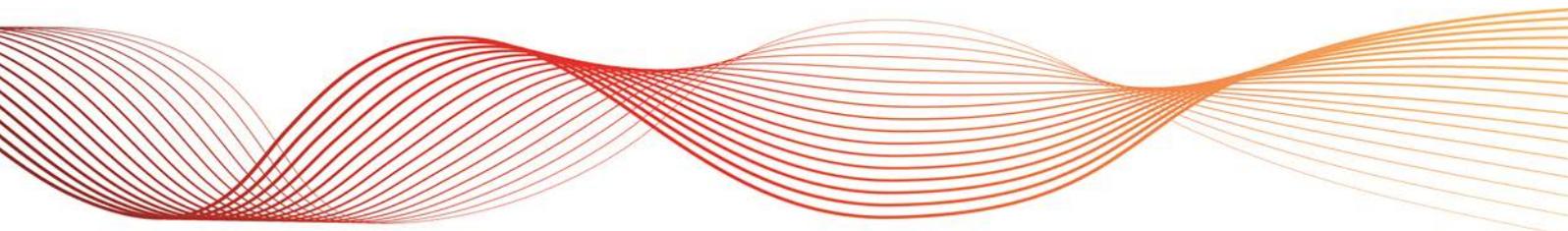




# NEM REALLOCATION PROCEDURES

ISSUES PAPER

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## EXECUTIVE SUMMARY

The publication of this Issues Paper commences the first stage of the Rules consultation process conducted by AEMO to consider proposed amendments to the *Reallocation Procedure: Swap and Option Offset Reallocations* and the *Reallocation Procedure: Energy and Dollar Offset Reallocations* (*Reallocation Procedures*) under the National Electricity Rules (NER).

On 23 February 2016 (effective 1 March), AEMO was granted a Clearing and Settlement (CS) Facility Exemption by the Minister under the Corporations Act. The CS Facility Exemption applies to *reallocations* to be applied under the *Reallocation Procedure: Swap and Option Offset Reallocations*. The CS Facility Exemption contains a number of mandatory operational conditions. This procedure therefore requires amendment in order to facilitate compliance with the conditions of the CS Facility Exemption.

In reviewing the procedure for swap and option offsets, AEMO identified a number of drafting corrections and potential improvements, which are also common to both *Reallocation Procedures*.

In summary, the key proposals involve:

- Amendments to the *Reallocation Procedure: Swap and Option Offset Reallocations* to facilitate compliance with the conditions of the CS Facility Exemption
- For both *Reallocation Procedures*:
  - Removal of the *reallocation timetable*, with the *timetable* to be established as a stand-alone document.
  - Reformatting, removal of unnecessary duplication of NER provisions, drafting changes to better reflect rules and procedural requirements, and updated references.

AEMO has prepared this Issues Paper to invite participants to review the proposed amendments to the *Reallocation Procedures*. AEMO asks stakeholders to identify any unintended adverse consequences of the proposed changes.

Stakeholders are invited to submit written responses on the issues and questions identified in this paper, and any other matter they consider relevant to the proposed amendments, **by 5.00 pm (Sydney time) on 20 September 2016**, in accordance with the Notice of First Stage of Consultation published with this paper.



# CONTENTS

<b>EXECUTIVE SUMMARY</b>	<b>1</b>
<b>1. STAKEHOLDER CONSULTATION PROCESS</b>	<b>3</b>
<b>2. BACKGROUND</b>	<b>3</b>
2.1 NER requirements	3
2.2 Context for this consultation	3
<b>3. DRAFTING FOR PROPOSED CHANGES</b>	<b>4</b>
3.1 <i>Reallocation Procedure: Swap and Option Offset Reallocations (SOOR Procedure)</i>	4
3.2 <i>Reallocations Procedure: Energy and Dollar Offset Reallocations (EDOR Procedure)</i>	6
3.3 <i>Reallocation Timetable</i>	7



# 1. STAKEHOLDER CONSULTATION PROCESS

As required by the NER, AEMO is consulting on proposed amendments to the *Reallocation Procedures*, comprising the *Reallocation Procedure: Swap and Option Offset Reallocations (SOOR Procedure)* and the *Reallocation Procedure: Energy and Dollar Offset Reallocations (EDOR Procedure)* in accordance with the Rules consultation procedures in rule 8.9.

