

The background of the lower half of the page is a photograph of a wind farm and power lines, overlaid with a semi-transparent blue filter. On the left, several white wind turbines are visible, with their blades extending outwards. On the right, a tall, lattice-structured power transmission tower stands prominently. The overall scene is set against a clear sky.

Independent Market Operator

**Final Market Rule Change
Report:
Under Construction for the
Reserve Capacity Mechanism**

Ref: RC_2009_07

Date: 17 July 2009

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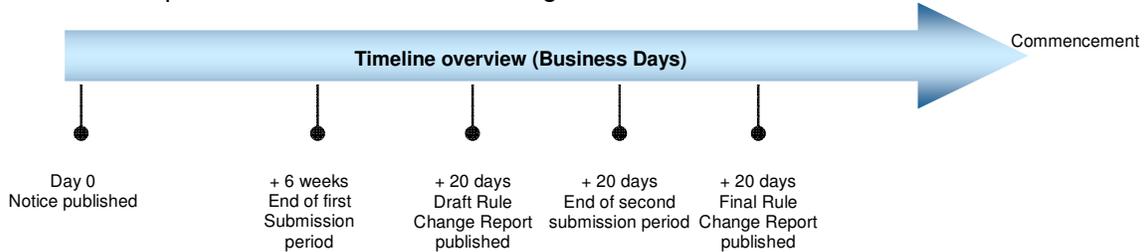


1. INTRODUCTION

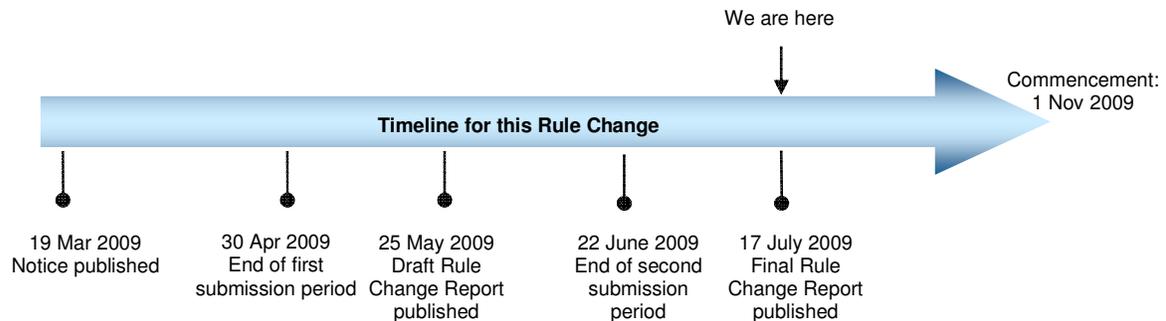
On 16 February 2009 System Management submitted a Rule Change Proposal regarding changes to clause 7.2.5 of the Wholesale Electricity Market Rules (Market Rules).

This Proposal was processed using the Standard Rule Change Process, described in section 2.7 of the Market Rules.

The standard process adheres to the following timelines:



The key dates in processing this Rule Change Proposal are:



The IMO's final decision is to accept the Rule Change Proposal. The detailed reasons for the IMO's decision are set out in section 6 of this report.

In making its final decision on the Rule Change Proposal, the IMO has taken into account:

- the Wholesale Market Objectives;
- the practicality and cost of implementing the proposal;
- the views of the Market Advisory Committee's (MAC); and
- the submissions received.

All documents related to this Rule Change Proposal can be found on the IMO website: http://www.imowa.com.au/Attachments/RuleChange/RuleChange_2009_07.html.

2. THE RULE CHANGE PROPOSAL

2.1 Submission Details

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Organisation:	IMO
Address:	Level 3, Governor Stirling Tower, 197 St George's Terrace
Date submitted:	17 March 2009
Urgency:	Standard Rule Change Process
Change Proposal title:	Under Construction for the Reserve Capacity Mechanism
Market Rule(s) affected:	4.2.7, 4.14.6 and Appendix 3

2.2 Details of the Proposal

In its proposal the IMO stated that a key objective for the Wholesale Electricity Market is to ensure that electricity is provided reliably as well as economically. This is a particularly significant issue in Western Australia because the electricity system is isolated and supplies cannot be drawn from neighbouring systems.

