use of the levy on gas transporters and electricity distributors. These are discussed in detail in chapter 3 of this document.

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# 1. Introduction

- 1.1. This section explains why Ofgem decided to conduct an exercise to test its procedures for dealing with a supplier failure.

## ***Background***

- 1.2. Ofgem's principal objective is to protect the interests of consumers, wherever appropriate by promoting effective competition. From time to time, companies in competitive markets fail. On one hand, failure is regrettable, in that investors lose money, jobs are lost and inconvenience is caused to customers. On the other hand, failure can be a sign that competition is working effectively, and is a key mechanism for limiting inefficiency. This logic applies as much to the gas and electricity supply markets as it does to other markets.
- 1.3. In the event of a supplier failure, Ofgem's priority is to ensure that all customers continue to receive supplies of gas and/or electricity. Ofgem sees trade sales as generally more in consumers' interests than regulatory intervention. However in certain circumstances Ofgem can revoke a supplier's licence and direct another supplier (the Supplier of Last Resort (SoLR)) to take over responsibility for supplying customers.
- 1.4. Since the GB gas and electricity supply markets were opened up to competition a number of supply businesses have failed including Independent Energy and Enron. More recently, TXU's supply business was sold rapidly when funding expected from its parent company did not materialise. In all these cases a trade sale occurred and Ofgem did not have to appoint a SoLR.

## ***Context***

- 1.5. Following the failure of Independent Energy in September 2000, Ofgem initiated the Supplier/Shipper Failure Project. The project has considered many aspects of the failure of a gas or electricity supplier or gas shipper. In addition to developing robust internal procedures, Ofgem published a Guidance Document<sup>1</sup>

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<sup>1</sup> March 2001 'Supplier of Last Resort: Guidance on current arrangements'

in March 2001 that explained Ofgem's powers and policies for dealing with supplier and shipper failures, including how a SoLR would be selected.

## ***Rationale***

1.6. The Guidance Document explains the circumstances in which Ofgem would be likely to revoke a failing supplier's licence and appoint a SoLR. However because all the failures to date have resulted in trade sales, the process for selecting a SoLR has never been put into practice. Ofgem therefore decided that it should carry out an exercise involving industry participants to test the SoLR selection procedures to ensure that:

- ◆ both Ofgem and industry participants know what to do during the SoLR selection process;
- ◆ Ofgem and industry procedures are robust; and
- ◆ the timescales anticipated in the Guidance Document were feasible.

1.7. Ofgem established an industry Expert Group to assist with the planning, design and conduct of the exercise. The terms of reference for the group are attached at Appendix 1. The test was conducted between 23 and 25 September 2002.

1.8. This report describes the planning and conduct of the exercise, and the lessons learned from it. Where appropriate, these will be incorporated into Ofgem's internal procedures for dealing with supplier and/or shipper failures. Ofgem will also revise and re-issue its Guidance Document in early 2003.

## ***Structure of this document***

1.9. The remainder of this document is structured in the following way:

- ◆ Chapter 2 explains how the exercise was planned, designed and carried out;

- ◆ Chapter 3 outlines the lessons that were learnt as a result of the exercise;
- ◆ Chapter 4 highlights some of the issues concerning the challenges facing a SoLR after appointment that were not considered as part of the exercise;
- ◆ Appendix 1 sets out the terms of reference of the Expert Group;
- ◆ Appendix 2 explains Ofgem's decision not to extend the scope of the exercise to include testing what happens after a SoLR is appointed; and
- ◆ Appendix 3 sets out the exercise outline.

1.10. Although this document is not a consultation document, Ofgem welcomes views on any aspects of it. Comments should be sent to:

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It is open to respondents to mark all or part of their response as confidential. However, we would prefer as far as possible that responses are made available in the Ofgem library, and on our website ([www.ofgem.gov.uk](http://www.ofgem.gov.uk)).

## 2. The Exercise

- 2.1. This section outlines the procedure for selecting a SoLR and explains briefly how the exercise was planned, designed and carried out.

### *Ofgem's procedure*

- 2.2. Full details of the procedures that Ofgem follows in the event of a supplier failure can be found in the Guidance Document (a revised version, building on the lessons learned from this exercise will be published in early 2003). The process is as follows:
- ◆ the first stage is to obtain portfolio information. This comprises high-level summary information from Transco, Elexon and distribution companies and, if possible, detailed customer information from the failing supplier;
  - ◆ the second stage is get information from potential SoLRs about:
    - whether the supplier wants to volunteer to be a SoLR<sup>2</sup> and which customer groups it could supply;
    - the circumstances in which the supplier might want to claim for some of the cost of being a SoLR by asking Ofgem to agree a levy on Transco and distribution companies<sup>3</sup>;
    - its ability to obtain gas and/or electricity for the additional customers while still maintaining supplies to its existing customers;
    - its arrangements for complying with various credit cover obligations;

