



Report to the Minister

For the Year Ending December 31, 2011

March 23, 2012



March 23, 2012

The Honourable Dr. Ted Morton
Minister of Energy
323 Legislative Building
1088 – 97 Avenue
Edmonton, Alberta T5K 2B6

Dear Minister:

RE: ANNUAL REPORT FOR 2011

It is my pleasure to submit the Annual Report of the Market Surveillance Administrator for the year ending December 31, 2011. The Report is provided to you pursuant to subsection 38(1) of the *Alberta Utilities Commission Act*.

Sincerely yours,

A handwritten signature in blue ink, appearing to read 'Harry Chandler', is written over a light blue horizontal line.

Harry Chandler
Market Surveillance Administrator

cc: Willie Grieve, Chair Alberta Utilities Commission

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1 Introduction

This Annual Report for 2011 is pursuant to paragraph 38(1) of the *Alberta Utilities Commission Act*, which directs the Market Surveillance Administrator (MSA) to provide the Minister of Energy with an annual update “(a) reporting on its activities in the fiscal year, and (b) containing its audited financial statements for the fiscal year”. The MSA’s fiscal year coincides with the calendar year.

The first part of the Report summarizes the activities of the MSA during the year, all of which is described in more detail and available to stakeholders through individual documents on the MSA website at <http://www.albertamsa.ca/> (and cited in the Report’s Reference section). The final section introduces the MSA’s financial state of affairs in 2011 and a copy of our year end financial statements audited by PricewaterhouseCoopers LLP.

As set out in section 39 of the *Alberta Utilities Commission Act*, the MSA’s mandate is to promote the fair, efficient and openly competitive operation of the electricity and retail natural gas markets. The MSA is authorized to do so in various ways, including monitoring and assessing the conduct of the various entities involved in the markets and monitoring and assessing market structures and arrangements that may affect competition. The MSA is empowered to publish guidelines to support the fair, efficient and openly competitive operation of these markets. Pursuant to subsection 20.4(4) of the *Electric Utilities Act* it may also file an objection with the Alberta Utilities Commission to a market rule on various grounds, including an adverse effect on the structure and performance of the electricity market. In its independent discretion the MSA may also investigate and seek financial penalties or other remedies for contraventions of the market rules or the *Electric Utilities Act* through adjudication by the Alberta Utilities Commission.

During 2011 the MSA touched many of the aspects of this mandate. These are described below in successive sections under the headings Market Monitoring, Promotion and Enforcement of FEOC, and Rules and Reliability Standards Compliance.

2 Market Monitoring

The daily review and assessment of activities in Alberta’s wholesale electricity market and associated markets is part of the core work of the MSA. It is from this exercise that the MSA identifies anomalous outcomes for further study to understand causes and take action if appropriate. The MSA deploys market monitoring indices to help identify unanticipated outcomes and the results are published in our quarterly reports to the market. These reports also provide summary statistics on the operation of the market and complement information published by the Alberta Electric System Operator (AESO), the goal of which is to provide a window on market operations for stakeholders.

In addition to market activity reports, during 2011 the MSA also included in its quarterly reports commentary on different features of the market designed to enhance efficiency by improving the fidelity and usefulness of market information. For example, the MSA suggested ways in which

the AESO short term price forecast could be improved and identified benefits that would flow from closer attention to outage scheduling. The MSA also drew the AESO's attention to a potential error in its published monthly and short term outage reports that the AESO acknowledged and corrected.

In its first quarter 2011 report the MSA commented on competition in the retail electricity market. This covered three facets. The first was an assessment of difficulties some members of Rural Electrification Associations encountered obtaining access to competitive retailers. The second reported on the evolution of the number of retail customers who switched from regulated or default service to competitive energy supply. The third aspect addressed retail prices by way of a comparison of the Regulated Rate Option price to competitive retail offerings over the five year period 2006 – 2010.

As a result of market monitoring work the MSA interacted frequently with market participants and other stakeholders to understand the facts and other perspectives on the issues.

