

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 *IMO-administered markets*. Include the Chapter and Section number of the relevant market rules.

The Technical Panel has identified that accepting cash to satisfy a prudential support obligation (“PSO”) is not a secure form of collateral and thus poses a financial risk to the electricity marketplace and its participants. Specifically, in the event of a bankruptcy of a market participant that provided cash to satisfy its PSO, the IMO could be forced to return the cash collateral to the bankrupt participant or its creditors. This could result in a default levy to the marketplace for the equivalent amount only if the bills remain unpaid. Furthermore, such other costs as legal and staff time would be incurred to attempt recovery of the cash. These costs would also be borne by all participants.

Currently, there are 28 participants posting \$13.2 million of cash collateral to satisfy a total PSO to the market of \$25.2 million (the difference is satisfied through other forms of acceptable). The IMO has spoken with each of the 28 participants asking specifically if they would be able to use an alternative means to satisfy their obligation. For the majority, a letter of credit or treasury bills would not be particularly difficult. However, approximately half the group cited that they would either not be able to post anything other than cash or that it would cause undue burden to them. Many of these participants are quite small (PSO under \$200,000) and they are not normally involved with sophisticated financial arrangements. For example, one participant’s PSO is \$418, and another’s is \$2,140. All of these factors were taken into consideration when developing solutions to mitigate the risk.

The IMO considered not accepting cash from any participant but eliminated this solution on the basis that it could be costly for the smaller MPs and that some would simply not be able to comply. The IMO also considered continuing to accept cash from all participants but would mitigate the risk by “perfecting” its security interest in the cash. This solution was investigated but was also eliminated due to the very significant administrative cost and burden for participants and the IMO. The final recommended solution blends some aspects of the two aforementioned alternatives arriving at a compromise that balances risk mitigation and the needs of certain participants.

The IMO recommends that it grandfather the existing rule that allows cash to be posted as collateral to **ONLY** those participants who are currently using cash as a means to satisfy their PSO **IF** their PSO is and remains \$200,000 or less. The \$200,000 level was chosen for three important reasons. The first being that it captures those participants that we believe would suffer undue burden and/or would not be able to comply with market rules that would not allow the use of cash. Secondly, the probability is very small that all participants within this group would become insolvent at the same time therefore should a default occur and the monies not be available to the IMO, the default levy would be limited to \$200,000 to be shared by all remaining participants. And finally, the aggregate exposure would be significantly **reduced and capped** at approximately \$1.3 million. Grandfathering to current cash users only allows the obvious benefit of not increasing the risk to the market in future years.

PART 4 – PROPOSAL (BY SUBMITTER)

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

In order to reduce the market risk associated with accepting cash as a means of meeting prudential support obligation, the market rules should be amended to only permit market participants that meet all of the following criteria to be able to provide cash to meet their prudential support obligation:

- The market participant currently provides cash to meet their prudential support obligation; and
- The market participant's prudential support obligation currently is, and remains in the future, less than or equal to \$200,000.

PART 5 – FOR IMO USE ONLY

Technical Panel Decision on Rule Amendment Submission	
MR number: MR-00280-Q00	
Date submitted to Technical Panel: August 24, 2004	
Accepted by Technical Panel as: <input checked="" type="checkbox"/> General <input type="checkbox"/> Urgent Minor (please indicate with X)	Date: August 24, 2004.
Criteria for acceptance: It identifies ways to simplify the market and/or reduce participant or IMO costs. In the event of a bankruptcy of a market participant that provided cash to satisfy its Prudential Support Obligation, this market rule amendment reduces the probability and the size of a default levy being applied to the marketplace.	
Priority: Medium	
Criteria for assigning priority: The pervasiveness of the problem. The implications of the IMO not being able to draw upon a cash deposit from a market participant in the event of a payment default by the participant potentially impacts all market participants because of an increasing risk of a need for the imposition of a default levy.	
Not accepted (please indicate with X):	
Clarification/interpretation required (please indicate with X):	
Technical Panel minutes reference: IMOTP 148-1	
Technical Panel Comments:	