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<sup>2</sup> A supplier may be directed to be a SoLR even if it does not volunteer to be one

<sup>3</sup> Gas / electricity supply SLC 29A. In principle, Ofgem would prefer any SoLR not to make a claim on the levy, and in smaller scale failures this might be appropriate. In large scale failures there are perceived risks of managing the purchase of electricity and/or gas in the short term, and concerns over costs in terms of registration transfer in the medium term. Ofgem documents 'Supplier of last resort: Guidance on current arrangements' published in March 2001 and 'Supplier of last resort: Security cover and levies' published in June 2001 explain the issues in more detail

- how it would deal with customers, including dealing with enquiries, transferring them to its own systems and getting meter readings;
  - the price it would charge different groups of customers<sup>4</sup> and details of any notice period before the customer could switch to another supplier;
- ◆ in the exercise suppliers were given 6 hours to provide the information to Ofgem;
  - ◆ an Ofgem Panel assesses the responses and seeks clarification as necessary; and
  - ◆ Ofgem contacts the insolvency office holder to establish the exact situation before taking a decision on whether to revoke the failing supplier's licence and appoint a SoLR.
- 2.3. Once information is received from potential SoLRs Ofgem does not have to proceed to appointment if it considers it would be inappropriate to do so – each case is considered on its merits.

## ***Planning and design***

### **Industry involvement**

- 2.4. The Expert Group met on three occasions before the exercise to assist in its planning and design, and once after the exercise to discuss the lessons learned. Details of the Expert Group's activities, including minutes of meetings, can be found on the Ofgem website at <http://www.ofgem.gov.uk/ssf/exercise.htm>

### **Scope of the exercise**

- 2.5. It was decided that the exercise would test the procedures leading up to the appointment of one or more SoLRs, but would not test the period post

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<sup>4</sup> In the exercise suppliers were asked for their average GB price for domestic direct debt, quarterly cash/cheque and prepayment customers and an average GB price for non-domestic customers.



appointment. Ofgem produced a paper for the Expert Group meeting held on 2 August explaining this decision. This paper is at Appendix 2.

### **The failing company**

- 2.6. The Expert Group decided that it was appropriate to deal with a fairly straightforward supplier failure:
- ◆ an administrative receiver ('the receiver') is appointed to an energy company ("EnergyCo Limited"), which has a large portfolio of electricity and gas customers;
  - ◆ the receiver tries to sell EnergyCo in a trade sale, but in the meantime refuses to accept obligations to meet any liabilities for the gas and electricity being used by customers<sup>5</sup>; and
  - ◆ Ofgem decides to start the process that would enable it to appoint one or more SoLRs in the event that a trade sale does not take place quickly.

### **Data requirements**

- 2.7. The exercise assumed that EnergyCo had between 5% and 10% of both the gas and electricity markets. Dummy data files were created by Transco, ELEXON and a distribution company using aggregated data. These data files did not identify any individual company either directly or indirectly, but were of sufficient detail and quality for the purposes of the exercise.

### **Duration of exercise**

- 2.8. Using the timescales published in the Guidance Document the Expert Group agreed that a period of three working days from the appointment of a receiver to EnergyCo to the appointment of a SoLR was necessary.

### **Prior work**

- 2.9. Ofgem and the Expert Group agreed that prior to the exercise Ofgem would provide draft information requests to the supplier participants together with

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<sup>5</sup> One of the circumstances in which Ofgem might revoke a licence – see Guidance Document para 3.10

details of the criteria that Ofgem would use to assess the information received in order to select one or more SoLRs. The Group also agreed that the aggregated data should be provided to Ofgem before the exercise started<sup>6</sup>.

### **Post exercise processes**

2.10. Ofgem decided that there would only be real value in the exercise if there was a rigorous approach to monitoring and results were properly recorded and communicated to all participants. To achieve this:

- ◆ a small Ofgem team was established to monitor the exercise;
- ◆ the final Expert Group meeting provided an opportunity for participants to comment on the exercise; and
- ◆ a follow up report (this document) would be drafted.

### ***Running the exercise***

2.11. An outline of the exercise is attached at Appendix 3.

2.12. Six companies took part in the exercise:

- ◆ Centrica;
- ◆ Innogy;
- ◆ London Electricity Group;
- ◆ PowerGen;
- ◆ Scottish and Southern Energy; and
- ◆ TXU.

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<sup>6</sup> This decision was based on the knowledge that the processes had been tested in real time for previous actual failures. There was therefore no need to impinge on the exercise time.

- 2.13. A description of the various activities over the three days of the exercise is given below.

### **Day 1**

- 2.14. The exercise started with a teleconference between Ofgem and the receiver. Following this, mock information requests and details of Ofgem's selection criteria were sent by e-mail to participants. Participants were given 6 hours to respond to the requests. A number of questions about the information requests were raised with Ofgem throughout the day. All participants' responses were received close to or reasonably soon after the 5.30 pm deadline. These were copied and distributed to the Ofgem Panel that was assessing the information and deciding who could be appointed as SoLR.