3 Promotion and Enforcement of FEOC

The legal standard and focus of virtually all the MSA's work is FEOC, the fair, efficient and openly competitive operation of the market. Section 6 of the *Electric Utilities Act* directs that: "Market participants are to conduct themselves in a manner that supports the fair, efficient and openly competitive operation of the market." Alberta Regulation 159/2009, the *Fair, Efficient and Open Competition Regulation* provides greater specificity on the meaning of this provision in particular areas. As example of activity spawned by the FEOC Regulation during 2011, the MSA published an annual market share offer control report.

While clearly the MSA plays an enforcement role with respect to the FEOC standard, the MSA also makes an effort to be proactive in identifying situations that may undermine FEOC. For example, during 2011 the MSA commissioned a consultant's report on the potential for vigorous competition to be compromised by too liberal release of market data. The matter is still under consideration in a stakeholder consultation conducted jointly with the AESO.

Late in 2011 the MSA filed a settlement for approval by the Alberta Utilities Commission relating to an alleged contravention by a market participant of the conduct standard set out in section 6 of the *Electric Utilities Act*. This matter is before the Commission for decision in 2012.

Over the course of 2011 the MSA conducted other investigations that may or may not find their way to the Commission depending on their merits once the investigations are completed. The MSA has a policy of not releasing information on current investigations because they are testing allegations that may be unfounded once the fact finding is completed.

Finally, in 2011 four organizations were the subject of compliance audits pursuant to Alberta Regulation 160/2003, the electricity *Code of Conduct Regulation*. This regulation is in place to ensure the interactions between owners of electricity distribution systems and their affiliated retailers do not result in discriminatory treatment against non-affiliated retailers. All the issues the issues identified in the audits were addressed through remedial action.

4 Rules and Reliability Standards Compliance

The MSA plays a role in ensuring the good functioning of the Alberta interconnected electric system by promoting compliance with the ISO rules and the Alberta reliability standards. In 2011 the MSA worked with the AESO and market participants to implement a compliance process designed to address a greater number of these matters quicker. The detailed results for 2011 are the subject of a separate published report, Compliance Review 2011. Of note is the significant increase of self reports by market participants compared to 2010. The MSA issued 35 notices of specified penalty totaling \$69,750 as compared to 46 notices of specified penalty totaling \$75,000 in 2010. None of the notices of penalty issued in 2011 were disputed or remained unpaid.

5 Financial Statements

During 2011 the MSA made an effort to balance the need to meet its mandate and to show restraint in the cost of running the agency and came in slightly under budget (\$38,000).

In the coming year the MSA will continue its efforts to manage costs in a prudent manner and to look for areas in which we can realize more internal efficiencies.

The audited statements of the MSA for the year ended December 31, 2011 follow. No significant issues were brought to our attention by the auditors.

Market Surveillance Administrator

Financial Statements

Twelve Months Ended December 31, 2011



Independent Auditor's Report

To the Management of the Market Surveillance Administrator:

We have audited the accompanying financial statements of Market Surveillance Administrator ("MSA") which comprise the balance sheet as at December 31, 2011 and the statements of operations and cash flows for the year then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statement that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of MSA as at December 31, 2011 and the results of their operations and their cash flows for the year then ended in accordance with Canadian generally accepted accounting principle.

PricewaterhouseCoopers LLP

Chartered Accountants

February 27, 2012
Calgary, Alberta

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**Market Surveillance Administrator
Balance Sheet
As at December 31,**

| | 2011 | 2010 |
|--|-----------------------|-------------------------|
| | \$ | \$ |
| ASSETS | | |
| Current Assets | | |
| Cash | 654,145 | 1,035,760 |
| Accounts receivable | - | 13,660 |
| Prepaid expenses and deposits | <u>50,844</u> | <u>50,819</u> |
| | 704,989 | 1,100,239 |
| Capital Assets (note 3) | <u>53,233</u> | <u>42,894</u> |
| | <u><u>758,222</u></u> | <u><u>1,143,133</u></u> |
| LIABILITIES | | |
| Current Liabilities | | |
| Accounts payable and accrued liabilities | 423,492 | 821,076 |
| Deferred revenue (note 4) | <u>334,730</u> | <u>322,057</u> |
| | 758,222 | 1,143,133 |
| EQUITY (note 1) | <u>-</u> | <u>-</u> |
| | <u><u>758,222</u></u> | <u><u>1,143,133</u></u> |

The accompanying notes are an integral part of these financial statements.

