

WHOLESALE ELECTRICITY MARKET

PROCEDURE CHANGE REPORT: AEPC_2019_03
REDUCTION OF THE PRUDENTIAL EXPOSURE IN THE
RESERVE CAPACITY MECHANISM

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EXECUTIVE SUMMARY

Purpose

Under clause 2.10.3 of the WEM Rules, if an Amending Rule requires AEMO to develop new Market Procedures or to amend or replace existing Market Procedures, then AEMO is responsible for the development, amendment, or replacement of Market Procedures so as to comply with the Amending Rule.

On 31 May 2018, the Rule Change Panel published its final decision on AEMO's Rule Change Proposal: Reduction of the prudential exposure in the Reserve Capacity Mechanism (RC_2017_06). A number of transitional clauses commenced on 1 August 2018, with the remainder of the Amending Rules due to commence on 1 June 2019.

On 18 March 2019, AEMO published the Procedure Change Proposal: Reduction of the Prudential Exposure in the Reserve Capacity Mechanism (AEPC_2019_03) to implement the changes resulting from RC_2017_06 to the following Market Procedures:

- Individual Reserve Capacity Requirements (IRCR);
- Capacity Credit Allocation; and
- Prudential Requirements.

The publication of this Procedure Change Report, and the accompanying Market Procedures, completes the Procedure Change Process conducted by AEMO under section 2.10 of the Wholesale Electricity Market Rules (WEM Rules).

Proposed amendments

These amendments to the WEM Rules introduced as part of RC_2017_06 were designed to address the identified shortfall of prudential support held as a result of the inadequate consideration of the IRCR related payments that would be owed on any given day.

The Procedure Change Proposal AEPC_2019_03 subsequently proposed to amend the Market Procedures as follows:

Market Procedure: Individual Reserve Capacity Requirements

This procedure is proposed to be amended to remove the concept of an initial IRCR in October, with an updated IRCR in every other Trading Month, and replace it with, for each Trading Month:

- the Indicative IRCR, calculated prior to the Trading Month;
- the IRCR, calculated prior to the initial Non-STEM Settlement Statement; and
- three adjustments to the IRCR, calculated as part of settlement adjustments.

Market Procedure: Capacity Credit Allocation

This procedure is proposed to be amended twice.

The first proposed amended procedure (version 3.0) will introduce transitional arrangements that will allow Rule Participants to perform any actions under the proposed new amended procedure (version 4.0) prior to version 4.0 of the procedure being effective, and, if they do this, they will be deemed to be compliant, where appropriate.

The second proposed amended procedure (version 4.0) will reflect the new Capacity Credit Allocation process in the WEM Rules effective from 1 June 2019. The new procedure provides information on the following processes:



- the new ability for Market Generators to make multiple Capacity Credit Allocations to multiple Market Customers in any Trading Month;
- reversing a Capacity Credit Allocation; and
- the methodology for AEMO to assess the Trading Margin of a:
 - Market Generator, when approving or rejecting a Capacity Credit Allocation Submission or Capacity Credit Allocation Acceptance; and
 - Market Customer, when reversing a Capacity Credit Allocation.

Market Procedure: Prudential Requirements

This procedure is proposed to be amended to:

- change the calculation of the Outstanding Amount to more accurately reflect a Market Participant's Capacity Credit Allocations, rather than projecting forward their Capacity Credit Allocations from the last issued Non-STEM Settlement Statement; and
- reflect AEMO's templates and process for Market Participants to provide Credit Support under a Security Deposit deed or corresponding Security Deposit direction.

Consultation

Draft versions of the proposed amended Market Procedures were presented at the 'AEMO WEM Procedure Change Working Group held on 21 February 2019. Details of this forum are available at: <http://aemo.com.au/Stakeholder-Consultation/Industry-forums-and-working-groups/WA-Forums/WEM-APCWG>. Minor changes were suggested, and the relevant procedures have been updated accordingly.

The RCP Secretariat did not convene a meeting of the Market Advisory Committee (MAC) regarding this Procedure Change Proposal. AEMO published the Procedure Change Proposal (AEPC_2019_03) and issued a notice calling for submissions on 18 March 2019.

The submission period closed on 15 April 2019. No submissions were received.

AEMO's decision

AEMO's decision is to accept the Market Procedures, as amended, following the consultation period.

AEMO considers that the revised Market Procedures are consistent with the Wholesale Market Objectives, the *Electricity Industry Act*, the WEM Regulations and the WEM Rules.