### **Day 2**

- 2.15. During Day 2 Ofgem's Panel analysed the various responses against Ofgem's criteria. A number of queries about particular aspects of the submissions were clarified with the participants.
- 2.16. Towards the end of Day 2, an initial Panel meeting was held to discuss the responses and to try to form a view about which participants might be appointed as SoLR if Ofgem decided to revoke EnergyCo's licence.
- 2.17. Discussion focussed on the relative merits of the responses and on the key issues that distinguished one response from another. Through this process, the Panel determined that some suppliers should not be considered further. The Panel was, however, unable to come to a final decision, primarily because there were some difficult trade-offs to make between submissions and additional information was required as a result of the discussion.

### **Day 3**

- 2.18. Ofgem's Panel reconvened on the morning of Day 3 to agree the information that needed to be clarified with participants. After talking to the suppliers the Panel considered further which were the most appropriate to be a SoLR. It concluded that two companies should be appointed, one for gas and one for

electricity. A telephone conversation was held with the receiver that led to a decision to revoke EnergyCo's licence.

- 2.19. The exercise ended when mock notices to revoke EnergyCo's licences and appoint the SoLRs were issued.

## 3. Lessons Learned

- 3.1. This section outlines the main lessons learned from the exercise. It indicates areas where further work is required and where Ofgem considers it is appropriate to change its procedures for dealing with future supplier failures.

### ***General***

- 3.2. Some suppliers did not always provide answers to specific questions. For instance, where they were asked to provide an average deemed contract price for domestic customers some provided all their regional prices while others responded by stating “see published prices”.

### ***Portfolio information***

- 3.3. Ofgem sent participants high-level aggregated data about the number and type of customers in EnergyCo’s portfolio together with some consumption information.
- 3.4. Participants confirmed that good quality information about the failed supplier’s portfolio is key to their decision whether to volunteer to be a SoLR for some or all of the failed supplier’s customers and what price to charge them. Information requests to potential SoLRs will always be accompanied by high-level information about the failed supplier’s customer portfolio including gas or electricity consumption information. Detailed customer information (such as names, addresses etc) is not provided at the SoLR selection stage, although Ofgem will state whether this information is available and provide details about the format in which it has been obtained. Where the information is available, Ofgem would provide it to the SoLR on appointment. Participants told Ofgem that the more information they have once they are appointed, the less risk they face as a SoLR and the better the service they will be able to provide to customers.

## **Outcome**

- 3.5. Participants suggested that Ofgem should work with Transco, Elexon and distribution companies to agree standard formats for the high-level portfolio information so that potential SoLRs can quickly interpret it. In addition, participants indicated that some simple summary information, for example the total numbers of domestic and non-domestic customers in both gas and electricity would be helpful.
- 3.6. Ofgem has already agreed a standard format for information from Transco and is working with Elexon and distribution companies to agree similar reports.

## ***Timescales***

- 3.7. The timescales given to participants to complete information requests were sufficient given the urgency of the situation. Participants said that they would have welcomed more time to analyse the portfolio information and provide responses.
- 3.8. However, participants pointed out that in a real failure (and particularly a large one), the information they provided to Ofgem would normally require Board approval. This would inevitably extend the time needed by suppliers to complete information requests.

## **Outcome**

- 3.9. Ofgem believes that suppliers are able to prepare a considerable amount of the information that Ofgem needs in advance of an actual failure. This will ensure that when the SoLR selection process starts, companies can spend more time on key decisions. Ofgem will take into account the likelihood that suppliers will need to get Board level approval when setting deadlines for responses.

## ***Use of the Levy***

- 3.10. Ofgem would prefer a SoLR not to make a claim on the levy arrangements for costs it has incurred carrying out its role (see paragraph 2.2). However, the exercise highlighted a need for Ofgem to consider this issue in more detail.

In some cases suppliers had factored into their deemed contracts prices the additional cost (and risk) of being a SoLR. Others indicated that they would not make a claim if they were given a number (but not all) of the failed supplier's customers. Others agreed not to claim in any circumstances. This made it difficult to compare responses.

## **Outcome**

- 3.11. Ofgem recognises that the circumstances of supplier failures are different and that there may be some instances when a SoLR incurs unrecoverable costs. However, an efficient SoLR should be able to minimise these costs. In future, therefore, Ofgem will decide on a case by case basis whether, and in what circumstances, it might be appropriate for a SoLR to make a claim on the levy. In coming to a decision Ofgem will consider issues such as the number of customers and their total consumption of gas/electricity, whether customer details are available (either from the failed supplier or a third party) and whether it would be in customers' best interests to appoint more than one SoLR. The policy for any particular failure will be included with the guidance issued when information requests are sent to potential SoLRs as part of the selection process.

