



06 March 2009

Dr John Tamblyn (Chairman)  
Australian Energy Market Commission  
PO Box A2449  
SYDNEY SOUTH NSW 1235

Dear John

**Futures Offset Arrangement Rule Change Proposal 2008  
Submission to Draft Rule Determination (22<sup>nd</sup> January 2009)**

d-cyphaTrade has reviewed the Draft Rule Determination National Electricity Amendment (Futures Offset Arrangements (FOAs)) Rule 2009 of 22<sup>nd</sup> of January 2009 and has participated in the Expert Panel formed under the s.45 NER review initiated by the Commission. We note that the AEMC has acknowledged that the FOA proposal has merit. While d-cyphaTrade is pleased to provide ongoing technical input to the Review process and the wider scope of financial market and spot market issues covered by that Review, we believe that a simplified FOA draft Rule could now be effectively implemented by the AEMC under the current Rule change process. A "Direct Retailer FOA" model would address concerns raised in the Draft Rule Determination, is more efficient than the original FOA proposal and could be implemented under the current Rule Change process. Implementation via the current Rule Change process would avoid further delays in significant efficiency benefits flowing to Market Participants. d-cyphaTrade will provide a proposed draft Rule Change to implement Direct Retailer FOAs for the AEMC's consideration by 13<sup>th</sup> March 2009.

The Direct Retailer FOA model has been designed using input and suggestions made by members of the Expert Panel involved in the s.45 Review. The Direct Retailer FOA model addresses the following concerns raised in the Draft Determination:

1. Under the amended proposal, SFE Clearing Participants would not be a party to the FOA. Hence legal rights and obligations of the FOA parties (NEM Participants) are governed by the Rules. A condition of the FOA is that the Market Participant's SFE Clearing Participant must confirm the Market Participant's relevant futures position to NEMMCO daily.
2. The Direct Retailer FOA is between the Market Participant and NEMMCO and only NEMMCO can terminate an FOA. NEMMCO will not terminate an FOA at the Market Participant's request unless the Market Participant provides sufficient alternative credit support under the Rules. This addresses the issue of the termination risk (also referred to as non-firmness) of the original FOA proposal.
3. Direct Retailer FOA arrangements utilise existing payment arrangements and are unlikely to increase legal clawback risk (more detailed analysis will be included with d-cyphaTrade's subsequent submission).
4. Both parties to the Direct Retailer FOA (Market Participant and NEMMCO) are governed by the Rules, hence the dispute resolution process is governed by the Rules as well.
5. The Direct Retailer FOA does not (and nor did the original FOA proposal) permit interregional MCL offsets.
6. Our analysis (Annex 1) demonstrates that Direct Retailer FOAs would have retained a much higher MCL credit support for NEMMCO than under reallocation since 2005 (an average \$50.08/MWh of FOA bank guarantee support compared to \$17.35/MWh under reallocation) plus FOAs would have contributed additional Security Deposit protection which has been ignored in the analysis.

d-cyphaTrade shares the Commission's view that it is important to balance the prudential needs of generators and retailers whilst maintaining a sound and efficient prudential regime in line with the national electricity objective (NEO). The Direct Retailer FOA model would, as an alternative but complementary offset mechanism to reallocations, support the prudential regime of the NEM whilst



reducing the working capital cost to retailers and generators alike. Thus, we believe that the Direct Retailer FOA fulfils the national electricity objective.

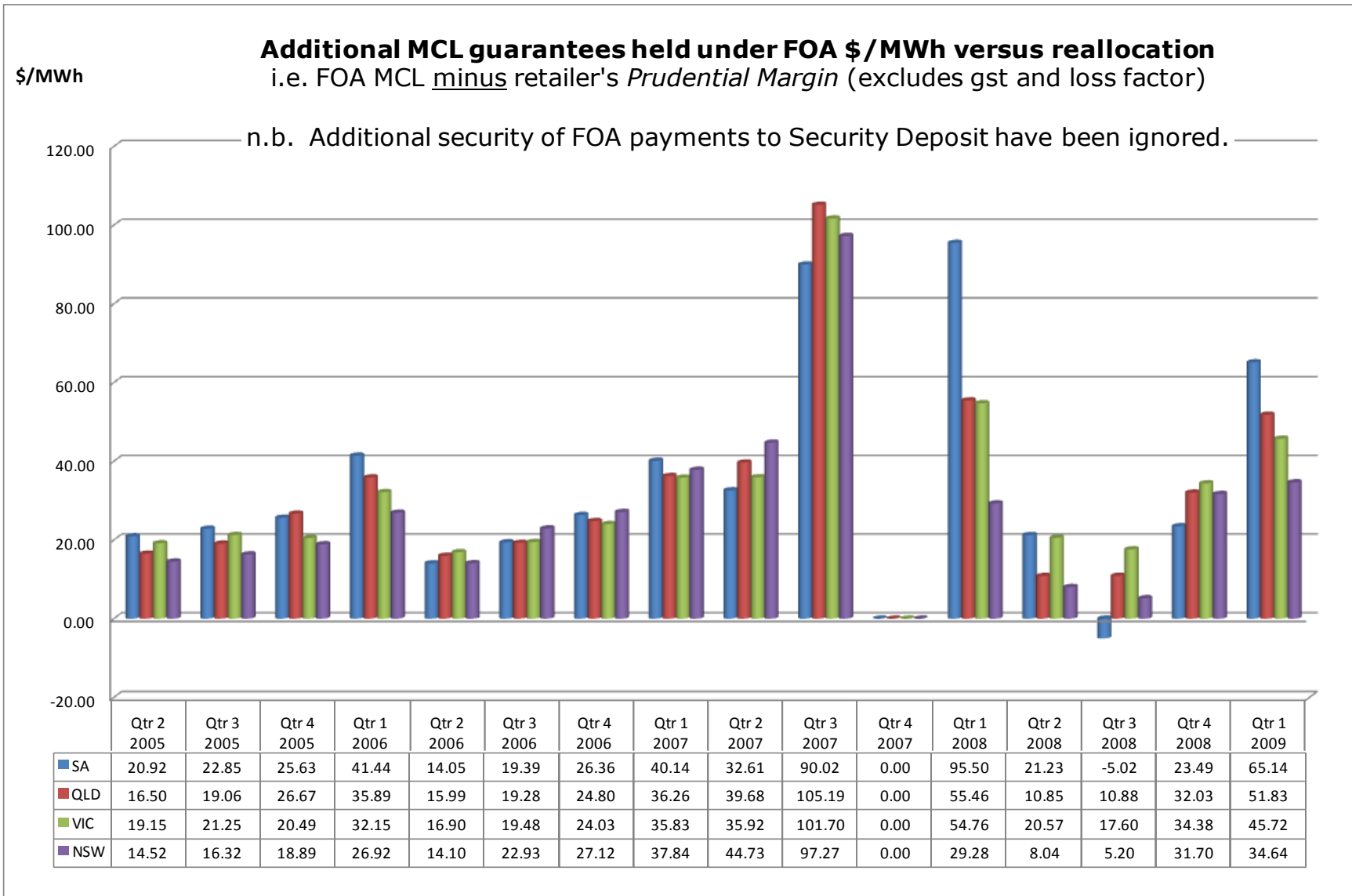
We therefore urge the AEMC to approve the Rule change consistent with the amendments which we will provide by 13<sup>th</sup> March 2009, to enable NEM Participants to benefit from cost savings delivered by FOAs as soon as is practical.