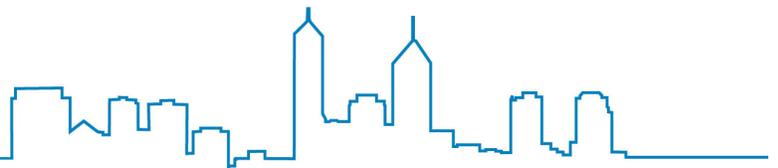
The IMO noted that reliability is achieved through the Reserve Capacity Mechanism (RCM). Where RCM is a set of processes through which the IMO determines the amount of generation and Demand Side Management (DSM) capacity required to meet future demand and facilitates the provision of this to the market.

The IMO contended that the reliability of the SWIS depends on generators and DSM providers actually delivering the capacity that they have offered. The IMO undertakes a process of certification thorough which it satisfies itself that, among other things:

- The Facility will be able to deliver the quantity of capacity that is being offered; and
- If the Facility is yet to enter service, that it will be able to supply power into the South West interconnected system (SWIS) by the date claimed.

The IMO stated that Facilities that are certified may apply to the IMO for Capacity Credits. The IMO assigns Capacity Credits following the priority rules set out in Appendix 3 of the Market Rules. In assigning Capacity Credits to Facilities under the RCM, the IMO must make a determination of the status of a Facility. The IMO stated that in the case of Facilities yet to enter service, a Facility may be in either *proposed* status or *under construction*. The IMO contends that it has been found that the term *under construction* may not be optimal or broad enough for the full range of projects being considered or may be considered in the future.

In its proposal the IMO considered that the term *under construction* implies the Facility is in the process of physically being constructed. Facilities with short lead times may be constructed within 12 - 18 months, for example, and would not be under construction two years in advance of the start of the relevant Capacity Year when the IMO assigns Capacity Credits.



The IMO gave another example of a Market Participant seeking Certified Reserve Capacity (CRC) and Capacity Credits for a Facility upgrade. The IMO contended that construction in this case is not necessarily required, only the ability for the relevant participant to complete the upgrade during planned maintenance periods. The IMO also contended that although these Facilities are fully *committed* at the time of application and in all other ways able to qualify for Capacity Credit assignment, a broader definition of this class is warranted.

The IMO proposed to amend the Market Rules and replace the word *under construction* with *committed*. The IMO states that the assessment criteria to enable the IMO to determine whether a Facility is *committed* will be included in the Market Procedure for Declaration of Bilateral Trades and the Reserve Capacity Auction. Given this it should still be noted that there are a number of factors the IMO will need to take into account when undertaking its assessment. The definition of *committed* (changes from the current definition of *under construction* are underlined) is proposed to be:

Factors which the IMO states will be taken into consideration when assessing whether a project is “committed” include:

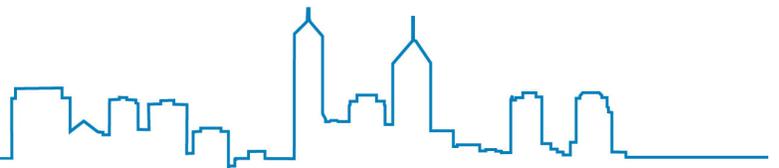
- *financial commitment by the Rule Participant to the primary equipment supplier. (This would usually take the form of a signed contract indicating purchase of the main plant equipment including penalty clauses associated with non-compliance of the purchase agreement).*
- *formal commitment, including financial approval, on behalf of the company in respect of the project, for example Board approval;*
- *details of planning, construction and environmental applications, approvals and licences;*
- *access to land either through ownership or an appropriate leasing agreement;*
- *a signed contract for civil works (or appropriate alternative), including contractual delivery times, which indicate the construction phase has started; and*
- *where a facility is being built primarily to supply energy to one or more foundation customers, evidence that relevant power supply contracts are in place.*

The IMO contended that the proposed changes will help to remove any uncertainty around the order which offers for Capacity Credits relating to these projects will be accepted in Appendix 3 of the Market Rules.

2.3 The Proposal and the Wholesale Market Objectives

The IMO submitted that the proposed changes, which replace the term “under construction” with “committed”, will support market objective (c) by allowing committed projects with lead times of under two years (for which construction has not begun at the time of application), for example small diesel generators, to be assigned Capacity Credits under step 2A in Appendix 3 of the Market Rules.

The IMO considered that the proposed changes are consistent with the other market objectives.



