IN THE MATTER OF

the *Alberta Utilities Commission Act,* S.A. 2007, c. A-37.2

And

IN THE MATTER OF an Application

By the

Market Surveillance Administrator *("MSA")*

Involving

TransAlta Energy Marketing Corp.

("TransAlta")

Reply Argument of the MSA

April 4, 2012

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INDEX

Reply Argument of the MSA

I. Introduction

1. This Reply Argument (the "Reply") contains the response of the Market Surveillance Administrator ("MSA") to the arguments of the Alberta Direct Connect Consumer Association ("ADC"), the Utilities Consumer Advocate ("UCA") and Industrial Powers Consumers Association of Alberta ("IPCAA") dated March 28, 2012. Collectively the ADC, UCA and IPCAA will be referred to as the "Interveners". In addition to responding to the Interveners the MSA also wishes to comment briefly on one aspect of the argument submitted on behalf of TransAlta.

2. To the extent that this Reply is silent on an issue where one or more of the Interveners takes a position contrary to that set out in the MSA's March 28, 2012 Argument, the MSA's silence is not a sign of agreement with the Intervener. Rather the silence is because the MSA is satisfied that the issue was sufficiently covered in the MSA's Argument and that it is not necessary or appropriate to repeat its position.

3. The MSA appreciates the support for the settlement by the UCA, while recognizing that the UCA has some concerns with approach and process. These concerns will be addressed along with the arguments of ADC and IPCAA. Due to the overlap in positions of the Interveners the MSA will address the issues raised by the Interveners by subject, rather than by party. The key topics arising out of the Intervener Arguments that the MSA wishes to address are:

    - Benefits of settlement;
    - Appropriateness of the proposed settlement;
    - MSA consultation with Interveners during investigations and negotiations; and
    - Exclusion of an amount on account of costs in the settlement.

II. Response to TransAlta

5. In paragraphs 36 and 37 of its argument TransAlta states:

> *36. In the March 14, 2012 hearing, the Commission explored what guidance this case and the Commission's pending decision upon it might provide to the wider market. While that is a reasonable focus for the Commission, it is also a difficult matter in the particular circumstances of this case.*
>
> *37. No AESO market Rule was broken, and the MSA's evidence is that this is not a matter that could be addressed by amendments to such Rules (3T505). MSA Guidelines are themselves neither a Rule nor otherwise of legal force, but rather provide views of the MSA as to how the MSA might interpret broadly stated FEOC obligations in specific circumstances. Indeed, the relevant OBEG Guideline was itself in a state of being created through consultation at the time, and did not become final until January 14, 2011 (3T498), being some time after TransAlta both engaged in and then stopped the actions that led to the Settlement Agreement.*

6. In the submission of the MSA, when the Commission considers these two paragraphs and the associated breach of Section 6 of the *Electric Utilities Act*, (the "EUA") and Section 2 of the *Fair, Efficient and Open Competition Regulation* (the "FEOC Regulation"), the Commission must put them in the context of the Agreed Statement of Facts set out in the Application in Appendix 1, and paragraphs 27 and 28 thereof in particular. Both paragraphs are set out below for the convenience of the Commission:

> *27. The Parties agree that:*
>
> *(a) the timing of the export e-tags created by TransAlta was such that it was not reasonably possible for another market participant to then schedule an import to utilize the incremental ATC;*
>
> *(b) the export e-tags could have been created by TransAlta earlier, if it chose to do so;*
>
> *(c) TransAlta was aware that the timing of the export e-tags would likely restrict or prevent the ability of another market participant to utilize the incremental import ATC resulting from the TransAlta export; and*

(d) TransAlta was aware that other market participants were or would likely be seeking to schedule the import of electric energy into Alberta, given the arbitrage opportunity.

28. The MSA alleges, and TransAlta does not contest, that in each of the 31 hours involved in the Events:

(a) the inability of such imports to reach the market restricted competition and competitive response;

(b) TransAlta expected to derive an economic benefit from the timing of the export e-tags, in that the absence of a subsequent import could result in a higher pool price in Alberta than would have existed if a market participant had successfully imported and thereby counter-flowed the TransAlta export; and

(c) the fidelity of the Alberta market was affected by the conduct involved in the Events, specifically that to the extent the pool price was higher than it would otherwise have been, it affected both sellers and buyers in the market.

III. Benefits of settlement

7. The MSA submits that the submissions of ADC and IPCAA have ignored or failed to give sufficient weight to the value of a settlement over a litigated proceeding, in the face of breach of the EUA and the FEOC Regulation. The MSA submits that the value of a settlement is significant and must be taken into account in the Commission's consideration of this matter.

