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## Market Rule Amendment Submission

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This form is used to request an amendment to, or clarification of, the *Market Rules*. Please complete the first four parts of this form and submit the completed form by email or fax to the following:

Email Address: [Rule.Amendments@ieso.ca](mailto:Rule.Amendments@ieso.ca)

Fax No.: (416) 506-2847 Attention: Market Rules Group

**Subject: Market Rule Amendment Submission**

All information submitted in this process will be used by the *IESO* solely in support of its obligations under the *Electricity Act, 1998*, the *Ontario Energy Board Act, 1998*, the *Market Rules* and associated policies, standards and procedures and its licence. All submitted information will be assigned the *confidentiality classification* of “Public” upon receipt. You should be aware that the *IESO* will *publish this amendment submission* if the *Technical Panel* determines it warrants consideration and may invite public comment.

Terms and acronyms used in this Form that are italicized have the meanings ascribed thereto in Chapter 11 of the *Market Rules*.

### PART 1 – SUBMITTER’S INFORMATION

Please enter contact information in full.	
Name: <u>IESO Staff</u>	
(if applicable) <i>Market Participant / Metering Service Provider</i> No. <sup>1</sup> : <u>N/A</u>	<i>Market Participant Class</i> : <u>N/A</u>
Telephone: <u>905-403-6955</u>	Fax: _____
E-mail Address: <u>rule.amendments@ieso.ca</u>	

### PART 2 – MARKET RULE AMENDMENT SUBMISSION INFORMATION

Subject: <u>Market Administration</u>	
Title: <u>Revisions to the Suspension, Termination and Disconnection Provisions for Events of Default</u>	
Nature of Request (please indicate with x)	
<input checked="" type="checkbox"/> Alteration	<input type="checkbox"/> Deletion
<input type="checkbox"/> Addition	<input type="checkbox"/> Clarification
Chapter: <u>3</u> Appendix: _____ Sections: <u>6.3, 6.4, 6.5</u>	
Sub-sections proposed for amending/clarifying: <u>Various</u>	

<sup>1</sup> This number is a maximum of 12 characters and does not include any spaces or underscore.

### PART 3 – DESCRIPTION OF THE ISSUE

Provide a brief description of the issue and reason for the proposed amendment. If possible, provide a qualitative and quantitative assessment of the impacts of the issue on you and the *IESO-administered markets*. Include the Chapter and Section number of the relevant *market rules*.

#### **Background**

The market rules (sections 6.3, 6.4, 6.5 of Chapter 3) provide for the suspension and termination of a market participant and disconnection of a facility for financial events of default and for persistent breaches of the market rules. The recent insolvencies of two market participants exposed gaps in the market rules relating to suspension, termination and disconnection for events of default. Among other things, these gaps create a risk that the market may be required to “carry” a defaulting market participant for an extended period of time. The IESO is seeking to reduce this risk by streamlining the process and limiting or removing measures that duplicate legal protections available to a defaulting market participant outside of the market rules.

At its meeting on June 28, 2007 the IESO Board reviewed these issues and provided a preliminary policy direction that the IESO undertake stakeholder consultation on amendments to the market rules to address these gaps identified and bring forward these amendments to the IESO Board for its review and consideration later in 2007. The IESO Board also directed the IESO to establish predetermined criteria for those instances in which the IESO seeks to convert an existing market rule obligation (shall) into a market rules permission (may). This would provide greater transparency to market participants with respect to the IESO’s process for invoking that discretion.

#### **Shortcomings of the Current Rules**

The issues that the IESO is seeking to address include the following:

- *Clarifying the Relationship to Court Supervised Process:* In many cases, a market participant that commits an event of default will also be subject to, or on the verge of, a court-supervised process such as creditor protection or bankruptcy. In such cases, the court proceedings will take precedence over the market rules and the IESO will represent the interests of the IESO-administered markets in those proceedings. The current rules neither recognize the legal protections that the court process offers for the defaulting market participants nor the restrictions that it places on the IESO’s ability to deal with a defaulting market participation. For example, where a market participant is under court supervision, the IESO will be required to obtain leave of the court prior to taking any step in the disconnection process and may need to obtain leave on multiple occasions before completing the process.
- *Length and Complexity of the Current Process:* The default protection amount (DPA) used to calculate a market participant’s prudential support obligation is premised on the assumption that no more than 21 days will elapse between the date an event of default occurs and disconnection. Any shortfall between outstanding amounts owed by the defaulting participant and the available prudential support will be made by the imposition of a default levy on all market participants by the IESO. The current process may allow a market participant to extend the process longer than 21 days which exceeds the DPA thus exposing the market to an increased risk of the imposition of the default levy.
- *Disconnection of an Embedded Market Participant:* The IESO is currently only permitted to issue disconnection orders to transmitters and distributors. The market rules do not permit the IESO to issue disconnection orders to any other kind of market participant that is the “host” of an embedded market participant where the embedded participant has defaulted. For example, a