Next steps

The revised Market Procedures will commence as follows:

- Capacity Credit Allocation v3.0 will commence at 8:00 AM on 1 May 2019;
- Capacity Credit Allocation v4.0 will replace version 3.0 and commence at 8:00 AM on 1 June 2019;
- Individual Reserve Capacity Requirements will commence at 8:00 AM on 1 June 2019; and
- Prudential Requirements will commence at 8:00 AM on 27 June 2019.



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1. BACKGROUND

1.1. Regulatory requirements

1.1.1. Requirements for the Procedure Change Proposal

Under clause 2.10.3 of the WEM Rules, if an Amending Rule requires AEMO to develop new Market Procedures or to amend or replace existing Market Procedures, then AEMO is responsible for the development, amendment, or replacement of Market Procedures so as to comply with the Amending Rule.

Under clause 2.9.3 of the WEM Rules, Market Procedures:

- (a) must:
 - i. be developed, amended or replaced in accordance with the process in the WEM Rules;
 - ii. be consistent with the Wholesale Market Objectives; and
 - iii. be consistent with the WEM Rules, the *Electricity Industry Act* and the Regulations; and
- (b) may be amended or replaced in accordance with section 2.10 of the WEM Rules and must be amended or replaced in accordance with section 2.10 of the WEM Rules where a change is required to maintain consistency with Amending Rules.

AEMO has published this Procedure Change Report in accordance with the Procedure Change Process specified in section 2.10 of the WEM Rules.

The Procedure Change Proposal addresses the necessary consequential changes to AEMO's Market Procedures as required to be developed and progressed under clause 2.10.3 of the WEM Rules, specifically related to the Market Procedures:

- Individual Reserve Capacity Requirements (IRCR);
- Capacity Credit Allocation; and
- Prudential Requirements.

1.1.2. Requirements for proposed amended Market Procedures

Clause 4.28.12 of the WEM Rules provides the requirement for the Market Procedure: Individual Reserve Capacity Requirements:

4.28.12. AEMO must document the process to be followed in initially calculating, and subsequently revising, Individual Reserve Capacity Requirements in a Market Procedure, and AEMO and Market Customers must follow that documented Market Procedure.

The current version of the Market Procedure: Individual Reserve Capacity Requirements commenced on 3 November 2017.

Clause 9.4.3 of the WEM Rules provides the requirement for version 3.0 of the Market Procedure: Capacity Credit Allocation:

9.4.3. A Market Participant making a Capacity Credit Allocation Submission must provide to AEMO the information specified in clause 9.5.1 using the form prescribed by AEMO and the method prescribed in the Settlement Procedure.

The current version (version 2.0) of the Market Procedure: Capacity Credit Allocation commenced on 30 November 2015.



Clause 9.4.18 of the WEM Rules, to be introduced in the Rule Change Proposal: Reduction of the Prudential Exposure in the Reserve Capacity Mechanism (RC_2017_06) provides the requirement for version 4.0 of the Market Procedure: Capacity Credit Allocation:

9.4.18. AEMO must develop a Market Procedure dealing with:

- (a) Capacity Credit Allocations; and
- (b) other matters relating to sections 9.4, and 9.5.

This will replace version 3.0 of the procedure, which will commence on 1 May 2019.

Clause 2.43.1 of the WEM Rules provides the requirement for the Market Procedure: Prudential Requirements:

2.43.1. AEMO must develop a Market Procedure dealing with:

- (a) determining Credit Limits;
- (b) assessing persons against the Acceptable Credit Criteria;
- (c) Credit Support arrangements, including:
 - i. the form of acceptable guarantees and bank letters of credit;
 - ii. where and how it will hold cash deposits and how the costs and fees of holding cash deposits will be met;
 - iii. the application of monies drawn from Credit Support in respect of amounts owed by the relevant Market Participant to AEMO;
- (d) calculation of Trading Margins;
- (e) the list of factors to be taken into account for assessing the expected value of transactions;
- (f) issuing of Margin Calls; and
- (g) other matters relating to clauses 2.37 to 2.42,

and Market Participants and AEMO must comply with that Market Procedure.

The current version of the Market Procedure: Prudential Requirements commenced on 18 April 2017.

AEMO has developed and reviewed the proposed amended Market Procedures to ensure compliance with the relevant provisions in the *Electricity Industry Act*, WEM Regulations and WEM Rules (as in force and as proposed to be amended).

