

## Draft Rule - Direct Retail Futures Offset Arrangement

The following Rule Changes will be required to implement and support FOAs:

### New National Electricity Rules

- 3.3.2B Futures Offset Arrangement Request
- 3.3.2C Preserved cash flows from Futures Offset Arrangements
- 3.3.2D Termination of Futures Offset Arrangements
- 3.15.11B Futures Offset Arrangements

### Amendments to existing National Electricity Rules

- 1.11 NEMMCO Rule funds
- 3.3.8 Maximum credit limit and prudential margin
- 3.3.8A Security Deposits
- 3.3.13 Response to Call Notices
- 3.15.1 Settlements management by NEMMCO

Schedule 3.3 - Principles for Determination of Maximum Credit Limits & Prudential Margins  
Chapter 10 Definitions

### **3.3.2B Futures Offset Arrangement Request [NEW RULE]**

- (a) A *Market Participant* may request *NEMMCO* to register a proposed *futures offset arrangement* ("a *futures offset arrangement request*") in accordance with the *futures offset arrangement rules*.
- (b) A *futures offset arrangement request* must set out the details of the proposed *futures offset arrangement* which includes:
  - (1) the term of the *futures offset arrangement*, including:
    - (i) the first day on which the arrangement is to take effect ("**the starting day**");
    - (ii) the last day that the arrangement is to be in effect ("**the termination day**");
  - (2) a confirmation in writing from a *SFE Clearing Participant* to *NEMMCO* that the *SFE Clearing Participant* holds futures contracts on behalf of the *Market Participant* or an entity controlled by or related to the *Market Participant* as specified in the *futures offset arrangement request*, in a volume greater than or equal to the quantity of futures contracts specified at subparagraph (iv);
  - (3) specification of the futures contracts nominated to become subject of the arrangement including:
    - (i) the *region* of futures contract;
    - (ii) the futures product code as referenced by the Sydney Futures Exchange;

- (iii) the futures contract term (specifying the time and date of the first half hour interval of energy and the time and date of the last half hour interval of energy encompassed by the term of the futures contract);
  - (iv) the quantity of futures contracts;
  - (v) the MWhs incorporated in one futures contract;
  - (vi) the futures contract cash settlement day;
  - (vii) the futures contract load shape (being either Base or Peak); and
  - (viii) the official Sydney Futures Exchange settlement price of the futures contract on the Sydney Futures Exchange business day immediately before the day the *futures offset arrangement request* is lodged with NEMMCO by the *Market Participant* ("**Futures Lodgement Price**"), quoted in \$/MWh.
- (c) NEMMCO must register a proposed *futures offset arrangement*:
- (1) within 1 hour of receipt of a *futures offset arrangement request* where such receipt occurs between 9 am to 4 pm on a *business day*;
  - (2) by 9 am on the next business day following the receipt of a *futures offset arrangement request* where such receipt occurs after 4 pm on a *business day*; or
  - (3) by 9 am on the same *business day* of receipt of a *futures offset arrangement request* where such receipt occurs before 9am of that same day.
- (d) NEMMCO must immediately inform the *Market Participant* of the registration of the *futures offset arrangement* under paragraph (c) including the confirming the details of the *futures offset arrangement* (being the details set out in paragraph (b)).
- (e) NEMMCO may impose conditions on the registration of a *futures offset arrangement* including requiring the *Market Participant* to procure from a *SFE Clearing Participant*, a daily confirmation to be provided to NEMMCO that the volume of relevant contracts held on behalf of the *Market Participant* or an entity controlled by or related to the *Market Participant* is no less than specified in the *futures offset arrangement request*.
- (f) A *Market Participant* who has registered a *futures offset arrangement* must pay NEMMCO monies equivalent to futures variation margins above the Futures Lodgement Price (as specified in the *futures offset arrangement request*) in accordance with clause 3.15.11B.

NB: Prescribes (a) the minimum balance of Security Deposit (SDA) for a *Market Participant* which is subject to a FOA. The clause is silent on how the FOA amount in the SDA will be used after the term of the futures offset arrangement has expired. NEMMCO would have the discretion to apply the money to billing period transactions.

**3.3.2C Preservation of security deposit from futures offset arrangements. [NEW RULE]**

During the term of a *futures offset arrangement* the *Market Participant* must retain an amount (in cash or other approved security) in the *Market Participant's* security deposit of no less than:

Max [(DSP<sub>t</sub> – FLP) x FQ, 0] where such terms are as defined in clause 3.15.11B [new],

unless otherwise agreed with NEMMCO.