2.4 The Amending Rules Proposed by the IMO

The IMO proposed the following amendments to the Market Rules (~~deleted text~~, added text):

- 4.2.7. By the date and time specified in clause 4.1.6, the IMO must publish the following information:
- (a) the number of Expression of Interests received;
 - (b) based on the Expression of Interests, the additional Reserve Capacity potentially available, categorised as:
 - i. capacity associated with Facilities that are ~~under construction~~ committed; and
 - ii. capacity associated with Facilities that are yet to commence being constructed, where this capacity is to be further categorised between new Facilities for which:
 - 1. an offer by the relevant Network Operator to enter into an Arrangement for Access (“**Access Offer**”) has been made and all necessary Environmental Approvals granted;
 - 2. applications for both Access Offers and Environmental Approvals have been made and one or both are being processed;
 - 3. no Access Offer has been applied for or some or all Environmental Approvals have not been applied for;
- ...
- 4.14.6. If two or more Facilities cannot simultaneously exist (for example, because more than one Market Participant is proposing to build a Facility that will be located at the same site,) then the IMO cannot accept a non-zero value provided in accordance with clause 4.14.1(c) in respect of more than one of these Facilities and must reject all but one Facility based on the following criteria:
- (a) Facilities that are operational or are ~~under construction~~ committed will be accepted ahead of other Facilities; then
 - (b) if more than one Facility remains, then Facilities that can demonstrate having secured financing will be accepted ahead of other Facilities; then
 - (c) if more than one Facility remains, then Facilities with the greatest quantity of Certified Reserve Capacity will be accepted ahead of Facilities with lower Certified Reserve Capacity; then

...

Appendix 3: Reserve Capacity Auction & Trade Methodology

...

The algorithm is as follows:

Step 1: Start with $a = 1$

Step 2: Let the set of active offers comprise all offers from Availability Class “a”.

Step 2A: In the case of bilateral trade offers, accept offers from operating facilities and committed facilities ~~under construction~~ and remove them from the set of active offers.

Step 3: Accept offers from the set of active offers in order of

- In the case of testing bilateral schedules, decreasing availability.
- In the case of the reserve capacity auction, increasing price

until the capacity requirements of Availability Class “a” are fully covered or until there are no offers left unaccepted in the set of active offers.

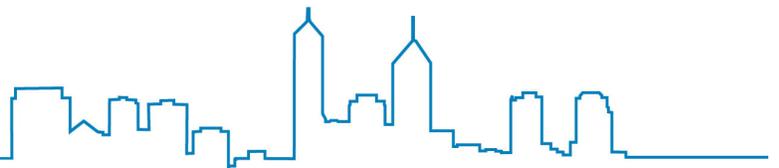
Where two or more offers are tied with respect to the selection criteria such that accepting all but one of them would result in the total capacity selected exceeding the total capacity requirement of the Availability Class then the tied offers are to be accepted according to the following rules until the tie is resolved.

- In the case of the reserve capacity auction, offers from operating facilities and committed facilities ~~under construction~~ are to be accepted ahead of facilities that are not committed ~~yet to commence construction~~; then
- Offers are to be accepted in decreasing order of capacity offered; then
- Offers for capacity that was included in an Expression of Interest are to be accepted ahead of capacity that was not; then
- Offers are to be accepted in the order of the time the offers were received, with the earlier offer being taken first; and then
- Offers are to be accepted in the order the capacity secured Certified Reserve Capacity;

...

Step 11: End.

In the case of the auction only:



- While leaving the Reserve Capacity Price unchanged, the IMO must exchange one or more offers not accepted for one or more offers accepted in the auction if
 - the total capacity scheduled in the auction exceeds the Reserve Capacity Auction Requirement by more than 100 MW;
 - the Reserve Capacity Price exceeds zero,
 - the exchange produces the maximum possible reduction in the total value of offers accepted;
 - the exchange does not create an overall Reserve Capacity shortfall where none existed;
 - in the event that a capacity shortfall exists in one or more Availability Classes, the exchange will not shift a shortfall from an Availability Class with low availability to an Availability Class with high availability; and
 - this would not result in an existing facility, or a committed facility ~~under construction~~ being excluded.

2.5 The IMO's Initial Assessment of the Proposal

The IMO decided to proceed with the proposal on the basis of its preliminary assessment, which indicated that the proposal was consistent with the Wholesale Market Objectives.