## ***Information requests***

- 3.12. A number of lessons were learned about the information requests that were sent to participants:
- ◆ questions in the information requests could be clearer. This would have the following advantages:
    - to allow suppliers to indicate the optimum and maximum number of customers that they could supply and how their approach might differ, in particular in terms of contract price or claims on the levy;
    - to remove ambiguities which led to different interpretations of the same question;
    - to enable suppliers to provide comprehensive answers, reducing the need to add caveats;

- ◆ more detailed explanatory notes from Ofgem would be helpful, particularly about its policy and expectations on the levy arrangements.

3.13. Lessons were also learned by Ofgem about analysing the responses:

- ◆ Ofgem found it difficult to analyse price information from participants, especially for non-domestic customers. Although evaluation of the responses did not focus solely on price, it was taken into account and it would therefore have been helpful if more ready comparisons could have been made. Ofgem understands that it is difficult for suppliers, especially in the short timescales involved, to conform their individual prices to a standard format. For non-domestic customers some suppliers provided their normal deemed contract information which splits customers into many different groups according to consumption patterns and allocates different prices to each group. Ofgem considered that this approach did not seem realistic as it was unlikely, given the size of the portfolio, that any SoLR would be able to quickly identify customers and bill them in this way; and
- ◆ the Panel needed to be able to contact suppliers to clarify individual responses and, if necessary, negotiate on certain aspects of the responses, particularly the interaction of deemed contract prices, the number of customers a supplier was willing to accept compared to the maximum number it could accept and the potential for any claim on the levy arrangements<sup>7</sup>.

3.14. A suggestion from the Expert Group was that the standard documentation, especially that relating to information requests, should be issued to potential SoLRs from time to time for the purposes of guidance. This would enable potential SoLRs to ensure that their systems and processes are updated to enable them to respond quickly in a real situation.

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<sup>7</sup> Ofgem documents 'Supplier of last resort: Guidance on current arrangements' published in March 2001 and 'Supplier of last resort: Security cover and levies' published in June 2001 explain in more detail



## **Outcome**

- 3.15. Ofgem will review and revise the standard information requests for potential SoLRs to ensure that they can provide as clear and unequivocal answers as possible. In addition Ofgem will issue indicative guidance on completing the information requests. Work will focus on:
- ◆ how to differentiate between the optimum and maximum number of additional customers that could be supplied;
  - ◆ clarification of the position on the levy; and
  - ◆ the best method of obtaining information about deemed contract prices.
- 3.16. These documents will be circulated to members of the Expert Group in January 2003. However suppliers must realise that the circumstances of a particular failure may mean that both the information requests and the guidance may need to be revised.

## ***SoLR Appointment***

- 3.17. Some exercise participants stated that they did not believe that Ofgem's appointment of a single SoLR for EnergyCo's gas customers and a single SoLR for EnergyCo's electricity customers was realistic. In particular, some participants felt that the appointment of multiple SoLRs for both gas and electricity would make it easier for the SoLRs to source energy and to contact and transfer acquired customers.
- 3.18. Ofgem and the industry have been working for some time on ensuring that industry processes can support the appointment of multiple SoLRs. In electricity, current processes allow the appointment of different SoLRs for each Grid Supply Point (GSP). However, there are constraints on the total numbers of customers that distribution companies can transfer at any one time, whether or not there is a single SoLR.
- 3.19. In gas, Ofgem has recently received a Network Code modification proposal (0580) from Transco that changes the Network Code obligations of a SoLR's shipper. The modification proposes a procedure that will provide information

about the acquired portfolio to the shipper to enable it to balance the portfolio until supply point transfers have taken place. Modification proposal 0580 does not support the appointment of more than one SoLR, and Transco has informed Ofgem that it will not be feasible to enhance its systems so as to support the appointment of multiple SoLRs using the procedure proposed in 0580. If 0580 is accepted by Ofgem, it will therefore be important for the industry and Transco to develop arrangements that would support the appointment of multiple SoLRs.

## **Outcome**

- 3.20. Ofgem is aware of the challenges that would be faced by a SoLR appointed to a very large portfolio of customers. Ofgem would prefer to appoint one SoLR only to a failed supplier's customers as it would be less confusing for affected customers. However, in the scenario of a large supplier failure this may not be feasible, and when selecting SoLRs Ofgem will carefully consider whether the appointment of multiple SoLRs would be more appropriate. This decision would need to be based on the individual circumstances of each failure.
- 3.21. Ofgem's revised SoLR Guidance Document will set out the SoLR selection and appointment processes in detail.

## ***Additional Work***

- 3.22. Additional work will focus on:
- ◆ whether standard terms (other than price) for deemed contracts would benefit customers;
  - ◆ whether it would benefit the SoLR selection process to have other documents as standard – e.g. a statement to be signed by potential SoLRs stating that they will comply with data protection principles upon receiving information about the failed supplier's portfolio;
  - ◆ revising Ofgem's procedures to ensure they allow sufficient time to clarify responses and negotiate with potential SoLRs;
  - ◆ consideration of whether another meeting of the Expert Group is required to discuss progress and identify any further work required; and

- ◆ consideration of whether there is a need for another exercise in 2003.