Defines the notification procedure and obligations for early termination of FOA.
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### **3.3.2D Termination of Futures Offset Arrangements [NEW RULE]**

- (a) If a *default event* occurs in relation to the *Market Participant* which is a party to a *futures offset arrangement* prior to the termination day (as specified in the *futures offset arrangement request*), NEMMCO may terminate the *futures offset arrangement* by giving notice to the *Market Participant* at any time whilst the *default event* is subsisting. The termination is effective immediately from the receipt of the notice of termination by the *Market Participant*, notwithstanding that the *default event* may be subsequently cured.
- (b) NEMMCO may terminate a *futures offset arrangement* if the *Market Participant* breaches its *prudential support* obligations.
- (c) NEMMCO may terminate a *futures offset arrangement* if the *Market Participant* fails to comply with any conditions imposed by NEMMCO in respect of the *futures offset arrangement* at the time it was registered.
- (d) NEMMCO may terminate a *futures offset arrangement* at the request of the relevant *Market Participant*. NEMMCO may make such termination conditional upon the *Market Participant* meeting requirements specified by NEMMCO, including but not limited to NEMMCO being satisfied that the *Market Participant* will meet *prudential support* requirements upon termination of the *futures offset arrangement*.
- (e) In addition to any other right which NEMMCO may exercise in relation to a *default event*, upon termination of a *futures offset arrangement* NEMMCO may redetermine the *maximum credit limit*, *prudential factor* and *trading limit* for the *Market Participant* which was the subject of the *futures offset arrangement* having regard to the termination which has occurred.

### **3.15.11B Futures Offset Arrangements [NEW RULE]**

#### **Calculation methodology**

- (a) The *Market Participant* must pay the amounts calculated in accordance with paragraph (c) to NEMMCO on:
  - (1) the next SFE business day after the starting day (as specified in the *futures offset arrangement request*) ("**First Calculation Day**")
  - (2) each business day of the Sydney Futures Exchange ("**SFE business day**") other than the First Calculation Day that occurs during the term specified in the *futures offset arrangement request* but excludes days

after the last trading day of the relevant futures contract ("**Calculation Day**"); and

- (3) where the termination day of the *futures offset arrangement* (as referred to in the *futures offset arrangement request*) occurs after the last trading day of the relevant futures contract, the cash settlement day of the relevant futures contract after the last trading day of the relevant futures contract ("**Last Calculation Day**").

- (b) The amount payable by a *Market Participant* under paragraph (b) is as follows:

$$\text{Max} [(DSP_t - \text{Max} [DSP_{t-1}, \text{FLP}, DSP_h]) \times \text{FQ}, 0]$$

Where:

**FLP** means the Futures Lodgement Price as specified in the *futures offset arrangement request*;

**DSP<sub>h</sub>** means the previous highest Sydney Futures Exchange official daily settlement price that has occurred during the term of the *futures offset arrangement* as specified in the *futures offset arrangement request*;

**FQ** means the quantity of Futures Contracts multiplied by the MWhs incorporated in each Futures Contract; and

**DSP<sub>t</sub>** means:

- (1) for the First Calculation Day, the SFE official daily settlement price as at close of business on the starting day (as specified in the *futures offset arrangement request*) (unless the starting day is not an SFE business day, in which case DSP<sub>t</sub> means the SFE official daily settlement price as at close of business on the next SFE business day); and
- (2) for a Calculation Day, the SFE official daily settlement price immediately prior to the Calculation Day;
- (3) for a Last Calculation Day, the Sydney Futures Exchange official cash settlement price of the relevant futures contract;

**DSP<sub>t-1</sub>** means:

- (1) for the First Calculation Day, FLP;
- (2) for a Calculation Day, the most recent SFE official daily settlement price prior to DSP<sub>t</sub>;
- (3) for the Last Calculation Day, the Sydney Futures Exchange official daily settlement price as at close of business on the last exchange trading day of the relevant futures contract.