AEMO’s indicative timeline for this consultation is outlined below. Dates may be adjusted depending on the number and complexity of issues raised in submissions and any meetings with stakeholders.

Deliverable	Indicative date
Issues Paper published	12 August 2016
Submissions due on Issues Paper	20 September 2016
Draft Report published	18 October 2016
Submissions due on Draft Report	4 November 2016
Final Report published	16 November 2016

Prior to the submissions due date, or in a submission on this Issues Paper, stakeholders can request a meeting with AEMO to discuss the proposed changes.

## 2. BACKGROUND

### 2.1 NER requirements

Under NER clause 3.15.11A, AEMO is responsible for developing and publishing the *Reallocation Procedures*, which may be amended or replaced from time to time. The *Reallocation Procedures* may be amended in accordance with the ‘rules consultation procedures’ set out in NER rule 8.9.

The *timetable* for *reallocation* requests (*Reallocation Timetable*) is to be published by AEMO under NER clause 3.15.11(d)(2).

### 2.2 Context for this consultation

The National Electricity Amendment (*Reallocations*) Rule 2007 No.1 commenced operation on 31 May 2007, and AEMO published the first *EDOR Procedure* in December 2007. A *reallocation* is a process under which two Market Participants ask AEMO to make matching debits and credits to the financial position of those market participants with AEMO. Market Participants can reduce their collateral requirements with AEMO by submitting *reallocations*.

Market Participants regularly enter financial agreements outside the NEM to manage their own financial risk and exposure to the potential volatility of the wholesale electricity price. *Reallocation transactions* provide a means by which those agreements can be used to effectively manage day to day exposure and reduce NEM credit support requirements.

The *SOOR Procedure* was developed in 2008 to offer an enhanced range of *reallocations*, underpinned by swap, cap, and floor agreements between Market Participants. This procedure could not be brought into effect at that time as AEMO would be considered to operate a clearing and settlement facility relating to financial products, which required appropriate authorisation under the *Corporations Act 2001*.

On 23 February 2016, AEMO was granted the CS Facility Exemption, which came into effect on 1 March 2016. The CS Facility Exemption contains a number of mandatory conditions and the *SOOR Procedure* requires amendment to facilitate compliance with them. Non-compliance by AEMO with these conditions will nullify the exemption.

As part of its review of the *Reallocation Procedures* review, AEMO has identified a number of corrections and additional amendments that it considers necessary or desirable for clarity and efficiency.

In particular, AEMO proposes to:

- Remove the provisions comprising the *Reallocation Timetable* from the *Reallocation Procedures* (section 6) and establish it as an independent document. A separate timetable is contemplated by NER clause 3.15.11(d) and would align the *Reallocation Timetable* with other timetables that AEMO publishes under the NER. This also means that, should changes be required to the *Reallocation Timetable* in the future, these can be implemented without the administrative cost of amending the *Reallocation Procedures*.
- Update the *Reallocation Procedures* to reflect AEMO's current template and format for procedures under the NER.
- Remove unnecessary repetition of provisions of the NER within the *Reallocation Procedures*.
- Make the deregistration request process clearer, specifying what must be contained in a request.

If, at the close of this consultation process, AEMO makes the amendments to the *SOOR Procedure* necessary to comply with the conditions of the CS Facility Exemption, an AEMO Electricity Market Management System improvement will be released to effect swap, cap, and floor *reallocations*.

## 3. DRAFTING FOR PROPOSED CHANGES

To help stakeholders and other interested parties respond to this Issues Paper, AEMO has published a draft of the *SOOR Procedure* and the *EDOR Procedure* incorporating the changes AEMO proposes for consultation, together with the proposed separate *Reallocation Timetable*. Clean and change-marked versions are available at: <http://www.aemo.com.au/Stakeholder-Consultation/Consultations>.

