



Independent Market Operator

Final Rule Change Report

**Title: List of Entities Meeting Acceptable
Credit Criteria**

RC_2011_04

Standard Rule Change Process

Date: 17 October 2011

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EXECUTIVE SUMMARY

Background

The IMO has proposed that the four major Australian banks be included on a list of entities not required to provide evidence that they meet the Acceptable Credit Criteria prescribed in the Market Rules. Currently, a Market Participant must complete the Acceptable Credit Criteria Form and have it signed by a solicitor of a reputable commercial law firm accepted by the IMO if they wish to use a nominated financial institution for Credit Support or Reserve Capacity Security.

Consultation

- The Pre Rule Change Discussion Paper was endorsed by the Market Advisory Committee at the June 2011 meeting.
- The IMO formally submitted the Rule Change Proposal and called for submissions on 13 June 2011. Submissions were received from Landfill Gas and Power (LGP) and Synergy. Both submissions supported the proposed amendments. LGP also suggested a minor clarification to the Amending Rules which has been accepted by the IMO.
- The Draft Rule Change Report was published on 22 August 2011. Second round submissions were received from Synergy and Alinta, both supporting the change. Alinta suggested some changes to the drafting to ensure that it fully meets the intent of the proposal. The IMO agreed with Alinta's concerns and has updated the proposed amendments accordingly.

Assessment against the Wholesale Market Objectives

The IMO has found the proposed amendments will promote Wholesale Market Objective (a) and are consistent with the remaining Wholesale Market Objectives.

Practicality and Cost of Implementation

Implementing the amendments is considered to be within the day to day operation of the IMO and therefore will not incur additional costs. Submissions from Market Participants did not raise any practical implications.

The IMO's Decision

The IMO's decision is to accept the Rule Change Proposal as modified following the first and second submission periods.

Next steps

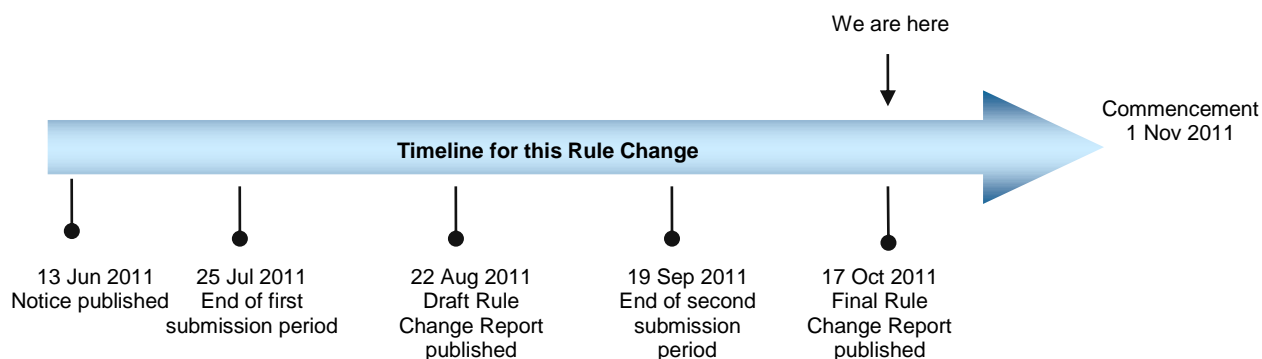
The resultant Amending Rules will commence at **8:00am** on **1 November 2011**.

1. RULE CHANGE PROCESS AND TIMETABLE

On 13 June 2011 the Independent Market Operator (IMO) submitted a Rule Change Proposal regarding amendments to clause 2.38.7 of the Wholesale Electricity Market Rules (Market Rules).

This proposal has been processed using the Standard Rule Change Process, described in section 2.7 of the Market Rules.

The key dates in processing this Rule Change Proposal have been:



2. PROPOSED AMENDMENTS

2.1 *The Rule Change Proposal*

To confirm whether a Credit Support or Reserve Capacity Security provider meets the Acceptable Credit Criteria, a Market Participant or Network Operator must complete the Acceptable Credit Criteria Form available on the IMO's website. This includes ensuring that the Form has been signed by a solicitor of a reputable commercial law firm acceptable to the IMO. This must happen independently for Credit Support and for Reserve Capacity Security even when the same financial entity is providing both services.

The IMO has proposed that the four major Australian banks be included on the List of Entities not required to provide evidence that they meet the Acceptable Credit Criteria when a Market Participant puts forward a guarantee or bank undertaking as Credit Support or Reserve Capacity Security from one of those entities.

The full details of the Rule Change Proposal are contained in Appendix 1.