- (c) On a Calculation Day, NEMMCO may reset DSP<sub>h</sub> if:

- (1) DSP<sub>t</sub> < DSP<sub>h</sub>; and
- (2) the Market Participant has withdrawn funds or instructed NEMMCO in writing that it will withdraw funds from the Market Participant's Security Deposit thereby reducing the balance of the Security Deposit to  $\text{Max}[(DSP_t - \text{FLP}) \times \text{FQ}, 0]$

and in which case  $DSP_h$  will be reset on this Calculation Day to  $\text{Max} [DSP_t, \text{FLP}]$  and NEMMCO will inform the *Market Participant* of the new  $DSP_h$

#### **Form and Timing of payments to NEMMCO**

- (d) If a *Market Participant* is required to pay NEMMCO under this clause 3.15.11B, the *Market Participant* must pay NEMMCO by no later than 11 am on the relevant Calculation Day.
- (e) NEMMCO must deposit the money in its security deposit fund established in accordance with rule 1.11 in respect of the *Market Participant*.
- (f) NEMMCO will provide the *Market Participant* with a daily invoice detailing:
  - (1) any amount payable under the *futures offset arrangement*;
  - (2) the volume in MWh of the *futures offset arrangement*; and
  - (3) the relevant Sydney Futures Exchange official daily settlement prices (including FLP, DSPT-1, DSPT and DSPH) of futures contracts relevant to the *futures offset arrangement*,by 9:00 am on the relevant Calculation Day.

#### **Termination**

- (g) Upon termination of the *futures offset arrangement* by NEMMCO in accordance with 3.3.2D, the obligation for the *Market Participant* to make payments to NEMMCO in accordance with the *futures offset arrangement* will cease upon payment by the *Market Participant* to NEMMCO of all amounts owing in relation to Calculation Days up to and including the date of termination.

## Amendments to Existing National Electricity Rules

Note: new wording is denoted in underlined blue.

N.B: The amendments to clause 1.11 are to enable NEMMCO to use the security deposit fund to retain monies relating to FOAs.

### 1.11 NEMMCO Rule Funds [amended]

- (a) *NEMMCO* must continue to maintain, in the books of the corporation:
  - (1) the registration and administration fund;
  - (2) the security deposit fund; and
  - (3) any other fund which the *Rules* provide will be maintained in *NEMMCO's* books,(each a "*Rule fund*").
- (b) *NEMMCO* must ensure that there is paid into each *Rule fund*:
  - (1) in the case of the registration and administration fund, all amounts of *Participant fees* and *auction expense fees* and any other amounts payable under the *auction rules* or *SRD agreements* as *NEMMCO* considers necessary from time to time other than those which are to be paid into another *Rule fund*;
  - (2) in the case of the security deposit fund, amounts which are received by *NEMMCO* under clauses 3.3.8A, 3.3.13(a)(2) and 3.3.13(a)(3) and the future offset arrangement rules;
  - (3) in the case of a fund referred to in paragraph (a)(3):
    - (i) all amounts which are received by *NEMMCO* in connection with carrying out its functions or powers in relation to that fund;
    - (ii) all amounts of *Participant fees* which are received or recovered by *NEMMCO* which relate to *NEMMCO's* actual or budgeted costs and expenses for carrying out its functions or powers in relation to that fund; and
  - (4) in the case of each *Rule fund*, income from investment of money in the *Rule fund*.
- (c) In respect of the security deposit fund, *NEMMCO* must keep records, in respect of each individual *Market Participant*, of:
  - (1) security deposits made by that *Market Participant* and actual interest or other income earned on that *Market Participant's* payments to that fund which will be recorded as credits for that *Market Participant*;
  - (2) any application, or return to that *Market Participant*, of monies in the security deposit fund in accordance with clause 3.3.13A or the futures offset arrangement rules;

- (3) deductions for liabilities and expenses of the security deposit fund referable, or allocated, to that *Market Participant* which will be recorded as debits to that *Market Participant*; and
  - (4) the credit or debit balance for that *Market Participant*.
- (d) NEMMCO must ensure that money from each *Rule fund* is only applied in payment of:
- (1) in the case of the registration and administration fund, costs and expenses of NEMMCO carrying out its functions or powers:
    - (i) in relation to a fund referred to paragraph (a)(3) to the extent that such costs and expenses cannot be met from the money contained in that fund; or
    - (ii) other than those functions and powers referred to in subparagraph (i);
  - (2) in the case of the security deposit fund, monies owing to NEMMCO by a *Market Participant* or the return of monies to a *Market Participant* in accordance with clause 3.3.13A [and the futures offset arrangement rules](#);
  - (3) in the case of a fund referred to in paragraph (a)(3), costs and expenses of NEMMCO carrying out its functions or powers in relation to that fund; and
  - (4) in the case of each *Rule fund*:
    - (i) other than the security deposit fund, reimbursement to a *Registered Participant* or another *Rule fund* to make any necessary adjustment for any excess amounts which are paid as *Participant fees* as a result of any of NEMMCO's actual costs and expenses being less than the budgeted costs and expenses or as a result of the payment of any interim *Participant fees*; and
    - (ii) liabilities or expenses of the *Rule fund*.