### 3.1 *Reallocation Procedure: Swap and Option Offset Reallocations (SOOR Procedure)*

This section lists the material amendments proposed to the *SOOR Procedure*. Minor variances have not been noted here, however the change-marked versions are available at:

<http://www.aemo.com.au/Stakeholder-Consultation/Consultations>.

- 1) Updated Format
  - Since the *Reallocation Procedures* were last revised, AEMO has updated its procedures template. Changes include formatting and numbering, and changes to the way in which introductory provisions are presented.
- 2) Effective Date
  - At the conclusion of this consultation process, an effective date will be assigned to the amended *SOOR Procedure*, and from that date Market Participants will be able to enter swap, cap, and floor *reallocation requests* in the AEMO Electricity Market Management System via the AEMO web browser.

### 3) 1.2.1 Glossary

- The term CS Facility Exemption has been added in reference to the Corporations (Australian Energy Market Operator Limited) CS Facility Exemption Notice 2016, made under section 820C of the *Corporations Act 2001* (Cth) on 23 February 2016.
- The terms *ex ante* timetable and *ex post* timetable have been removed and the *SOOR Procedure* refers directly to the *Reallocation Timetable* that is proposed to be established as a separate document.
- Amendments have been made to clarify definitions of the terms *ex ante reallocation*, *ex post reallocation*, *Participant ID*, and *Letter of Agreement*.

### 4) 1.4 Amendment

- The CS Facility Exemption requires AEMO to notify ASIC of proposed changes to the *SOOR Procedure*. Clause 1.4 therefore provides that any amendment to this procedure has no effect unless and until AEMO has complied with that conditions.

### 5) 2 Overview of *Reallocations*

- It is unnecessary to repeat the NER definitions of *reallocation* and *reallocation transaction*, therefore these have been removed.
- Additional drafting changes have been made to better reflect the nature of reallocation transactions.
- Reference to the maximum credit limit and prudential margin have been replaced with ‘prudential settings’, which also include the outstandings limit under NER clause 3.3.8.

### 6) 4 & Appendix A *Letter of Agreement*

- Participants must submit a correctly executed Letter of Agreement before they will be permitted to request swap, cap and floor *reallocations*. To meet the CS Facility Exemption conditions, AEMO proposes to make the Letter of Agreement in Appendix A specific to swap and option offset reallocations. Participants who wish to register reallocations under both *Reallocation Procedures* will need to execute a separate *Letter of Agreement* for each set of offset types.
- The *Letter of Agreement* for the *SOOR Procedure* has been amended to expand definitions and include participant eligibility criteria (also reflected in clause 4):
  - It is a condition of this *Letter of Agreement* that the Participant is registered under the NER as a Market Customer, Market Generator or Market Network Service Provider, and is a Wholesale Client.
  - The Participant represents and warrants to AEMO that it is, and will at all times during the term of this *Letter of Agreement* remain, a Wholesale Client.
  - If a Participant becomes aware that it will cease or has ceased to be a Wholesale Client, it must promptly notify AEMO in writing.
  - This Letter of Agreement terminates automatically on the date on which the Participant ceases to be either:
    - registered as a Market Customer, Market Generator or Market Network Service Provider; or
    - a Wholesale Client.
- The *Letter of Agreement* also includes participant acknowledgments of the information that AEMO may be required to give to ASIC as a condition of the CS Facility Exemption.

#### 7) 6 *Reallocations Timetable*

- This section has been largely removed. The *Reallocation Timetable* has been separated from the *Reallocation Procedures* and is intended to be established as an independent document. AEMO has published a draft *Reallocation Timetable* with this Issues Paper.

#### 8) 6 Prudentials

- This replaces section 6.2, item 3 of the existing *SOOR Procedure*, noting that *ex ante reallocations* registered in accordance with the *timetable* are considered in the calculation of prudential settings for a Market Participant. This provision now refers to the Credit Limit Procedures as posted on the AEMO website [www.aemo.com.au](http://www.aemo.com.au).