### PART 3 – DESCRIPTION OF THE ISSUE

wholesale customer may have a defaulting market participant embedded within or behind its facility. This is an issue because the defaulting embedded market participant would be able to continue to consume electricity thereby exposing the market to a risk of the imposition of a default levy. Although this has not happened to date in IESO-administered markets there is a possibility this might occur and therefore the IESO should be granted the authority necessary to order the disconnection of the defaulting market participant in this circumstance.

- *Disconnection of a “Host” Market Participant:* The current rules obligate the IESO when issuing a termination order to issue orders disconnecting the facilities of a defaulting market participant even if it is the “host” of an embedded market participant that is in good standing. Such a disconnection would deny the embedded market participant access to the IESO-Controlled Grid. The IESO should be provided flexibility under the market rules to not issue the termination order in this circumstance so that it may permit electricity consumption by the embedded non-defaulting market participant without exposing the IESO-administered markets to a risk of the imposition of the default levy.
- *Disconnection if a Risk to Public Safety:* The IESO is presently obligated to issue a disconnection order when terminating a market participant even if disconnection would create a risk to public or worker safety or result in environmental damage. While a transmitter or distributor in accordance with the market rules can refuse to carry out such an order if it would create a risk to public/worker safety or result in environmental damage, this discretion is not extended to the IESO. The IESO should not be placed in a position where it is compelled under the market rules to issue a disconnection order even though it knows that such action would endanger public/worker safety or damage the environment.
- *Interaction with the Obligations of Distributors:* Where a market participant is disconnected from the IESO-controlled grid, there is a risk in some cases that the participant is physically able and entitled to withdraw electricity through the distribution system because of the distributor’s obligation to serve under the Distribution System Code (DSC) and the *Electricity Act, 1998*. The market rules should acknowledge the primacy of these other regulatory obligations.
- *Other Changes:* Parts of sections 6.3, 6.4 and 6.5 are duplicative (*e.g.* sections 6.4.2 and 6.5.1) and there are some discrepancies between the different sections (*e.g.* a disconnection order for a suspended market participant can be issued to a transmitter under section 6.3.7B.4, while a disconnection order for a terminated market participant can be issued to a transmitter *or a distributor* under section 6.4.4A). Further, section 6.5 contains provisions concerning de-registration and termination for persistent breaches of the market rules. These provisions have been intertwined with the default rules and should be separated so that they are easier to understand.

#### **Hearing before the IESO Board**

As part of these amendments, the IESO is proposing to limit the ability of a market participant to seek a “show cause” hearing before the IESO Board for suspension and termination in cases of financial events of default. The IESO believes the hearing is unnecessary in light of other procedural protections available to a defaulting market participant. These include the court-supervised process in cases of creditor protection and bankruptcy, the exemption process for temporary relief from a requirement that a market participant is unable to satisfy, and the dispute resolution process to resolve disagreements over an amount owed by a market participant.

In addition, a market participant has a right to appeal to the OEB an order that “terminates, suspends or restricts the person’s rights to participate in the IESO-administered markets or to cause or permit

**PART 3 – DESCRIPTION OF THE ISSUE**

electricity to be conveyed into, through or out of the IESO-controlled grid” under paragraph 36(1)(c) of the *Electricity Act, 1998*.

In light of recent events, the IESO has become concerned that a defaulting market participant could use hearing process to prolong the disconnection process while continuing to draw electricity from the IESO-controlled grid thereby exposing the market to undue financial risk. Although to date this has been identified as a hypothetical risk since there has never been a “show cause” hearing before the IESO Board it is possible a market participant could prolong the process. The IESO believes this risk cannot be justified given the range of other procedural protections outlined above.

A hearing before the IESO Board will still be permitted for termination or de-registration resulting from a persistent breach of the market rules by a market participant.

**PART 4 – PROPOSAL (BY SUBMITTER)**

Provide your proposed amendment. If possible, provide suggested wording of proposed amendment.

