Wholesale Electricity Market
Rule Change Submission Form

RC_2012_23 Prudential Requirements

Submitted by

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Submission

1. Please provide your views on the proposal, including any objections or suggested revisions.

Background

The prudentials regime in the Wholesale Electricity Market (WEM) is designed to ensure that sufficient protection is provided to the market where a Market Participant may find itself in a default position where it cannot settle is Short Term Energy Market (STEM) or Non-STEM invoices on time. That is the prudentials regime attempts to mitigate against the risk of a short payment to Market Participants occurring. Consequently there are a number of safe guards for the market built into the current prudentials regime, including:

- Requiring a Credit Support of an amount sufficient to cover a Market Participants anticipated market exposure (Credit Limit) to be provided prior to competing in the WEM;

- Monitoring by the IMO of whether a Market Participants Outstanding Amount (aggregate of amounts payable to the IMO less amount to be paid to the participant by the IMO) is reaching the participant's Trading Limit (set as a ratio of 0.87 of the participants Credit Limit);

- Requiring Market Participants to provide additional Credit Support where its Trading Limit reaches zero (Margin Call) or alternatively setting the participants Credit Limit higher.

Proposed changes

The prudentials regime that currently applies in the WEM has not been changed since

- ***Typical Accrual and the amount of the Margin Call (Issue 5)***: The IMO proposes to remove the concept of Typical Accrual and directly link the IMO's determination of whether a Margin Call should be issued to the amount of Trading Margin at the time when the Margin Call is made. The IMO also proposes to require the IMO to re-determine a Credit Limit following a Margin Call being made and to ensure that any responses from a Market Participant (as required under the clause 2.42.2) are completed within 24 hours of the Margin Call being issued.

- ***Credit support arrangements (Issue 6 and 8)***: The IMO proposes clarifications to a number of the obligations for Market Participants relating to the provision of a Credit Support and Reserve Capacity Security including clarifying that:

    - All participants must provide a Credit Support, re than they can afford. Arguably without this incentive, as is created by ensuring that each approach (as is imbedded in the Market Rules) is inefficient, capital intensive and ultimately increases prices to end consumers (inconsistent with market objectives (a) and (d))[3]. Alinta notes that nowhere else in the Market Rules, including for the purposes of procuring sufficient capacity to cover the Reserve Capacity Target (which is acknowledged to be a conservative approach) is a level of 100% coverage prescribed.

Alinta does not support the IMO simply enshrining the existing approach into the Market Rules.

The proposal to change the amount of Prudential coverage in the Market from the second highest value in a given period to the highest value is a fundamental change to the principles underlying the amount of prudential risk that the market is prepared to bear. This change in principle has not been adequately supported by the IMO nor evidence provided which substantiates the claims made that the current process has "proven to be a robust, predictable and repeatable". Simply because the IMO has been unable to implement the previous approach prescribed in the rules is not sufficient rationale for the changes to be made. Alinta considers that the justification provided by the IMO to date is overly operational in nature and does not appropriately consider the broader market implications of the prudentials regime.

date and appears to be generally supported this is not apparent in the proposed Amending Rules put forward by the IMO.

Alinta also notes that clause 2.37.4 as proposed to be amended appears to cover any 70 day period which Alinta understands is not the intention (nor would Alinta support this if it was the intention). To cover any 70 day period would be mean that exposure during events such as Varanus Island would be potentially forever taken into account in setting a participants Credit Limit. While detail that the 70 day period is from the last 24 months is provided in the requests that the IMO amends this aspect of the proposal to make it optional for decreases in exposure to be notified to the IMO (and not subject to a civil penalty).

Issue 3: Guidelines for determining the expected value of a transaction

Alinta notes the IMO's issues with developing definition guidelines to calculate the expected value of a transaction and supports the IMO in proposing a set of factors to be taken into account when determining the expected value of a transaction, rather than guidelines.

Issue 4: Accounting for voluntary prepayments in the calculation of the Outstanding Amount

Alinta supports the IMO in better defining the current processes for accounting for voluntary prepayments from Market Participants who may be reaching their Trading Limit. In particular, the IMO proposes to amend the current calculation of the Outstanding Amount to take into account any prepayment amounts. Alinta agrees that these changes are necessary for reducing the financial risk to the market and providing greater assurance to participants that prepayments will apply immediately thereby ensuring their ability to continue trading in the market.

Issue 5: Typical Accrual and the amount of Margin Call

Alinta acknowledges the IMO's concerns that the concept of Typical Accrual is complex and may produce a more reliable estimate compared to the Outstanding Amount. Alinta is therefore supportive of the IMO's proposed amendments to remove the concept of Typical Accrual.

Alinta does not however support amending the rules to require additional credit to be provided within 24 hours where a Margin Call has been issued. The ability to provide additional monies through to the IMO in this circumstance is heavily reliant on banking cut off times and working days. For example, in the circumstances where a Margin Call is issued post pm ACST on a Friday or any time on a Saturday it is simply not possible to acquire additional monies by 24 hours later. Alinta strongly opposes this obligation being incorporated into the Market Rules given it will be impossible to ensure compliance.

Issue 6: Credit Support arrangements

Alinta notes that the rationale for the changes to clause 2.38.1 is not entirely clear. No case has been presented as to whas y .ount ana.297393425 0 Td 5 nhswtt the Acceptable Credit Criteria mst
101(r)-4.158 repeatedly clarifying that a Credit Support 32101(e)1.32101(739313.539(d 5)-4.77819(24.415(C)4.17943(r)-4.15
ause 2.38.4. Given that -276.679(a)1.32034(ny)10.576( )-113.538(s)-11.1761(i)4.47947(n)1.31968(g)-9.55639(l)4.47947(e)1

While Alinta considers it is unclear why an entity could not provide evidence to the IMO that it meets the Acceptable Credit Criteria rather than the relevant Market Participant. The intention of introducing this amendment into the rules originally was to enable financial institutes etc. to directly engage with the IMO to be included onto the list of entities. While this might not have occurred to date it is unclear why removing this ability is necessary or required. Alinta requests further details of the IMO’s rationale for this amendment.

Additionally Alinta notes that details of the obligations for monitoring the list of entities etc. are not currently provided in the Market Rules and requests clarity of what exactly the IMO intends to move from the rules into the Market Proc