## 4. Issues following appointment as a SoLR

- 4.1. This chapter highlights a number of concerns that suppliers raised during the Expert Group meetings that were not tested as part of the exercise.

### ***Customer details***

- 4.2. Participants said that there is a significant risk to any SoLR if customer contact details are not available to a SoLR. Although the meter point addresses are available from Transco and distribution companies these are not necessarily the same as the billing address (for example for non-domestic multi-site customers). This significantly increases the likelihood that the SoLR will not be able to bill customers for a long period after appointment, leading to potentially large losses. An additional risk arises if the supplier has failed because of inadequate billing systems since any information obtained about customers is likely to be unreliable.
- 4.3. In practice, the Group considered that contact details would probably be available in a real failure from one or more of the following sources:
- ◆ Ofgem (where they had been collected in advance from the failing supplier);
  - ◆ the insolvency office holder, although the SoLR would probably have to pay for the information. The insolvency practitioner on the Expert Group stated that the appointment of more than one SoLR would complicate matters as the insolvency office holder would prefer to only have to negotiate with one party and splitting the portfolio information might not be possible in any event; and
  - ◆ a third party in circumstances where it was providing billing services for the failed supplier. (Again the SoLR would probably have to pay for the information and there could be contractual/confidentiality issues that complicated this approach).

## ***Transfer to the SoLR***

4.4. The Expert Group raised a number of issues about customer transfers:

- ◆ for a large supplier failure the scale of the requirement to transfer customers to the SoLR's own billing system is likely to swamp existing processes. Many of these work in batch mode in overnight runs and there would therefore be limited capacity to cope with millions of transfers. Overall, the Group felt that the time needed to process customer transfers would be far greater than previously anticipated (for example the three month limit stipulated in the electricity BSC for electricity registrations could not be met by a SoLR who had acquired a large portfolio);
- ◆ there would be considerable problems if customers transferred to a new supplier before the SoLR had transferred them to its portfolio because:
  - the SoLR would have limited ability to capture the customer details and bill them for energy used. This would result in losses for the SoLR;
  - there is potential for erroneous transfers back to the SoLR; and
- ◆ the Expert Group asked how the SoLR would cope with acquiring Prepayment meter customers. Ofgem has conducted some work on this issue, and has introduced into its internal procedures various measures designed to minimise the problems. This has included consulting on the problems that a SoLR would face, and working with Transco and distribution companies to try to ensure that address details of these customer types could be quickly identified in the event of a supplier failure.

4.5. At the final Expert Group, supplier participants agreed that they would take forward work addressing post-SoLR appointment concerns. Ofgem is willing to facilitate these meetings if necessary and encourages the industry to take them forward.

# Appendix 1 - Terms of Reference for Expert Group

## *Introduction*

- 1.1 Ofgem has been working for some time on the processes and procedures that should be adopted in the event of a gas or electricity supplier failure. The failures of Independent Energy and Enron have given additional impetus to this work. Ofgem has published a number of documents in relation to its work on supplier failure, which can be found on the Ofgem website at:  
[http://www.ofgem.gov.uk/projects/supplierfail\\_index.htm](http://www.ofgem.gov.uk/projects/supplierfail_index.htm)
- 1.2 Ofgem now believes that it is appropriate to conduct an exercise involving key elements of the electricity and gas communities, to determine how robust the procedures to be used in the event of the appointment of one or more SoLRs are, and to ensure that both it and the industry are aware of what needs to be done, especially in relation to the very limited timescales for particular actions. As a first step, Ofgem wishes to establish an Expert Group to assist in the design of the exercise.

## *Objectives of Exercise*

- 1.3 The Supplier Failure exercise has two key objectives:
- ◆ to test the processes in the period between the alert of a potential supplier failure and the appointment of a SoLR;
  - ◆ to provide a platform to train Ofgem and industry personnel on what needs to be done by whom and to what deadlines in the steps leading to the appointment of a SoLR.

For the avoidance of doubt, this exercise will not be testing the following:

- ◆ bulk registration/transfer systems or processes. These are already established by the central service providers in some instances, and in others the separation of financial and registration responsibility allows enduring processes to be used for such transfers;

- ◆ dealing with receivers, administrators or liquidators, other than the steps necessary to follow due process in the run up to the appointment of an SoLR;
- ◆ handling a trade sale, other than necessary parallel processes in the run up to the appointment of a SoLR.

### ***Membership***

1.4 Ofgem proposes to invite those parties and individuals that are best placed to assist in this process, and who are willing to do so, to participate in this group. It is proposed that the chairmanship of the group will rest with Ofgem. It is expected that one or more other Ofgem representatives will also attend meetings.