1.2. Context for this consultation

Under clause 2.10.3 of the WEM Rules, if an Amending Rule requires AEMO to develop new Market Procedures or to amend or replace existing Market Procedures, then AEMO is responsible for the development, amendment, or replacement of Market Procedures so as to comply with the Amending Rule.

On 31 May 2018, the Rule Change Panel published its final decision on AEMO's Rule Change Proposal: Reduction of the prudential exposure in the Reserve Capacity Mechanism (RC_2017_06). AEMO submitted the Rule Change Proposal on 17 July 2017 to address the identified shortfall of prudential support held as a result of the inadequate consideration of the IRCR related payments that would be owed on any given day.



The Rule Change Panel decided to implement the following changes:

- a change to the responsible party reference month¹ in the IRCR calculation from month n-3 to month n, so that Market Customers no longer incur IRCR liabilities for any future periods;
- amendments to the Capacity Credit Allocation process to allow Capacity Credit Allocations to be made by Market Generators and accepted by Market Customers prior to the Market Customers incurring the IRCR liability, where these Capacity Credit Allocations cannot be reversed by AEMO without consideration of the prudential implications; and
- consequential amendments to support the implementation of the proposed WEM Rule and Market Procedure changes.

The Rule Change Panel's final decision also implemented transitional provisions, which commenced on 1 August 2018, to allow the necessary actions to be undertaken with respect to the calculation of the Indicative IRCR, and the Capacity Credit Allocation process, under both the existing and new WEM Rules².

The remainder of the proposed Amending Rules come into effect on 1 June 2019.

The Procedure Change Proposal addresses the necessary consequential changes to AEMO's Market Procedures for IRCR, Capacity Credit Allocation and Prudential Requirements.

1.3. Procedure Change Process and timetable

On 18 March 2019, AEMO published a Procedure Change Proposal: Reduction of the Prudential Exposure in the Reserve Capacity Mechanism (AEPC_2019_03) and issued a call for submissions, which are available at: http://aemo.com.au/Stakeholder-Consultation/Consultations/AEPC_2019_03.

The proposal was progressed using the Procedure Change Process specified in section 2.10 of the WEM Rules, with submissions required by 15 April 2019.

2. PROCEDURE CHANGE PROPOSAL

2.1. Detail of the Procedure Change Proposal

The following sections provide an overview of the key changes that were made to each of the affected procedures.

2.1.1. Market Procedure: Individual Reserve Capacity Requirements

This procedure was proposed to be amended to remove the concept of an initial IRCR in October, with an updated IRCR in every other Trading Month and replace it with, for each Trading Month:

- the Indicative IRCR, calculated prior to the Trading Month;
- the IRCR, calculated prior to the initial Non-STEM Settlement Statement; and
- three adjustments to the IRCR, calculated as part of settlement adjustments.

AEMO proposed to commence the proposed amended Market Procedure on 1 June 2019 in line with the associated WEM Rules that will be effective for the June 2019 Trading Month.

¹ The responsible party reference month is the reference period used to allocate a meter's IRCR charges to a Market Customer. That is, the Market Customer(s) to which the meter is registered in the Meter Registry during the responsible party reference month will incur the IRCR charges for that meter.

² This will allow Market Participants to perform actions (and be deemed compliant) under both the old Capacity Credit Allocation Process, and the new Capacity Credit Allocation Process during May 2019. This transition is required to allow the necessary obligations to be met by all Rule Participants prior to the beginning of the June Trading Month from which the new process will apply.



2.1.2. Market Procedure: Capacity Credit Allocation

This procedure was proposed to be amended twice.

The first proposed amended procedure (version 3.0) will introduce transitional arrangements that will allow Rule Participants to perform any actions under the proposed new amended procedure (version 4) prior to the version 4 of the procedure being effective, and, if they do this, they will be deemed to be compliant where appropriate. This procedure will be effective from 1 May 2019 through to 1 June 2019.

The second proposed amended procedure (version 4.0) will reflect the new Capacity Credit Allocation process in the WEM Rules, effective from 1 June 2019. The new procedure provides information on the following processes:

- the new ability for Market Generators to make multiple Capacity Credit Allocations to multiple Market Customers in any Trading Month;
- reversing a Capacity Credit Allocation; and
- the methodology for AEMO to assess the Trading Margin of a:
 - Market Generator, when approving or rejecting a Capacity Credit Allocation Submission or Capacity Credit Allocation Acceptance; and
 - Market Customer, when reversing a Capacity Credit Allocation.