2.2 *The IMO's Initial Assessment of the Proposal*

The IMO decided to proceed with the proposal on the basis that Market Participants should be given an opportunity to provide submissions as part of the rule change process,

3. CONSULTATION

3.1 *The Market Advisory Committee*

This Rule Change Proposal was originally presented to the Market Advisory Committee (MAC) at the 8 June 2011 meeting as a Pre Rule Change Discussion Paper. There was

general support from MAC members for the proposal. Full minutes of the meeting can be accessed at http://www.imowa.com.au/MAC_39

3.2 Submissions received during the first submission period

The first submission period for this Rule Change Proposal was between 14 June 2011 and 25 July 2011. The IMO received submissions from Landfill Gas and Power (LGP) and Synergy during the first submission period. A copy of the full text of all submissions is available on the IMO website.

In summary, all of the submissions received support the proposed amendments. In particular, Synergy noted that the proposed changes will reduce the number of times a Market Participant is required to submit an Acceptable Credit Criteria Form and in doing so provide a cheaper and more streamlined approach to credit support. LGP supported the intent of the Rule Change Proposal on the grounds that it reduces the administrative burden and expense placed on Market Participants without impacting the substance of the Market Rules.

LGP also submitted that while concision in the drafting of the proposed amendments to the Market Rules was welcomed, inclusion of an additional amendment to specify the process around the placing of special entities on the list and the criteria for their nomination would be beneficial.

The assessment by submitting parties as to whether the proposal would better the Wholesale Market Objectives is summarised below:

Submitter	Wholesale Market Objective Assessment
LGP	consistent with all the Wholesale Market Objectives
Synergy	better addresses (b) and (d)

3.3 The IMO's response to submissions received during the first submission period

LGP submitted that further details of the process for placing entities on the list (which exempts them from having to provide evidence that they meet the Acceptable Credit Criteria) and the criteria for their nomination would be beneficial.

The IMO agreed with LGP's suggestion. The intention of the proposed amendments is to give the IMO discretion to include an entity on the list where it considers that the entity meets the Acceptable Credit Criteria outlined in clause 2.38.6. The IMO noted that it does not intend to exercise its discretion to include any other entities on the list other than the Big 4 (i.e. ANZ, Commonwealth Bank, NAB and Westpac) at this stage.

The IMO revised the proposed Amending Rules accordingly (new clause 2.38.10). For further details refer to Appendix 2 of this report.

3.4 Submissions received during the second submission period

The second submission period for this Rule Change Proposal was between 23 August 2011 and 19 September 2011. The IMO received submissions from Alinta and Synergy during the second submission period. A copy of the full text of all submissions is available on the IMO website.

In summary, both submissions supported the proposed amendments. Alinta however expressed concern that the amendments may not achieve the intended outcome. In particular, Alinta considered the proposed Amending Rules do not appear to prescribe that entities that are included on the list of entities maintained by the IMO under clause 2.38.7 meet the Acceptable Credit Criteria for the purposes of clause 2.38.6 (and therefore can be a party that provides Credit Support). Alinta suggested two options to modify the proposed drafting to address this issue.

The assessment by submitting parties as to whether the proposal would better the Wholesale Market Objectives is summarised below:

Submitter	Wholesale Market Objective Assessment
Alinta	As proposed, unlikely to be inconsistent with the Wholesale Market Objectives. Alinta considered that its suggested further amendments may better achieve the Wholesale Market Objectives.
Synergy	Better addresses (b) and (d)

3.5 *The IMO’s response to submissions received during the second submission period*

The IMO agrees with Alinta that a determination that an entity is not required to provide evidence of meeting the Acceptable Credit Criteria does not necessarily equate to a determination that the entity actually meets the Acceptable Credit Criteria (though this is most likely to be the case). To ensure that the intent of the proposal is achieved, the IMO has adopted Alinta’s suggestion to:

- amend clause 2.38.7(b) to specify entities the IMO has determined in its absolute discretion meet the Acceptable Credit Criteria, rather than entities the IMO has determined are not required to provide evidence of meeting the Acceptable Credit Criteria; and
- for the sake of brevity, removing clause 2.38.10 as its purpose is met by the amended clause 2.38.7(b).

Details of the proposed additional amendments are available in section 4.1 of this report.

3.6 *Public Forums and Workshops*

No public forums or workshops were held in relation to this Rule Change Proposal.

4. THE IMO’S ASSESSMENT

In preparing its Rule Change Report, the IMO must assess the Rule Change Proposal in light of clauses 2.4.2 and 2.4.3 of the Market Rules.

Clause 2.4.2 outlines that the IMO “*must not make Amending Rules unless it is satisfied that the Market Rules, as proposed to be amended or replaced, are consistent with the Wholesale Market Objectives*”. Additionally, clause 2.4.3 states, when deciding whether to make Amending Rules, the IMO must have regard to the following:

- any applicable policy direction from the Minister regarding the development of the market;
- the practicality and cost of implementing the proposal;

- the views expressed in submissions and by the MAC; and
- any technical studies that the IMO considers necessary to assist in assessing the Rule Change Proposal.