1.5 There are two other groups of parties that Ofgem will invite to attend:

- ◆ the first group comprises those providing central services, who will have important roles to play in the process leading to the appointment of one or more SoLRs. This includes Transco and ELEXON. It also includes one or more of the distribution businesses in the electricity industry (the equivalent role in the gas industry is fulfilled by Transco);
- ◆ the second group comprises industry participants who have an interest in being appointed as a SoLR. This includes suppliers in both gas and electricity. At this stage, invitations to attend are being extended to those who replied positively to previous correspondence in relation to SoLR appointments, although if there is considerable interest from the industry more participants will be invited.

1.6 Each company invited to participate will be asked to send one representative to meetings of the group, except for the central service providers, who will be asked to provide a variety of technical expertise which is likely to reside in more than one person.

### ***Frequency of Meetings***

1.7 It is anticipated that two or three meetings of the group will be required prior to the exercise and the first of these will be held on Thursday 4th July. It is

proposed that the meetings will be held at Ofgem's offices in London. A detailed schedule of convenient dates and venues for further meetings will be developed at the first meeting, although proposals for those further meetings are contained in the letter inviting participation in the group.

### ***Objectives of Expert Group***

1.8 The objectives of the group are as follows:

- ◆ to comment on the objectives for the exercise itself;
- ◆ to contribute to the design of the exercise;
- ◆ to identify issues of concern to the industry and to advise on how the exercise can best be structured to deal with these;
- ◆ to contribute to the development of the monitoring processes to be used during the exercise;
- ◆ to participate in the exercise itself and to help disseminate its results throughout the industry;
- ◆ to participate in the subsequent analysis of the lessons learned from the exercise.

### ***Timetable***

1.9 The timetable is for discussion within the group, in terms of the feasibility of particular actions. Nevertheless, Ofgem would like to proceed as soon as is practicable, and the following timetable is proposed:

Thursday 4<sup>th</sup> July

First Meeting of Group

Confirmation of Objectives, Review of Initial Design, Discussion of Issues, Preliminary Discussion of Date, Venue and Scale

Friday 2<sup>nd</sup> August

Second Meeting of Group  
Detailed Discussion of Design,  
Confirmation of Date, Venue and Scale



Week Commencing 23<sup>rd</sup> September    Hold Exercise

Friday 11<sup>th</sup> October

Final Meeting of Group  
Review of Lessons Learned Report on  
Exercise

***Transparency***

- 1.10    It is proposed that agendas, brief notes and working papers for the meetings will be made available to all interested parties, via a page on the Ofgem website.

***Expenses***

- 1.11    It is proposed that those attending will do so on a voluntary basis, and that they will fund their own expenses associated with attending the meetings.

***Avoidance of Doubt Statement***

- 1.12    For the avoidance of doubt, the exercise is solely for the purposes stated in this document. Participation in this exercise or in the Expert Group does not in any way confer preferential treatment on those parties involved in it and in the event that Ofgem is required to appoint a SoLR, its decision shall be made independently of this evidence.

**NOTE: An additional meeting of the Expert Group was held at the request of the Group on 5 September 2002**

## Appendix 2 - Testing the transfer of registrations

Ofgem has decided to lead an industry wide test of the procedures and processes to be used in the appointment of a Supplier of Last Resort (SoLR) and an Expert Group involving a number of participants has been established. At the first meeting of the Group some members expressed concern at what they felt were the relatively narrow terms of reference for the exercise; in particular they wanted it to continue beyond its planned termination point, the appointment of one or more SoLRs, so that the transfer of customers from the failed supplier to the SoLR(s) could also be tested. This paper considers the issues involved.

### Background

In its original internal papers proposing a SoLR test exercise, Ofgem considered incorporating the testing of customer transfers. In discussion with some of the Central Service Providers (CSPs), several problems came to light and it was decided eventually to confine the exercise to the testing of processes and procedures leading to the appointment of a SoLR. In particular:

- Ofgem's primary concern is to ensure that, in the event of a SoLR appointment, its procedures and processes work properly and that third parties, especially those wishing to be considered for appointment as a SoLR, know what to do. The testing of subsequent processes in which Ofgem plays little or no part is more a matter for those concerned;
- One CSP, ELEXON, has pointed out that in electricity it is possible to separate financial and registration responsibility at the point of SoLR appointment. This means that it is not necessary to transfer all customers at the point in time when a SoLR assumes responsibility for the customers of a failed supplier, and that instead enduring procedures for transfer can be used;
- another CSP, Transco, has already introduced processes for the bulk transfer of registrations. However, most gas shippers have indicated that their systems would not be able to receive and process the file formats that would be used for purposes of bulk transfer. The industry, through the Network Code SoLR Review Group, has

instead been working on developing solutions similar to those in the electricity regime, allowing an appointed SoLR to separate financial and registration liabilities. As these solutions have yet to be implemented, a test will not provide the industry with the assurances that it is looking for;