Version 4.0 of the procedure will replace version 3.0 and will commence on 1 June 2019 in line with the associated WEM Rules that will be effective from the June 2019 Trading Month onwards.

2.1.3. Market Procedure: Prudential Requirements

The procedure was proposed to be amended to:

- change the calculation of the Outstanding Amount to more accurately reflect a Market Participant's Capacity Credit Allocations, rather than projecting forward their Capacity Credit Allocations from the last issued Non-STEM Settlement Statement; and
- reflect AEMO's templates and process for Market Participants to provide Credit Support under a Security Deposit deed or corresponding Security Deposit direction.

AEMO proposed to commence the proposed amended Market Procedure on 27 June 2019 to change the Outstanding Amount calculation after the closure of the Capacity Credit Allocation Submissions for the June 2019 Trading Month.

2.2. Proposed drafting

AEMO published drafts of the proposed amended Market Procedures for IRCR, Capacity Credit Allocation (versions 3.0 and 4.0) and Prudential Requirements, incorporating the changes AEMO proposed, for consultation with stakeholders.

Clean and change-marked versions (for all procedures except version 4.0 of Market Procedure: Capacity Credit Allocation, which did not merit a change-marked version but instead contains consultation notes to assist stakeholders) are available at: http://aemo.com.au/Stakeholder-Consultation/Consultations/AEPC_2019_03.

AEMO also updated the IRCR and Capacity Credit Allocation procedures to use its current document template. Associated formatting changes were not change-marked.



3. CONSULTATION PROECESS

3.1. Market Advisory Committee or working group

The Market Advisory Committee (MAC) has delegated its advisory role with respect to AEMO Procedure Change Proposals to the AEMO Procedure Change Working Group (APCWG), in accordance with clause 2.3.17(a) of the WEM Rules.

Draft versions of the procedures were presented to the APCWG meeting held on 21 February 2019. Details of this forum are available at: <http://aemo.com.au/Stakeholder-Consultation/Industry-forums-and-working-groups/WA-Forums/WEM-APCWG>.

Market Participants from Kleenheat, Bluewaters, Perth Energy, Synergy and ERM Power attended the workshop and did not raise any material issues with the proposed amended procedures.

Market Participants suggested that more comprehensive feedback on the proposed amended procedures would be able to be provided though the consultation period, as it would allow the procedures to be tested against the relevant system changes. AEMO scheduled the consultation period in parallel with the scheduled system testing.

Minor changes were suggested and the relevant procedures were updated accordingly.

Since the meeting, and prior to consultation, AEMO made further minor and administrative updates to improve the procedures, and introduced transitional arrangements to allow participants to perform the necessary actions in relation to the Capacity Credit Allocation processes in May 2019, under both the Pre-Amending Rules and Post-Amending Rules. These procedural transitional arrangements were designed to align with those implemented by the Rule Change Panel in section 1.26 of the WEM Rules.

AEMO notified the Market Advisory Committee (MAC) when the Procedure Change Proposal was published and noted that the Rule Change Panel would convene a meeting of the MAC, in accordance with clause 2.10.9 of the WEM Rules, should two or more members request it. The Rule Change Panel did not convene a meeting of the MAC in relation to this Procedure Change Proposal.

3.2. Public workshop

No public workshops were held in relation to this Procedure Change Proposal.

3.3. Submissions received during consultation

AEMO published the Procedure Change Proposal (AEPC_2019_03) and issued a notice calling for submissions on 18 March 2019.

The submission period closed on 15 April 2019. No submissions were received.

4. AEMO'S ASSESSMENT

4.1. Further changes to the Market Procedures

Following the consultation process, AEMO has made a number of minor additional administrative amendments to each of the procedures as follows:



Market Procedure	Additional amendments
Individual Reserve Capacity Requirements	<ul style="list-style-type: none"> • Updates to section 1 of the procedure to reflect AEMO’s updated Market Procedure template and improve consistency of its procedures • Minor administrative amendments
Capacity Credit Allocation (version 3.0)	<ul style="list-style-type: none"> • Updates to section 1 of the procedure to reflect AEMO’s updated Market Procedure template and improve consistency of its procedures • Corrections to the mark-ups of the procedure by removing duplicated sections to accurately reflect the nature of the proposed changes • Minor administrative amendments
Capacity Credit Allocation (version 4.0)	<ul style="list-style-type: none"> • Updates to section 1 of the procedure to reflect AEMO’s updated Market Procedure template and improve consistency of its procedures • Minor administrative amendments
Prudential Requirements	<ul style="list-style-type: none"> • Updates to the procedure to reflect AEMO’s updated Market Procedure template and improve consistency of its procedures • Minor administrative amendments

Marked-up version distinguishing these amendments from those made prior to consultation are provided as Appendices 1, 3, 5 and 7 to this Procedure Change Report.