3. FIRST SUBMISSION PERIOD

The first submission period for this Rule Change Proposal was between 19 March 2009 and 30 April 2009.

3.1 Submissions received

The IMO received submissions on the Rule Change Proposal from Alinta, Landfill Gas & Power (LGP), Perth Energy and Verve Energy during the first submission period.

The details of the submissions received during the first submission period are summarised below. The full text of the submission is available on the IMO Market Web Site.

3.1.1 Submission from Alinta

Alinta supported the Rule Change Proposal on the grounds that will remove the implicit discrimination against Facilities and capacity expansions with short lead times (i.e. not needing to be physically under construction two years in advance of the start of the relevant Capacity Year) in the Market Rules.



Alinta suggested a possible change to the proposed clause 4.2.7(b) ii of the proposed Amending Rules to replace “*yet to commence being constructed*” with “*not committed*”.

The Rule Change Proposal and the Wholesale Market Objectives

Alinta supported the Rule Change Proposal on the grounds that it is likely to be consistent with market objectives (a), (b), (c) and (d), and it is not likely to be inconsistent with market objective (e).

3.1.2 Submission from Landfill Gas and Power

LGP supported the Rule Change Proposal on the grounds that requiring facility “commitment” as a pre-condition for the allocation of capacity credits is more reasonable and appropriate than requiring the facility be “under construction”.

The Rule Change Proposal and the Wholesale Market Objectives

LGP supported the IMO’s contention that the rule change promotes market objective (c) (*to avoid discrimination in that market against particular energy options and Technologies*) and is otherwise consistent with the other objectives.

Further, LGP considered that market objective (a) (*to promote the economically efficient, safe and reliable production and supply of Electricity*) is enhanced as the Rule Change Proposal. As LGP contends this removes the requirement that financiers would otherwise have to accept unnecessarily increased risk via the fact that they must start constructing a project that, at the point of commencement, does not actually create Capacity Credits.

3.1.3 Submission from Perth Energy

Perth Energy supported the Rule Change Proposal on the grounds that the process of developing a new project has many stages and a developer will have made very substantial commitments well before construction actually takes place. Perth Energy also supported the IMO’s contention that some projects take considerably less than two years so construction may not have commenced at the time that certification and Capacity Credits are sought and that this is particularly true for gas turbine, small renewable and plant upgrades.

Perth Energy anticipated that there may be some disagreement over what constitutes a Facility being “*committed*” and as every project is different, that the IMO will need some leeway to make its own determination on whether a project is really committed or not.

Perth Energy suggested a possible change for consistency to in clause 4.2.7(b) of the proposed Amending Rules to replace “*yet to commence being constructed*” with “*not yet committed*”.

3.1.2 Submission from Verve Energy

Verve Energy supported the Rule Change Proposal on the grounds that the present rule favours long lead time plant that is “*under construction*” compared to short lead time plant that may be as equally committed. Verve Energy contended that the proposed changes will reduce this discrimination.



The Rule Change Proposal and the Wholesale Market Objectives

Verve Energy supported the IMO's contention that the Rule Change Proposal will help with the achievement of market objective (c).

3.3 Public Forums and Workshops

No public forums or workshops were held in relation to this Rule Change Proposal.

3.4 Additional Amendments

As a result of submissions received during the first submission period the IMO has decided to make further changes to the Amending Rules. The changes to clause 4.2.7(b) and Appendix 3 are as follows (added text, ~~deleted text~~):

- 4.2.7. By the date and time specified in clause 4.1.6, the IMO must publish the following information:
- (a) the number of Expression of Interests received;
 - (b) based on the Expression of Interests, the additional Reserve Capacity potentially available, categorised as:
 - i. capacity associated with Facilities that are committed; and
 - ii. capacity associated with Facilities that are not yet committed yet to commence being constructed, where this capacity is to be further categorised between new Facilities for which:
 - 1. an offer by the relevant Network Operator to enter into an Arrangement for Access ("**Access Offer**") has been made and all necessary Environmental Approvals granted;
 - 2. applications for both Access Offers and Environmental Approvals have been made and one or both are being processed;
 - 3. no Access Offer has been applied for or some or all Environmental Approvals have not been applied for;

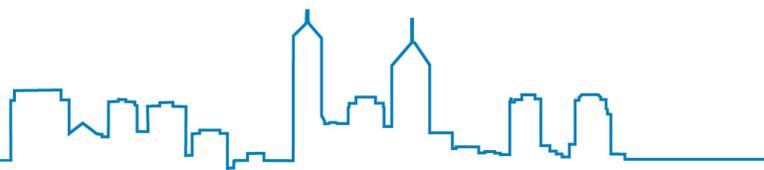
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Appendix 3: Reserve Capacity Auction & Trade Methodology

Step 3: ...