8. Settlements bring matters to a rapid conclusion and ensure that the market as a whole knows very quickly what conduct is considered wrong and what the consequences of such conduct may be. Continued investigation and litigation, which may take years, is not nearly as expeditious in achieving these important goals.

9. Settlements also encourage behaviour that is considered positively in AUC Rule 013, "Administrative Penalties", with respect to self reporting and cooperation. Settlements send a message to other market participants that matters can be dealt with fairly and quickly and that there is a meaningful alternative to protracted litigation. This also encourages market

participants who may engage in future violations to self-report and to comply with enforcement actions. This, in turn, reduces public expense and ensures that MSA, AUC and market participant resources are spent efficiently and effectively.

I. Appropriateness of the Proposed Penalty

(a) "Deterrence" and the preservation of market integrity

4. Both the ADC and the IPCAA argue that the penalty imposed on TransAlta must be sufficient to serve as a deterrent for any future misconduct.[1] The MSA agrees with this in principle and reiterates the submissions in its March 28th Argument that the quantum of penalty proposed for TransAlta is sufficient to deter both TransAlta and other market participants from engaging in similarly undesirable conduct in the future.[2]

5. IPCAA further argues that any manipulation in the real-time spot market will undermine consumer confidence in the entire system and that the MSA should expect customers to be concerned with the overall health of the marketplace.[3] In response, the MSA submits that the penalty imposed on TransAlta sends a strong statement to TransAlta, to other market participants, and to the general public, that TransAlta's conduct was unlawful, and most importantly will not be tolerated, but will be dealt with expeditiously and will be penalized. This should serve to boost, rather than undermine, market participant confidence in the system.

(b) Retribution

6. The ADC argues that "[t]he proposed Settlement Agreement does not provide the opportunity for retribution or appropriate redress on behalf of ADC members."[4] In response, the MSA submits that the role of the Commission is not to visit retribution on an offender or to provide specific redress to a market participant. The inappropriateness of retribution as a

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[1] ADC Argument at para. 13; IPCAA Argument at pg. 1.

[2] MSA Argument at paras. 70-80.

[3] IPCAA Argument at pg. 5.

[4] ADC Argument at para. 12.

basis for an administrative penalty was specifically addressed by the Supreme Court of Canada in *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission) ("Asbestos")*.[5] The appropriateness of considering "redress" in assessing a penalty is addressed in paragraph 11of this submission along with related IPCAA submissions.

(c) Role of Reputational Damage Determining the Quantum of the Penalty

7. IPCAA argues that the reputational damage suffered by TransAlta as a result of its conduct is not an appropriate factor to consider in determining the quantum of the penalty imposed on TransAlta.[6]

8. In response, the MSA submits because the role of an administrative penalty is to encourage compliance, and not to seek retribution or punishment,[7] reputational damage as a deterrent factor is one of the many factors the Commission should consider in determining the appropriate quantum of the penalty imposed on TransAlta. The MSA notes that the UCA agrees with the MSA on this point and accepts that TransAlta "has and will suffer damage to its reputation as a result of its misconduct" and accepts that it is appropriate to take such damage into account in assessing the level of penalty.[8]

(d) Inclusion of an estimate of the financial harm to market participants in the assessed penalty

9. IPCAA argues that the quantum of the penalty should " … reflect the full social cost of the violation."[9] The ADC argues that the quantum of the penalty should include the full cost of the harm to Alberta consumers caused by TransAlta's conduct as calculated by ADC.[10]

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[5] MSA Argument at para. 67. See also Asbestos at paras. 41 and 42.

[6] IPCAA Argument at pg. 6.

[7] MSA Argument at para. 67. See also Asbestos at paras. 41 and 42.

[8] UCA Argument at para. 15.

[9] IPCAA Argument at pg. 2.

[10] ADC Argument at paras. 5-12.

These submissions do not include authority or precedents for such a penalty. The MSA disagrees with the submissions of both Interveners in principle and in practice.

10. In the case of *Fischer v. IG Investment Management Ltd.*[11] the Ontario Court of Appeal draws a clear distinction between the role of regulatory bodies such as the Ontario Securities Commission (and by inference the Alberta Utilities Commission) which have a protective and preventative role, and the Courts, which have a remedial or compensatory role.

11. This is consistent with the Alberta regulatory scheme, which does not provide the Commission authority to order compensation or redress, but does require the Commission to look at many factors that properly consider the protection of the public. If there is a right of redress it lies in the Courts and not before this Commission. Accordingly, while pursuant to Rule 13 the Commission should consider the harm done generally to market participants as one of many factors in determining an appropriate penalty, the purpose of such a penalty must not be to compensate market participants and consumers for this harm.