4.2. Consistency with *Electricity Industry Act*, WEM Regulations and WEM Rules

The revised procedures have been reviewed by AEMO to ensure compliance with the relevant provisions in the:

- *Electricity Industry Act*;
- WEM Regulations; and
- WEM Rules.

4.3. Consistency with Wholesale Market Objectives

The steps outlined in the proposed amended Market Procedures describe how Rule Participants will implement their obligations under the WEM Rules in relation to the calculation of IRCR, the Capacity Credit Allocation process, and meeting the prudential requirements in the WEM.

AEMO considers that the steps are drafted in a way that does not change the objectives of the WEM Rules. Moreover, they provide critical information about how each Rule Participant may meet its obligations under the WEM Rules, thereby increasing procedural transparency and certainty.



As a result, AEMO considers that the Market Procedures, as proposed to be amended, are consistent with the Wholesale Market Objectives as follows:

Market Procedure	Objectives met	Reason
Individual Reserve Capacity Requirements	Better meets (a) and (d) Consistent with all other objectives	The proposed amendments facilitate the reduction of: <ul style="list-style-type: none"> • credit risk in the WEM, which in turn reduces risk premium borne by consumers; and • the cross-subsidy, which in turn increases confidence in the effectiveness of the prudential regime, which could otherwise discourage participation in the market.
Capacity Credit Allocation (version 3.0)	Consistent with all objectives	The proposed amendments allow Market Participants to perform actions in relation to the old Capacity Credit Allocation process under the Pre-Amending Rules, as well as the new process under the Post-Amending Rules as per the Final Rule Change Report. This will allow the commencement of the new arrangements earlier than otherwise, and improve efficiency.
Capacity Credit Allocation (version 4.0)	Better meets (a) and (d) Consistent with all other objectives	The proposed amendments reduce the prudential risk and correctly account for the reduced risk, in relation to prudential requirements, through the changes proposed to the Capacity Credit Allocation process. This promotes economic efficiency and assists in minimising the long term cost of electricity supplied to consumers.
Prudential Requirements	Better meets (a), (b) and (d) Consistent with all other objectives	The proposed amendments ensure the adequate procurement of Credit Support, the absence of which would otherwise: <ul style="list-style-type: none"> • encourage business practices or structures for net Market Customers that are inefficient and unduly risky; and • potentially result in a substantial Default Levy that would need to be paid by other Market Participants, and that would eventually be passed onto consumers, without unduly tying up an excessive amount of capital in Credit Support.

4.4. Implementation

The Market Procedures were developed in accordance with the WEM Rules due to commence on 1 June 2019, including a number of transitional clauses that commenced on 1 August 2018.

The Market Procedures, as amended, do not require system changes by AEMO.

The Market Procedures, as amended, will not require Rule Participants to implement any procedural or system amendments before commencement.



Consequently, AEMO considers that the proposed commencement, on or after 1 May 2019, will allow Rule Participants sufficient time from the date of publication of this Procedure Change Report to ensure compliance.

4.5. AEMO's decision and commencement

AEMO's decision is to accept the Market Procedures, as amended, following the consultation period. The revised Market Procedures will commence as follows:

- Capacity Credit Allocation v3.0 will commence at 8:00 AM on 1 May 2019;
- Capacity Credit Allocation v4.0 will replace version 3.0 and commence at 8:00 AM on 1 June 2019;
- Individual Reserve Capacity Requirements will commence at 8:00 AM on 1 June 2019; and
- Prudential Requirements will commence at 8:00 AM on 27 June 2019.

AEMO has made this decision on the basis that the revised Market Procedures:

- are consistent with the Wholesale Market Objectives;
- are consistent with the *Electricity Industry Act*, WEM Regulations and WEM Rules; and
- did not elicit any submissions during the consultation period.