### **3.3.8 Maximum credit limit and prudential margin [amended]**

- (b) The *maximum credit limit* for a *Market Participant* is a dollar amount determined by NEMMCO applying the principles set out in schedule 3.3, being an amount determined by NEMMCO on the basis of a *reasonable worst case* estimate of the aggregate payments for *trading amounts* (after *reallocation* [and futures offset arrangements](#)) to be made by the *Market Participant* to NEMMCO over a period of up to the *credit period* applicable to that *Market Participant*.
- (g) NEMMCO must notify the *Market Participant* of any determination or change under this clause 3.3.8 of that *Market Participant's maximum credit limit* or *prudential margin* (as the case may be) and, on request from that *Market Participant*, provide details of the basis for that determination or change, *including the trading, price, volatility, [prospective futures offset arrangement assumptions](#) and prospective reallocation assumptions and the average spot prices and ancillary service prices and average trading amounts*.

The amendments to the below clause has been amended to ensure that the Market Participant can provide NEMMCO money in relation to the security deposit for FOAs.

### **3.3.8A Security Deposits [amended]**

At any time, a *Market Participant* may provide a security deposit to NEMMCO with respect to:

(a) securing payment of any amount which may become payable in respect of a billing period; and

(b) in relation to a futures offset arrangement.

NB: 3.3.13 amended to enable Market Participants to lodge a *futures offset arrangement request* to meet Call Notices in a similar way in which NEMMCO reallocations may be applied for that purpose.

### **3.3.13 Response to Call Notices [amended]**

- (a) Subject to clause 3.3.13(b), where NEMMCO has given a *call notice* to a *Market Participant*, the *Market Participant* must before 11.00 am (Sydney time) on the next *business day* following the issue of the *call notice* either:
- (1) agree with NEMMCO to an increase in the *Market Participant's maximum credit limit* by an amount not less than the *call amount*, and provide to NEMMCO additional *credit support* where, by virtue of the increase in the *maximum credit limit*, the *Market Participant* no longer complies with its obligations under clause 3.3.5;
  - (2) (where clause 3.3.13(a)(1) is not satisfied) pay to NEMMCO in cleared funds a security deposit of an amount not less than the *call amount*;
  - (3) lodge either a *reallocation request* and/or futures offset arrangement request which would give rise to a reduction in the Outstandings of the Market Participant or both equal to an amount which is not less than the *call amount* and which is accepted by NEMMCO; or
  - (4) provide to NEMMCO any combination of clauses 3.3.13(a)(1), (2) and (3) such that the aggregate of the amount which can be drawn under the additional *credit support* provided and the amount of the security deposit paid and the amount of the *reallocation request* or futures offset arrangement request accepted by NEMMCO is not less than the *call amount*.
- (b) If NEMMCO gives a *call notice* to a *Market Participant* after noon (Sydney time), then NEMMCO is deemed to have given that *call notice* on the next *business day* for the purposes of this clause.

NB: 3.15.1 amended to include the facilitation of FOAs in billing and payments facilitation provided by NEMMCO.

### **3.15.1 Settlements management by NEMMCO [amended]**

- (a) NEMMCO must facilitate the billing and settlement of payments due in respect of *transactions and [futures offset arrangements](#)* under this Chapter 3, including:
- (1) *spot market transactions*;
  - (2) *reallocation transactions*; and
  - (3) ancillary services transactions under clause 3.15.6A.
- (b) NEMMCO must determine the Participant fees and the *Market Participants* must pay them to NEMMCO in accordance with the provisions of rule 2.11.

NB: Amendments to Schedule 3.3.1 to:

1. Introduce the consideration of FOAs within the Principles for Determination of Market Participant's MCL;
2. Define the calculation of the amount of MCL reduction created by FOAs. The MCL reduction is commensurate with the quantity, term and Lodgement Price of the relevant futures contracts in comparison to the volatility adjusted price assumption (adjusted for GST and Loss Factor) used by NEMMCO to calculate the MCL, before reallocations and FOAs. The residual MCL after reduction due to FOA cannot be less than the Prudential Margin in Schedule 3.3.2.

## **Schedule 3.3 - Principles for Determination of Maximum Credit Limits & Prudential Margins [amended]**

This schedule sets out the principles to be followed by NEMMCO in determining the *maximum credit limit* and *prudential margin* for a *Market Participant*.