The IMO notes that there has not been any applicable policy direction from the Minister or any technical studies commissioned in respect of this Rule Change Proposal. A summary of the views expressed in submissions and by the MAC is available in section 3 of this report.

The IMO’s assessment is outlined in the following sub-sections.

4.1 Additional Amendments to the Proposed Amending Rules

Following the closure of the second submission period the IMO has made some additional changes to the proposed Amending Rules to address the concerns raised by Alinta in its submission. The proposed changes are as follows (~~deleted text~~, added text):

- 2.38.7. The IMO must maintain on the Market Web Site a list of entities which:
- (a) have provided the IMO, in the previous twelve months, with evidence satisfactory to the IMO that they meet the Acceptable Credit Criteria outlined in clause 2.38.6; or
 - (b) the IMO has determined in its absolute discretion meet ~~under clause 2.38.10 are not required to provide evidence of meeting~~ the Acceptable Credit Criteria outlined in clause 2.38.6.

~~2.38.10. The IMO may add the name of an entity to the list described in clause 2.38.7 at any time if the IMO considers in its absolute discretion that the entity meets the Acceptable Credit Criteria outlined in clause 2.38.6.~~

4.2 Wholesale Market Objectives

The IMO considers that the Market Rules as a whole, if amended, will be consistent with the Wholesale Market Objectives.

Wholesale Market Objective	Consistent with objective
(a) to promote the economically efficient, safe and reliable production and supply of electricity and electricity related services in the South West interconnected system	Yes
(b) to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors	Yes
(c) to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions	Yes
(d) to minimise the long-term cost of electricity supplied to customers from the South West interconnected system	Yes
(e) to encourage the taking of measures to manage the amount of electricity used and when it is used	Yes

Further, the IMO considers that the Market Rules if amended would not only be consistent with the Wholesale Market Objectives but also allow the Market Rules to better address Wholesale Market Objective (a):

Impact	Wholesale Market Objectives
Allow the Market Rules to better address objective	a
Consistent with objective	b, c, d, e
Inconsistent with objective	-

The proposed amendments will remove the requirement for a solicitor to sign an Acceptable Credit Criteria form where a security is provided by an entity the IMO has deemed to be on the list and therefore not required to provide evidence that they meet the Acceptable Credit Criteria (i.e. one of the four major Australian banks). The IMO considers that the proposed changes will provide a more effective and efficient process than each of these Market Participant's solicitors signing the form. The proposed changes will therefore promote Wholesale Market Objective (a).

4.3 Practicality and Cost of Implementation

Practicality:

The IMO has not identified any issues with the practicality of implementing the proposed changes. None of the submissions received during the first and second round submission periods raised any implications for Market Participants.

Cost:

The proposed amendments will not require any changes to the Wholesale Electricity Market Systems operated by the IMO.

The IMO notes that there will be updates required to the following Market Procedures:

- Prudential Requirements; and
- Reserve Capacity Security.

The IMO considers that these updates fall within the day to day operation of the IMO and therefore will no incur additional personnel costs.

5. THE IMO'S DECISION

The IMO's decision is to accept the amendments to clause 2.38.7 as proposed in the Rule Change Proposal and modified following the first and second submission periods.

5.1 Reasons for the decision

The IMO has made its decision on the basis that the Amending Rules:

- will allow the Market Rules to better address Wholesale Market Objective (a);
- are consistent with the remaining Wholesale Market Objectives;
- had the support of the MAC; and
- had the general support of submissions received during the first and second submission periods.

6. AMENDING RULES

6.1 Commencement

The amendments to the Market Rules resulting from this Rule Change Proposal will commence at **8:00am** on **1 November 2011**.

6.2 Amending Rules

The following clauses are amended (added text, ~~deleted text~~):

2.38.7. The IMO must maintain on the Market Web Site a list of entities which:

- (a) _____ have provided the IMO, in the previous twelve months, with evidence satisfactory to the IMO that they meet the Acceptable Credit Criteria outlined in clause 2.38.6; or
- (b) _____ the IMO has determined in its absolute discretion meet the Acceptable Credit Criteria outlined in clause 2.38.6.

APPENDIX 1: ORIGINAL RULE CHANGE PROPOSAL

Change Proposal No: RC_2011_04
Received date: 13 June 2011

Change requested by:

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Date submitted:	13 June 2011
Urgency:	Medium
Change Proposal title:	List of Entities Meeting the Acceptable Credit Criteria
Market Rule affected:	2.38.7

1. Details of the proposed Market Rule Change

Rule Change Proposal Background

Under clause 2.38.7 of the Market Rules, the IMO must maintain on the Market Web Site a list of entities which have provided the IMO, in the previous twelve months, with evidence satisfactory to the IMO that they meet the Acceptable Credit Criteria outlined in clause 2.38.6 (the List).