...

Where two or more offers are tied with respect to the selection criteria such that accepting all but one of them would result in the total capacity selected exceeding the total capacity



requirement of the Availability Class then the tied offers are to be accepted according to the following rules until the tie is resolved.

- In the case of the reserve capacity auction, offers from operating facilities and committed facilities are to be accepted ahead of facilities that are not yet committed; then
- Offers are to be accepted in decreasing order of capacity offered; then
- Offers for capacity that was included in an Expression of Interest are to be accepted ahead of capacity that was not; then
- Offers are to be accepted in the order of the time the offers were received, with the earlier offer being taken first; and then
- Offers are to be accepted in the order the capacity secured Certified Reserve Capacity;

4. THE IMO'S DRAFT ASSESSMENT

The IMO's draft assessment, as contained in its Draft Rule Change Report can be viewed on the IMO's website.

5. THE IMO'S DRAFT DECISION

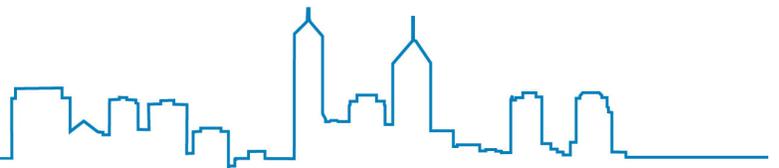
Based on the matters set out in the Draft Rule Change Report, the IMO's draft decision, in accordance with clause 2.7.7(f) was to accept the proposed amendments to clauses 4.2.7, 4.14.6 and Appendix 3 of the Market Rules as proposed in the Rule Change Proposal and amended following the first submission period.

The IMO has made its decision on the following basis:

- The Amending Rules:
 - Will allow the Market Rules to better address Wholesale Market Objective (c);
 - Are consistent with the remaining Wholesale Market Objectives;
 - Have no identified costs associated with the implementation; and
 - Have the support of both the MAC and all participants providing submissions during the first submission period.

6. SECOND SUBMISSION PERIOD

Following the publication of the Draft Rule Change Report on the IMO website, the second submission period was between 26 May 2009 and 22 June 2009.



The IMO received a formal submission from Aviva Corporation (Aviva) during the second submission period. The submission is summarised below, with the full text available on the IMO website.

6.1 Submission from Aviva Corporation

Aviva considers that this Rule Change Proposal is a sensible amendment given that in the real world of project development, construction always follows financial commitment. Aviva contended that the commitment decision by project sponsors (and associated lenders in most cases) is the key event which triggers a 'Notice to Proceed' to begin construction.

Aviva contends that the proposal complements the current Rule Change Proposal to introduce the concept of Early Certified Reserve Capacity (RC_2009_10), which allows the IMO to assess whether a project is committed well before the usual capacity cycle and at the same time gives certainty to the project sponsors that the plant will receive capacity credits.

Aviva also supports the consequential amendment proposed by Alinta to amend clause 4.2.7(b)(ii). Aviva considered that this would retain consistency for the definition of "committed" throughout the Market Rules.

The proposed rule change will not result in any increased costs for Aviva.

The Rule Change Proposal and the Wholesale Market Objectives

Aviva considered the proposed rule change is consistent with all the market objectives.

7. THE IMO'S FINAL ASSESSMENT

In preparing its Final Rule Change Report, the IMO must assess the Rule Change Proposal in light of clauses 2.4.2 and 2.4.3 of the Market Rules.

Market Rule 2.4.2 outlines that the IMO "*must not make Amending Rules unless it is satisfied that the Market Rules, as proposed to be amended or replaced, are consistent with the Wholesale Market Objectives*".

Additionally, clause 2.4.3 states, when deciding whether to make Amending Rules, the IMO must have regard to the following:

- Any applicable policy direction from the Minister regarding the development of the market;
- The practicality and cost of implementing the proposal;
- The views expressed in submissions and by the MAC; and
- Any technical studies that the IMO considers necessary to assist in assessing the Rule Change Proposal.