- Both Transco and ELEXON have indicated that a full scale exercise would require the real time processing of transfers. As such an exercise could not be conducted within the normal registration systems, as this would compromise live data, the exercise could only be carried out using a test environment. The only environments of sufficient scale would appear to be whatever backup systems were available, and the CSPs were not sure that all participants had fully functioning backup systems capable of being used for such an exercise<sup>8</sup>. Furthermore, the backup systems are regularly accepting data from the live systems, so as to be available should backup be required, and careful control of an exercise would be required accordingly;
- It is likely that supplier systems vary in the ways in which they interface with the central systems. Although enduring processes would be the basis for the test, as there are no separate bulk transfer processes, there may be different system implications for different suppliers;
- at present, the Expert Group and the exercise includes the participation of only one distribution company, nominated by the EA Distribution Commercial Group. If a full scale exercise is to be conducted, the scope of the exercise will need to be widened so as to include the other thirteen distribution companies. Consideration will also need to be given to the inclusion of non-Transco gas transportation companies. Widening the scope of the exercise to include many more participants, as well as increasing the complexity of the exercise will greatly lengthen the timescale for designing and conducting it;
- under current proposals, the costs to suppliers and CSPs of participating in the exercise are low, both in terms of financial cost and other resources. Ofgem believes that widening the scope of the exercise to include transfer testing will greatly increase the cost to participants, for example any full test would involve agents who

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<sup>8</sup> The alternative, of using a separate environment of reduced scale so that only a small number of transfers could be tested, was not felt sufficient to provide confidence in the integrity of the processes that would be used in a real situation.

are unlikely to participate without payment, and special test environments would probably need to be created;

- finally, through the failures of Independent Energy and Enron, Ofgem believes that much experience has been gained in terms of how to deal with the customers of a failed supplier. In these and other cases, the lack of fully tested registration procedures was not seen to be a problem. It is accepted that certain issues particular to an SoLR appointment have not been tested, the principal difference to a trade sale being a lack of customer information, but Ofgem does not think that it has a significant role to play in the testing of alternative ways of obtaining appropriate data.

Given these considerations, Ofgem decided not to incorporate a bulk transfer element into the present exercise.

## **Supplier Concerns**

At the Expert Group, suppliers expressed two principal concerns in relation to transfer of registration details:

- it seems illogical to terminate the present SoLR appointment exercise without testing the transfer of registration information;
- without such a transfer being tested, it would be difficult to understand the risks involved in a SoLR appointment.

Ofgem does not believe that it is illogical to terminate the present exercise at the moment of appointment, as it is at that time that Ofgem's primary involvement in the process winds down. Ofgem has a natural interest in ensuring that the appointment is successful, but procedures and processes after appointment are largely a matter for those appointed and other parties such as the failed supplier and the CSPs.

In terms of the risks of a SoLR appointment, Ofgem does not believe that these depend heavily on transfer processes. As has already been noted, a combination of prior testing, the work on the separation of financial and registration responsibility and balancing procedures and the lessons learned from earlier failures have all contributed to a general increase in the understanding of what needs to be done.

Nevertheless, Ofgem accepts that an issue in the minds of any party considering a SoLR appointment will be the risks associated with taking on many new customers on whom billing information may take time to find. Because of this, in assessing potential SoLRs, issues such as the ability of the company to manage a complex one-off exercise will be of importance. Furthermore, as the issues associated with customer billing will inevitably vary with each case, it is open to question whether a full test will cover all such issues, and therefore the level of comfort to be obtained from it.

As highlighted above, one issue that might be of concern, in both electricity and gas, is that until customers are transferred to the SoLR (or its shipper in gas), it is exposed to some residual imbalance settlement risk. In fact, there are processes that are already in place or that are being developed that can deal with this. In electricity, it is a straightforward matter to transfer the Balancing Mechanism Units relating to non half hourly metered customers (there is a single such BMU per supplier per GSP) to the new supplier(s), allowing immediate consolidation of production and consumption accounts. In gas, Transco and the Network Code SoLR Review Group are developing a procedure that will give the appointed SoLR some ability to proactively balance the portfolio until supply point transfer has taken place.

## **Conclusions and Next Steps**

For the reasons set out in this paper, Ofgem does not believe that it would be appropriate for the present exercise, which it is leading, to be expanded to incorporate the testing of registration transfers. Ofgem recognises, however, that a number of suppliers might still wish to test such transfers. Insofar as any dummy data generated in the exercise is useful, then it could be made available, although data design issues relating to the separate exercise, if any, should not be permitted to change the ways in which the present exercise will be run.

Ofgem believes that any tests relating to post appointment processes should be very much a matter for the industry. It does not believe that it has a central role, as the substance of the tests would be the transfer of data between third parties; whilst such parties are licensed entities, how they conduct their business is primarily a matter for them. Ofgem is willing to provide limited facilitation for such an exercise, providing that it is clearly understood that such facilitation does not extend to leading the exercise nor playing a key role in it.