The Rule Change Proposal: Acceptable Credit Criteria (RC_2010_36) removed the requirement for a solicitor to sign an Acceptable Credit Criteria form for each Market Participant providing Credit Support or Reserve Capacity Security where the financial entity being used was included on the List. The IMO considered that the proposed changes provided a more cost effective and efficient process than each Market Participant's solicitor signing the form. The amendments introduced by RC_2010_36 commenced on 1 April 2011.

In response to a suggestion from a Market Participant, the IMO has considered opportunities to further reduce the burden on Market Participants of providing evidence of the credit-worthiness of financial entities that provide guarantees or bank undertakings as either Credit Support or Reserve Capacity Security, where provision of that evidence is considered to be of little additional value.

Proposed Change to Existing Market Rule

It is proposed that, in addition to the provisions introduced by RC_2010_36, the four major Australian banks be included on the List. Entities on the List are not required to provide evidence that they meet the Acceptable Credit Criteria when a Market Participant puts forward a guarantee or bank undertaking as Credit Support or Reserve Capacity Security from one of those entities.

Other financial entities may be included on the List by either the financial entity itself or a Market Participant providing the necessary evidence as to the credit-worthiness of the financial entity. This can be done either at 12-month intervals (to maintain the exemption)

or as needed when a guarantee or bank undertaking is presented as Credit Support or Reserve Capacity Security.

When a financial entity is removed from the list because the 12-month period expires, the relevant Market Participant will not necessarily be required to replace its security. The financial entity, or the Market Participant, will simply have to provide the usual evidence of creditworthiness when it next puts forward a guarantee to the IMO. The IMO maintains its monthly monitoring of the credit ratings of all financial entities providing Reserve Capacity Security or Credit Support, regardless of whether they remain on the List.

However, Credit Support or Reserve Capacity Security will cease to be valid if the entity that provided the guarantee or bank undertaking ceases to meet the Acceptable Credit Criteria. This includes if its credit rating falls below the level specified in clause 2.38.6. In that event, the Market Participant would be in default of its Prudential Obligations and be required to immediately notify the IMO and replace the guarantee or bank undertaking with one from an organisation that meets the Acceptable Credit Criteria, or with cash.

2. Explain the reason for the degree of urgency:

The proposed rule changes are considered to be of a moderate level of urgency given that the issues with the existing rules prompting these changes do not put at risk the safe, effective and reliable operation of the WEM. The proposed rule changes cannot reasonably be considered to be of a high level of urgency for this reason.

3. Proposed specific changes to particular Rules: (for clarity, please use the current wording of the Rules and place a strikethrough where words are deleted and underline words added)

2.38.7 The IMO must maintain on the Market Web Site a list of entities which:

(a) _____ have provided the IMO, in the previous twelve months, with evidence satisfactory to the IMO that they meet the Acceptable Credit Criteria outlined in clause 2.38.6; or

(b) are one of the entities the IMO has determined are not required to provide evidence of meeting the Acceptable Credit Criteria outlined in clause 2.38.6.

4. Describe how the proposed Market Rule change would allow the Market Rules to better address the Wholesale Market Objectives:

The proposed Market Rule change would allow the Market Rules to better address Wholesale Market Objectives:

(b) to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors; and

(d) to minimise the long-term cost of electricity supplied to customers from the South West interconnected system;

by providing a more simple, efficient and cheaper way of certifying that an entity meets the Acceptable Credit Criteria.

5. Provide any identifiable costs and benefits of the change:

Engaging a solicitor to complete the Acceptable Credit Criteria Form for an entity already deemed by the IMO as meeting the Acceptable Credit Criteria is expensive and time-consuming and the additional costs incurred are ultimately passed on to end consumers. The proposed amendments will remove this requirement from the Market Rules.

APPENDIX 2: AMENDMENTS IN THE DRAFT REPORT

Following the closure of the first submission period and in response to the issues that were raised in submissions the IMO proposed to change the proposed Amending Rules to better clarify the IMO's discretion in including an entity on the list. The proposed changes are as follows (~~deleted text~~, added text):

- 2.38.7. The IMO must maintain on the Market Web Site a list of entities which:
- (a) have provided the IMO, in the previous twelve months, with evidence satisfactory to the IMO that they meet the Acceptable Credit Criteria outlined in clause 2.38.6; or
 - (b) ~~are one of the entities~~ the IMO has determined under clause 2.38.10 are not required to provide evidence of meeting the Acceptable Credit Criteria outlined in clause 2.38.6.
- 2.38.10. The IMO may add the name of an entity to the list described in clause 2.38.7 at any time if the IMO considers in its absolute discretion that the entity meets the Acceptable Credit Criteria outlined in clause 2.38.6.