12. In practice the MSA disagrees that the ADC and IPCAA calculations are representative of the actual harm experience by those parties or the market. The calculations presented by both parties are unreasonable and have limited evidentiary basis. This is because of their speculative nature and, in particular, the assumption that all of their own load and all of the market load was exposed to the pool price for the full 31 hours. The MSA responded to the calculations of ADC at paragraphs 20 -25 of the MSA March 5th Rebuttal Evidence[12] and to the calculations of IPCAA at paragraphs 37 to 43 of the MSA March 5th Rebuttal Evidence.

II. MSA consultation with Interveners during investigations and negotiations

13. The ADC argues that the MSA has not provided any evidence to the Commission that it undertook consultation with Alberta consumers to ascertain the extent and degree of harm that was done as a result of TransAlta's conduct.[13]

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[11] *Fischer v. IG Investment Management Ltd*., 2012 ONCA 47, at paras. 48 -57.

[12] Exhibit 37

[13] ADC Argument at para. 11.

14. In its March 5th Rebuttal Evidence and Submissions the MSA addresses efforts to look at the potential harm to the market as a result of TransAlta's conduct in this matter. It concluded some market participants would be better off and some worse off and that any general conclusions were exposed to substantial uncertainty and unreliable.

15. The MSA submits that its role in undertaking investigations and bringing matters before the Commission in accordance with sections 41 to 56 is an investigative and enforcement role, not a consultative role. This is clear from the plain language of these sections of the AUCA and the Market Surveillance Regulation, which make no reference to consultations with respect to investigations and enforcement, whereas there are clear references to consulting with respect to MSA guidelines.

16. Similar complaints to those raised by the Interveners were made by the Plaintiff investors in *Fischer*[14] with respect to a settlement involving over $200 million in a situation where the Ontario Securities Commission (OSC) staff did not consult with the investors in a proceeding against five mutual fund managers, and where the settlement was approved by the OSC in camera. The Ontario Court of Appeal recognized the limited role for the investors in the OSC process in the following passages:

> *[59] While a general notice of the settlement hearings was posted on the OSC's website, there was no attempt to notify the affected investors that the hearings were being held. Neither the investors nor their counsel attended the hearings or made submissions. Moreover, the substantive portions of the hearings took place in camera and were thus closed to anyone but counsel for the defendants and the relevant regulatory commissions.*
>
> *[60] Similarly, the procedure by which the settlements were arrived at did not facilitate investor participation. The amount of compensation that the defendants agreed to pay to the affected investors as a term of the settlement agreements was calculated without any opportunity for the investors to participate and without any details in the record of the OSC proceedings as to how this amount was calculated.*
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> *[61] In contrast, the purpose of the procedural vehicle of the class action is to allow for the appointment of a representative plaintiff who shares a sufficient*

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[14] *Fischer v. IG Investment Management Ltd*., 2012 ONCA 47

> *common interest with members of the class. The representative plaintiff conducts the litigation on behalf of class members under court supervision[6] and within the presumptive principle of an open court.*
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> *[62] The observations about the accessibility of the OSC proceedings are not meant to suggest that the elements of confidentiality and lack of participation by the investors made the hearings and settlement agreements somehow inappropriate or nefarious. On the contrary, the point is that the OSC proceedings were not intended or designed to provide the investors with access to justice for purposes of adjudicating the claims advanced in the proposed class proceeding. In short, the investors were not, and were not intended to be, parties to the OSC process.*
>
> (underlining added)

17. The MSA submits that the legislature considered the desirability of transparency in investigations and settlements in section 44 of the AUCA by imposing the requirement that settlements must be filed by the MSA with the Commission for approval under section 51(1)(b). This provision assures, as has been the case here, that there will be transparency, and where the Commission considers it appropriate, public input on any settlement reached by the MSA.

III. Responsibility of TransAlta for Investigation and Hearing Costs

18. IPCAA argues that TransAlta should be required to pay the administrative costs associated with this proceeding including: the MSA's investigation costs, the negotiated settlement costs, and the hearing costs.[15] The MSA disagrees.

19. The MSA is not shy about seeking recovery of the costs of its enforcement and related activities. It sought recovery of substantial costs in the Syncrude Canada Ltd. Specified Penalty case[16] and will not hesitate to seek a cost award again, where appropriate. In this case it is not seeking costs against TransAlta because the costs that were incurred fell largely within the normal investigation activities of the MSA. TransAlta cooperated with the investigation and moved to bring the matter to a expeditious conclusion, minimizing the cost

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[15] IPCAA Argument at pg. 9.

[16] Market Cost Order 2010-001

of enforcement. The MSA believes such conduct should be encouraged and will help achieve the expeditious and cost effective resolution of investigations.

IV. Conclusion

20. In conclusion, the MSA respectfully requests the Commission to approve the Application in this matter.