#### 9) 7.2 Deregistration

- The *reallocation transaction* deregistration process has been more clearly defined in the *SOOR Procedure* for Market Participants. Market Participants seeking to deregister *reallocation transactions* must submit their written request to AEMO containing the information now specified in the procedure, and requests must be received from both the credit and debit party to the *reallocation transaction*.

### 3.2 *Reallocations Procedure: Energy and Dollar Offset Reallocations (EDOR Procedure)*

This section lists the material amendments proposed to the *EDOR Procedure*. Minor variances have not been noted here, however the change-marked versions are available at:

<http://www.aemo.com.au/Stakeholder-Consultation/Consultations>.

#### 1) Updated Format

- Since the *Reallocation Procedures* were last revised, AEMO has updated its procedures template. Changes include formatting and numbering, and changes to the way in which introductory provisions are presented.

#### 2) 1.2.1 Glossary

- The terms *ex ante timetable* and *ex post timetable* have been removed and the *EDOR Procedure* refers directly to the *Reallocation Timetable* that is proposed to be established as a separate document.
- Amendments have been made to clarify definitions of the terms *ex ante reallocation*, *ex post reallocation*, *Participant ID* and *Letter of Agreement*.

#### 3) 2 Overview of *Reallocations*

- It is unnecessary to repeat the NER definitions of *reallocation* and *reallocation transaction*, therefore these have been removed.
- Additional drafting changes have been made to better reflect the nature of *reallocation transactions*.
- Reference to the maximum credit limit and prudential margin have been replaced with ‘*prudential settings*’, which also include the outstandings limit under NER clause 3.3.8.

#### 4) 4 & Appendix A *Letter of Agreement*

- Participants must submit a correctly executed *Letter of Agreement* before they will be permitted to request *energy* or *dollar offset reallocations*. The *Letter of Agreement* in Appendix A to the *EDOR Procedure* has been amended to specifically state and limit the *reallocation type* to *energy* or *dollar offset reallocations*.

### 5) 6 *Reallocations Timetable*

- This section has been largely removed. The *Reallocation Timetable* has been separated from the *Reallocation Procedures* and is intended to be established as an independent document. AEMO has published a draft *Reallocation Timetable* with this Issues Paper.

### 6) 6 Prudentials

- This replaces section 6.2, item 3 of the existing *SOOR Procedure*, noting that *ex ante reallocations* registered in accordance with the *timetable* are considered in the calculation of *prudential settings* for a Market Participant. This provision now refers to the Credit Limit Procedures as posted on the AEMO website [www.aemo.com.au](http://www.aemo.com.au)

### 7) 7.2 Deregistration

- The *reallocation transaction* deregistration process has been more clearly defined in the *EDOR Procedure* for Market Participants. Market Participants seeking to deregister *reallocation transactions* must submit their written request to AEMO containing the information now specified in the procedure, and requests must be received from both the credit and debit party to the *reallocation transaction*.

## 3.3 *Reallocation Timetable*

The *Reallocation Timetable* was previously located within each set of *Reallocation Procedures*. Use of *reallocations* is increasing among Market Participants. There are 78 Market Participants currently registered to use *reallocations*. In 2010, *reallocation transactions* were entered for 10% of all wholesale electricity purchased – in the current year of 2016 to date, *reallocation transactions* cover approximately 30% of all wholesale electricity purchased.

The *Reallocation Timetable* is a brief document and AEMO considers it would be more efficient to establish the *Reallocation Timetable* as an independent document that can be updated as required, without disturbing the *Reallocation Procedures*. A separate *timetable* is contemplated by NER clause 3.15.11(d).

AEMO has not proposed any changes to *reallocation* timings in the *Reallocation Timetable*, only clarification of definitions relating to *ex ante* and *ex post reallocations*. For any future changes to the *Reallocation Timetable*, AEMO would undertake Market Participant consultation through the appropriate consultative forum. It is anticipated that changes to the *Reallocation Timetable* may be required in order to implement the proposed 'Application of offsets in the prudential margin calculation' rule change, currently at the draft rule stage.