### **Schedule 3.3.1 Principles for determining maximum credit limits**

- (a) The *maximum credit limit* should be set on the principle of imposing a guarantee of payment being made to NEMMCO to a level of a *reasonable worst case*.
- (b) When calculating the *maximum credit limit* NEMMCO should have regard to:
- (1) impartial objectivity rather than subjectivity, though it is recognised that some key parameters will need to be subjectively estimated from a limited amount of data - the estimation should be as impartial as possible;
  - (2) the average level and volatility of the *regional reference price* for the *region* for which the *maximum credit limit* is being calculated, comparable to the frequency of breaches of the *maximum credit limit*;
  - (3) the pattern of the quantity of electricity recorded in the *metering data* for the *Market Participant*;

- (4) the quantity and pattern of the *prospective reallocation* in the immediate future;
- (5) the correlation between the metered amounts of electricity and the *regional reference price*;
- (6) the length of the *credit period*, which is the number of days from the start of a *billing period* to the end of the *reaction period* taking into account:
  - (i) the length of the *billing period*;
  - (ii) the typical time from the end of the *billing period* to the day on which *settlement* for that *billing period* is due to be paid (the *payment period*);
  - (iii) any current written request from the *Market Participant* to NEMMCO for the *maximum credit limit* to be determined on a *payment period* taken, for the purposes of clause 3.3.8 and not otherwise, to be 14 days; and
  - (iv) the time from a *default event* to the suspension or other removal of the *defaulting Market Participant* from the *market*, being a period of up to 7 days (the *reaction period*);
- (7) the statistical distribution of accrued amounts that may be owed to NEMMCO; and
- (8) the degree of confidence that the *maximum credit limit* will be large enough to meet large defaults (i.e. the degree of reasonableness in a *reasonable worst case*).
- (9) reducing the maximum credit limit for the Market Participant that is subject to a futures offset arrangement that is commensurate with the quantity and the term of the futures contracts for the immediate future which are the subject of a futures offset arrangement and the difference between:
  - (i) the expected worst case volatility-adjusted price outcome assumed by NEMMCO for maximum credit limit calculation purposes in accordance with this schedule 3.3.1; and
  - (ii) the Futures Lodgement Price (as specified in the futures offset arrangement request) of the futures offset arrangement;

and which is calculated using the following methodology:

Max [(P<sub>R</sub> x VF<sub>R</sub> - FLP<sub>R</sub>) x FL<sub>R</sub> x T x LF<sub>R</sub> x (GST+1), 0] but limited such that the reduced maximum credit limit is never less than the prudential margin calculated in accordance with schedule 3.3.2 assuming nil futures offset arrangement

where for each futures offset arrangement:

FLP<sub>R</sub> represents the Futures Lodgement Price covering region R;

FL<sub>R</sub> represents the associated average daily energy of futures offset arrangement for the Market Participant where the offset is to be calculated with reference to the spot electricity price of region R.

$P_R$  represents NEMMCO's estimate of the average future pool price for each region R;

$VF_R$  is a volatility factor, which ensures that the maximum credit limit is not exceeded more than once in 48 months;

T is the number of days assumed in NEMMCO's maximum credit limit credit period which coincide with days in the term of the futures contracts which are the subject of the futures offset arrangement.

GST represents the applicable rate for the Goods and Services Tax;

$LF_R$  represents NEMMCO's estimate of the loss factor applicable across all participants for each region R.

- (c) As far as practicable, this schedule 3.3 must be read and construed as taking into account *market ancillary service transactions* for the calculation of the *maximum credit limit* for the relevant *Market Participant*.

### **Schedule 3.3.2 Principles for determining prudential margins**

NB: Amendment to Schedule 3.3.2 to recognise that schedule 3.3.1 ensures that under FOA, the reduced MCL cannot be less than the prudential margin without an FOA.

3.3.2(4) eliminates a doubling of credit support coverage of the reaction period for FOAs.

(4) the extent to which the Market Participant's futures offset arrangements overlap with the reaction period, the prudential margin will be taken to be zero.

## **Chapter 10 definitions**

### **futures offset arrangement**

A proposed future offset arrangement the subject of a futures offset arrangement request that is registered by NEMMCO under clause 3.3.2B.

### **futures offset arrangement request**

A request by a Market Participant to NEMMCO to register a futures offset arrangement in accordance with clause 3.3.2B.

### **futures offset arrangement rules**

Means clauses 3.3.2B to 3.3.2D and clause 3.15.11B.

### **SFE Clearing Participant**

Means a "Clearing Participant" under the Clearing Rules of the Sydney Futures Exchange Clearing Corporation Pty Limited as made and amended in accordance with the Corporations Act 2001 (Cwth)