The IMO notes that there has not been any applicable policy direction from the Minister in respect of this Rule Change Proposal and that no technical studies have been determined necessary to assist in assessing the Rule Change Proposal.

The IMO’s assessment is outlined in the following sections.

7.1 Market Objectives

The IMO considers that the Market Rules as a whole, if amended, will be consistent with the Wholesale Market Objectives.

Wholesale Market Objective	Consistent with objective
(a) to promote the economically efficient, safe and reliable production and supply of electricity and electricity related services in the South West interconnected system	Yes
(b) to encourage competition among generators and retailers in the South West interconnected system, including by facilitating efficient entry of new competitors	Yes
(c) to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions	Yes
(d) to minimise the long-term cost of electricity supplied to customers from the South West interconnected system	Yes
(e) to encourage the taking of measures to manage the amount of electricity used and when it is used	Yes

Further, the IMO considers that the Market Rules if amended would not only be consistent with the Wholesale Market Objectives but also allow the Market Rules to better address Wholesale Market Objective (c):

Impact	Wholesale Market Objectives
Allow the Market Rules to better address objective	c,
Consistent with objective	b, c, d, e

The IMO’s assessment against market objective (c) is as follows:

(c) to avoid discrimination in that market against particular energy options and technologies, including sustainable energy options and technologies such as those that make use of renewable resources or that reduce overall greenhouse gas emissions

The IMO contends that by replacing the term *under construction* with *committed*, the proposal will allow committed projects with lead times of under two years (for which construction has not begun at the time of application) for example small diesel generators, to be assigned Capacity Credits under step 2A in Appendix 3 of the Market Rules.



7.2 Practicality and cost of implementation

The proposed changes will require changes to the IMO IT systems. It has been estimated that the associated changes to Wholesale Electricity Market Systems operated by the IMO will cost approximately AUD \$6,000.

To supplement this Rule Change Proposal, the IMO is also required to amend the Market Procedure for “Declaration of Bilateral Trades and the Reserve Capacity Auction” to include the assessment criteria to enable the IMO to determine whether a Facility is *committed*.

7.3 Views expressed in submissions

During the first submission period submissions were received from Alinta, LGP, Perth Energy and Verve Energy. The proposed Amending Rules had the support of all parties, however both Alinta and Perth Energy recommended further changes to the Amending Rules to replace “yet to commence being constructed” with “not committed” (Alinta) or “not yet committed” (Perth Energy).

The IMO agreed with this recommendation and amended the proposed Amending Rules accordingly.

During the second submission period, a submission was received from Aviva supporting the Rule Change Proposal. In this submission Aviva also supported the modification to the Amending Rules (clause 4.2.7(b)(ii)) proposed by Alinta. Aviva contended that this would retain consistency for the definition of “committed” throughout the Market Rules.

7.4 Views expressed by the Market Advisory Committee

The MAC was advised of the proposed rule change at its meeting on 11 March 2009. At the meeting the MAC unanimously agreed for the pre rule change proposal to be progressed as a rule change.

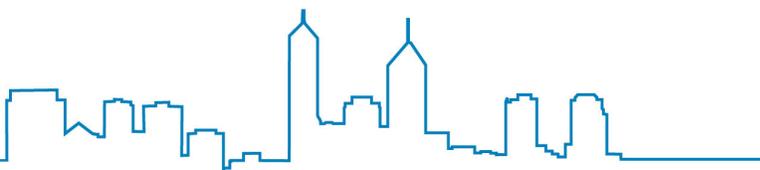
8. THE IMO'S FINAL DECISION

The IMO's final decision is to accept the proposed amendments to clauses 4.2.7, 4.14.6 and Appendix 3 of the Market Rules as proposed in the Draft Rule Change Report along with the additional amendments proposed to clause 4.2.7(b) and Appendix 3 in section 3.4 of this report.

8.1 Reasons for the decision

The IMO has made its decision on the following basis:

- The Amending Rules:
 - will allow the Market Rules to better address Wholesale Market Objective (a);
 - are consistent with the remaining Wholesale Market Objectives;



- have the support of the MAC;
- address the issues raised during the first submission period; and
- were supported in both submission periods (albeit with minor improvements).

Additional detail outlining the analysis behind the IMO's reasons is outlined in section 7 of this Final Rule Change Report.