Yours sincerely,

A handwritten signature in black ink that reads "Dean Price".

Dean Price  
General Manager

**ANNEX 1**



Historically since Q2 2005, average FOA MCL protection would have exceeded reallocated retailer MCL (prudential Margin) by 188%.

i.e. Average MCL under FOA = \$50.08/MWh. Average MCL under ex ante reallocation (i.e. prudential Margin) = \$17.35/MWh.

Workings:

Current MCL expressed in \$/MWh (excludes GST and Loss Factor)											MCL data not available					
Region	Q2 2005	Q3 2005	Q4 2005	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Q1 2007	Q2 2007	Q3 2007	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
SA	66.47	65.39	65.20	63.38	103.19	93.65	93.86	89.17	83.35	89.91	N/A	116.98	144.12	\$283.64	\$282.05	\$278.15
QLD	60.00	50.64	51.48	42.66	69.05	59.85	60.60	55.42	79.94	88.85	N/A	170.34	173.39	\$160.32	\$125.85	\$125.50
VIC	42.01	42.00	42.05	33.58	66.57	77.52	80.80	77.51	88.97	97.78	N/A	151.44	149.60	\$143.42	\$56.24	\$55.65
NSW	98.90	102.20	105.64	106.37	107.38	91.90	94.39	69.96	54.09	124.38	N/A	229.30	220.28	\$214.82	\$49.83	\$78.64
<b>Reallocation Prudential Margin based on 7 days of 42 day MCL expressed in \$/MWh</b>																
Region	Q2 2005	Q3 2005	Q4 2005	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Q1 2007	Q2 2007	Q3 2007	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
SA	11.08	10.90	10.87	10.56	17.20	15.61	15.64	14.86	13.89	14.98	N/A	19.50	24.02	47.27	47.01	46.36
QLD	10.00	8.44	8.58	7.11	11.51	9.98	10.10	9.24	13.32	14.81	N/A	28.39	28.90	26.72	20.98	20.92
VIC	7.00	7.00	7.01	5.60	11.10	12.92	13.47	12.92	14.83	16.30	N/A	25.24	24.93	23.90	9.37	9.28
NSW	16.48	17.03	17.61	17.73	17.90	15.32	15.73	11.66	9.02	20.73	N/A	38.22	36.71	35.80	8.30	13.11
<b>Futures settlement price (1 day prior to QTR start) = MCL Bank Guarantees preserved under FOA.</b>																
Region	Q2 2005	Q3 2005	Q4 2005	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Q1 2007	Q2 2007	Q3 2007	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
SA	32	33.75	36.5	52	31.25	35	42	55	46.5	105	57	115	45.25	42.25	70.5	111.5
QLD	26.5	27.5	35.25	43	27.5	29.25	34.9	45.5	53	120	104	83.85	39.75	37.6	53	72.75
VIC	26.15	28.25	27.5	37.75	28	32.4	37.5	48.75	50.75	118	54	80	45.5	41.5	43.75	55
NSW	31	33.35	36.5	44.65	32	38.25	42.85	49.5	53.75	118	67	67.5	44.75	41	40	47.75
<b>FOA MCL exceedence over Reallocation Prudential Margin expressed in \$/MWh</b>																
Region	Q2 2005	Q3 2005	Q4 2005	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Q1 2007	Q2 2007	Q3 2007	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
SA	20.92	22.85	25.63	41.44	14.05	19.39	26.36	40.14	32.61	90.02	N/A	95.50	21.23	-5.02	23.49	65.14
QLD	16.50	19.06	26.67	35.89	15.99	19.28	24.80	36.26	39.68	105.19	N/A	55.46	10.85	10.88	32.03	51.83
VIC	19.15	21.25	20.49	32.15	16.90	19.48	24.03	35.83	35.92	101.70	N/A	54.76	20.57	17.60	34.38	45.72
NSW	14.52	16.32	18.89	26.92	14.10	22.93	27.12	37.84	44.73	97.27	N/A	29.28	8.04	5.20	31.70	34.64