## Appendix 3 - Outline of the exercise

| Real Time |  | Ofgem   | CSPs  | Administrative Receiver          | Participants   | Meetings Schedule                            |
|-----------|--|---|---|----------------------------------|--|--|
| Day - 20  |  | Prepare detailed exercise blueprint<br>Identify best way of creating Energyco<br>Prepare all exercise materials<br>Establish exercise format and communication links<br>Prepare selection criteria for SoLR appointment using selection grid in handbook<br>Serve IRs on CSPs (Transco, ELEXON, Disco MPASs) re portfolio, trading and credit position of failed supplier | Research and understand role<br>Create relevant files for Energyco<br>Assign resources to exercise<br>Test environments<br>Respond to IRs by 12/9 | Prepare press release re failure | Research and understand role<br>Assign resources to exercise<br>Obtain necessary clearances<br>Test environments | 5 September<br>Third Meeting of Expert Group |
| Day - 10  |  | Prepare list of potential SoLRs<br>Review CSP responses to IRs and assemble information packs for potential SoLRs   | Final preparations  | Final preparations               | Final preparations   |  |

| Real Time |       | Ofgem   | CSPs                 | Administrative Receiver   | Participants                              | Meetings Schedule |
|-----------|-------|---|----------------------|---|---|-------------------|
| 23/9      | 10.00 | Set up Core Team and control room<br>Issue Press Release + Q&As<br>Prepare IRs for all licensees with relevant licensing structure<br><b>Issue IRs to licensees</b><br>Contact receiver re willingness to pay central bills<br>Notify energywatch and other relevant groups | Receive announcement | Announce failure and appointment<br>Issue standard notices as to conduct of future business | Receive IR<br>Start work on IR            |                   |
| Day 1     | 12.00 | Begin preparation of draft revocation notice  |                      |   | Respond to Ofgem confirming receipt of IR |                   |
| Day 1     | 16.00 | Receive completed IRs   |                      |   | <b>Send completed IRs to Ofgem</b>        |                   |
| Day 1     | 17.00 | Send acknowledgement of receipt of IRs<br>Chase missing IRs   |                      |   | Receive acknowledgement of receipt of IR  |                   |

| Real Time |       | Ofgem  | CSPs | Administrative Receiver  | Participants  | Meetings Schedule |
|-----------|-------|--|------|--|---|-------------------|
| Day 2     | 10.00 | Assess IRs against criteria<br>Follow up on queries with potential SoLRs<br>Deal with queries from potential SoLRs                         |      | Advise Ofgem of inability to complete information request<br><br>Advise Ofgem of inability to give assurances over meeting gas and electricity central bills | Deal with any queries raised by Ofgem<br><br>Raise queries on information accompanying IR |                   |
| Day 2     | 11.00 | <b><i>Advise receiver that licence revocation is being considered, and offer meeting</i></b><br><br>Prepare for meeting with administrator |      | Receive notice of meeting  |   |                   |
| Day 2     | 14.00 | Assemble IR information and rank potential SoLRs<br><br>Raise any final queries with potential SoLRs                                       |      |  | Deal with any final queries   |                   |
| Day 2     | 16.00 | Check re any further information required for meeting with administrator   |      |  |   |                   |



| Real Time |       | Ofgem   | CSPs  | Administrative Receiver                 | Participants   | Meetings Schedule  |
|-----------|-------|---|---|---|--|--|
| Day 2     | 17.00 | Incorporate final queries into assessment matrix<br><br><b><i>Take decision on SoLR appointment (subject to meeting with administrator)</i></b>   |   |   |  | 17.00 Ofgem meeting re potential SoLRs                         |
| Day 3     | 10.00 | Final preparations for meeting with administrator   |   |   |  |  |
| Day 3     | 11.00 | <b><i>Conduct meeting with administrator</i></b>  |   | Attend meeting                          |  | 11.00 Ofgem and receiver                                       |
| Day 3     | 13.00 | Consider issues raised by administrator at meeting<br><br><b><i>Decide to revoke and appoint SoLR</i></b><br><br><b><i>Issue revocation notice</i></b><br><br><b><i>Issue SoLR appointment notice(s) – all</i></b><br><br>Issue press notices<br><br>Advise interested parties not appointed of reasons why not appointed | Receive revocation notice<br><br>Receive notice of appointment of SoLR(s) | Receive notice of revocation of licence | Receive SoLR appointment notice<br>or<br>receive advice that not appointed | 13.00 Ofgem, final decision on revocation and SoLR appointment |

| Real Time |       | Ofgem                              | CSPs                                 | Administrative Receiver              | Participants                         | Meetings Schedule |
|-----------|-------|------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|-------------------|
| Day 3     | 16.00 | Issue notice closing down exercise | Receive notice closing down exercise | Receive notice closing down exercise | Receive notice closing down exercise |                   |