9. AMENDING RULES

8.1 Commencement

The amendments to the Market Rules resulting from this Rule Change Proposal will commence at **8:00am** on **1 November 2009**.

8.2 Amending Rules

The following clauses are amended (~~deleted text~~, new text):

- 4.2.7. By the date and time specified in clause 4.1.6, the IMO must publish the following information:
- (a) the number of Expression of Interests received;
 - (b) based on the Expression of Interests, the additional Reserve Capacity potentially available, categorised as:
 - i. capacity associated with Facilities that are ~~under construction~~ committed; and
 - ii. capacity associated with Facilities that are not yet committed ~~yet to commence being constructed~~, where this capacity is to be further categorised between new Facilities for which:
 - 1. an offer by the relevant Network Operator to enter into an Arrangement for Access ("**Access Offer**") has been made and all necessary Environmental Approvals granted;
 - 2. applications for both Access Offers and Environmental Approvals have been made and one or both are being processed;
 - 3. no Access Offer has been applied for or some or all Environmental Approvals have not been applied for;

...

4.14.6. If two or more Facilities cannot simultaneously exist (for example, because more than one Market Participant is proposing to build a Facility that will be located at the same site,) then the IMO cannot accept a non-zero value provided in accordance with clause 4.14.1(c) in respect of more than one of these Facilities and must reject all but one Facility based on the following criteria:

- (a) Facilities that are operational or are ~~under construction~~ committed will be accepted ahead of other Facilities; then
- (b) if more than one Facility remains, then Facilities that can demonstrate having secured financing will be accepted ahead of other Facilities; then
- (c) if more than one Facility remains, then Facilities with the greatest quantity of Certified Reserve Capacity will be accepted ahead of Facilities with lower Certified Reserve Capacity; then

...

Appendix 3: Reserve Capacity Auction & Trade Methodology

...

The algorithm is as follows:

Step 1: Start with a = 1

Step 2: Let the set of active offers comprise all offers from Availability Class “a”.

Step 2A: In the case of bilateral trade offers, accept offers from operating facilities and committed facilities ~~under construction~~ and remove them from the set of active offers.

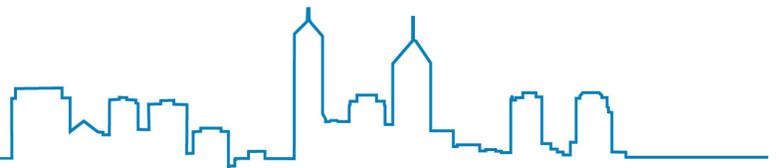
Step 3: Accept offers from the set of active offers in order of

- In the case of testing bilateral schedules, decreasing availability.
- In the case of the reserve capacity auction, increasing price

until the capacity requirements of Availability Class “a” are fully covered or until there are no offers left unaccepted in the set of active offers.

Where two or more offers are tied with respect to the selection criteria such that accepting all but one of them would result in the total capacity selected exceeding the total capacity requirement of the Availability Class then the tied offers are to be accepted according to the following rules until the tie is resolved.

- In the case of the reserve capacity auction, offers from operating facilities and committed facilities ~~under construction~~ are to be accepted ahead of facilities that are not yet committed ~~yet to commence construction~~; then



- Offers are to be accepted in decreasing order of capacity offered; then
- Offers for capacity that was included in an Expression of Interest are to be accepted ahead of capacity that was not; then
- Offers are to be accepted in the order of the time the offers were received, with the earlier offer being taken first; and then
- Offers are to be accepted in the order the capacity secured Certified Reserve Capacity;

...

Step 11: End.

In the case of the auction only:

- While leaving the Reserve Capacity Price unchanged, the IMO must exchange one or more offers not accepted for one or more offers accepted in the auction if
 - the total capacity scheduled in the auction exceeds the Reserve Capacity Auction Requirement by more than 100 MW;
 - the Reserve Capacity Price exceeds zero,
 - the exchange produces the maximum possible reduction in the total value of offers accepted;
 - the exchange does not create an overall Reserve Capacity shortfall where none existed;
 - in the event that a capacity shortfall exists in one or more Availability Classes, the exchange will not shift a shortfall from an Availability Class with low availability to an Availability Class with high availability; and
 - this would not result in an existing facility, or a committed facility ~~under construction~~ being excluded.