In order to address the issues outlined above, it is proposed to replace section 6.3, 6.4 and 6.5 of Chapter 3 of the market rules with new provisions that will:

Clarify the relationship of the suspension, termination and disconnection process to the court process by:

- Providing the IESO with discretion not to issue a margin call to a defaulting market participant under creditor protection (currently required by section 5.2.8 of Chapter 2). Because margin calls are not enforceable against a party under court protection, the IESO needs the flexibility to use other mechanisms to protect the market that may be more appropriate under the circumstances (such as an agreement with the market participant for more frequent invoices or prepayments). This amendment will also ensure that issuing a margin call is not a condition precedent for proceeding with other aspects of the suspension proceedings. Consequential amendments to section 5.2.8 of Chapter 2 will be necessary to effect this change.
- Providing the IESO with the discretion not to demand additional prudential support from a defaulting market participant under creditor protection (currently required by 5.4.2 of Chapter 2) for the reasons set out in the preceding paragraph. Consequential amendments to section 5.4.2 of Chapter 2 will be necessary to effect this change.
- Eliminating the ability of a seller to backdate changes in physical bilateral contracts to a date prior to the occurrence of the event of default where the buyer is in default. This will ensure that the obligations of the buyer to the seller cannot be retroactively transferred to the market.
- Allocating any rebate payable to a defaulting market participant that has filed for creditor protection, including any rebate under section 4.8.2 of Chapter 9, against the market participant’s pre-filing arrears. While the decision on how to allocate a post-

**PART 4 – PROPOSAL (BY SUBMITTER)**

filing rebate is ultimately in the hands of the court, the proposed provision may strengthen the IESO's case for having it applied to pre-filing arrears.

Reduce the length and complexity of the current process by:

- Removing the obligation to issue a default notice to a market participant in circumstances where the default cannot be cured in the time required (*e.g.* where the participant has been wound up or a receiver, liquidator, trustee in bankruptcy, etc. has been appointed) and instead allow the IESO to move straight to suspension proceedings.
  - Streamlining the complexity of the current process and tightening the timelines to reduce the risk to the market from a defaulting market participant that seeks to prolong the disconnection process.
  - Limiting the ability of a market participant to seek a “show cause” hearing before the IESO Board for suspension and termination in cases of financial default in accordance with the preliminary policy direction of the IESO Board.
- Providing the IESO with authority to issue disconnection orders to any kind of market participant that is the “host” of an embedded market participant where the embedded participant has defaulted and obligate the host market participant to disconnect.
  - Granting the IESO greater discretion in deciding whether to issue a disconnection order where a market participant has been terminated by replacing the imperative “shall” in section 6.4.4A with the permissive “may”. The IESO would not issue the disconnection order when it would create a risk to public or worker safety or result in environmental damage or when it would impact an embedded market participant which is located behind the defaulting market participant.
  - Removing the obligation on the IESO to issue a disconnection order where disconnection would create a risk to worker/public safety or cause environmental damage.
  - Making the distributors’ obligation to disconnect an embedded market participant when so directed by the IESO subject to any other applicable laws and codes, such as the Distribution System Code.

Simplify and consolidate existing market rules by:

- Consolidating provisions of sections 6.3, 6.4 and 6.5 that are duplicative and eliminate inconsistencies.
- Separating the provisions of section 6.5 pertaining to de-registration and termination for persistent breaches of the market rules from the rules governing financial defaults and place them into a separate section where they can be more easily understood.

**PART 5 – FOR IESO USE ONLY**

*Technical Panel Decision on Rule Amendment Submission: Warrants Consideration*

MR Number: MR-00335

**PART 5 – FOR IESO USE ONLY**Date Submitted to *Technical Panel*: July 18, 2007Accepted by *Technical Panel* as: (please indicate with x)

Date:

 General       Urgent       MinorJuly 24, 2007

Criteria for Acceptance: It identifies ways to simplify the market and/or reduce participant or IESO costs. Amending the market rules to recognize both the legal protections that are afforded insolvent market participants during court-supervised processes and the restrictions that are applied to the IESO's ability to deal with a defaulting market participant under the existing market rules during those court-supervised processes will simplify the administration of the market. Additionally, amending the market rules to address gaps in the market rules relating to suspension, termination, and disconnection of market participants for events of default will reduce the risk of the application of the default levy to non-defaulting market participants thus reducing the likelihood of these potential market participant costs.

Priority: Medium.

Criteria for Assigning Priority: Pervasiveness of the problem. The potential application of the default levy to non-defaulting market participants due to the identified existing gaps in the market rules would impact all market participants who were active in the real-time market at the time of the default. To date, no market participant has been suspended or terminated from participation in the IESO-administered markets or had its facilities deregistered or disconnected from the IESO-controlled grid (other than voluntarily). Two market participants waived their entitlement to a show cause hearing before the IESO Board because of the court supervised process available to them. So while the impact may be significant, the probability is low.

Not Accepted (please indicate with x): Clarification/Interpretation Required (please indicate with x): *Technical Panel* Minutes Reference: IESOTP 204-1*Technical Panel* Comments: None