On behalf of the corporation:

/Harry Chandler/

Harry Chandler
Market Surveillance Administrator

/Douglas Wilson/

Douglas Wilson
Legal Counsel & Secretary

**Market Surveillance Administrator
Statement of Operations
For the Twelve Months Ended December 31, 2011**

| | 2011 | 2010 |
|---|------------------|------------------|
| | \$ | \$ |
| Revenue | | |
| Alberta Electric System Operator (note 4) | 2,848,766 | 3,267,316 |
| Interest & Other Income | - | 10,000 |
| Total Revenue | <u>2,848,766</u> | <u>3,277,316</u> |
| Expenses | | |
| Salaries and benefits | 1,980,520 | 2,644,079 |
| Consultants, legal & audit | 427,364 | 241,572 |
| Operating, office and administrative | 415,401 | 382,090 |
| Amortization | 25,481 | 9,575 |
| Total Expenses | <u>2,848,766</u> | <u>3,277,316</u> |
| Net Earnings | <u>-</u> | <u>-</u> |

The accompanying notes are an integral part of these financial statements.

Market Surveillance Administrator
Statement of Cash Flows
For the Twelve Months Ended December 31, 2011

| | 2011 | 2010 |
|--|-----------------------|-------------------------|
| | \$ | \$ |
| Cash provided by (used for): | | |
| Operations | | |
| Net earnings | - | - |
| Item not involving cash: | | |
| Amortization | 25,481 | 9,575 |
| Change in non-cash operating items: | | |
| (Increase) decrease in accounts receivable | 13,660 | (13,660) |
| (Increase) decrease in prepaid expenses and deposits | (25) | (7,846) |
| Increase in accounts payable and accrued liabilities | (397,584) | 467,570 |
| Increase (decrease) in deferred revenue | 12,673 | (190,804) |
| | <u>(345,795)</u> | <u>264,835</u> |
| Investing | | |
| Expenditures on capital assets | <u>(35,820)</u> | <u>(39,231)</u> |
| (Decrease) Increase in cash | (381,615) | 225,604 |
| Cash, beginning of the period | <u>1,035,760</u> | <u>810,156</u> |
| Cash, end of the period | <u><u>654,145</u></u> | <u><u>1,035,760</u></u> |

The accompanying notes are an integral part of these financial statements.

Market Surveillance Administrator

Notes to the Financial Statements

For the Twelve Months Ended December 31, 2011

1 Nature of Operations

The Market Surveillance Administrator ("MSA") was incorporated as an independent, stand-alone entity on June 1, 2003 under the Electric Utilities Act of the Province of Alberta.

The business and affairs of the Market Surveillance Administrator corporation are overseen by an individual appointed as Market Surveillance Administrator by the Minister of Energy for the Province of Alberta.

As of January 1, 2008, the Market Surveillance Administrator was continued under the Alberta Utilities Commission Act with a broad mandate including surveillance, investigation, and enforcement to help ensure fair, efficient, and openly competitive electricity and retail natural gas markets in Alberta. The Market Surveillance Administrator is responsible for keeping a close eye on the behaviour of market participants and the overall performance of the market to ensure there are no anti-competitive activities and that rules are appropriate and are working as intended. The Market Surveillance Administrator communicates information arising from the various activities of the Market Surveillance Administrator within its mandate, to foster transparency and confidence for stakeholders. It responds to matters brought to the attention of the Market Surveillance Administrator through complaint or referral, and resolves issues before they become complaints. It examines the conduct of market participants to ensure compliance with legislation, regulations and rules; making sure sufficient remedies exist to avoid untoward market behaviour or activity. And the Market Surveillance Administrator issues guidance to the market and makes recommendations to the Department of Energy and other parties where appropriate, toward the development and operation of a fair, efficient and openly competitive market.

The Market Surveillance Administrator has no share capital. The Alberta Utilities Commission Act requires that the Market Surveillance Administrator prepare a budget for each fiscal year, for approval by the chair of the Alberta Utilities Commission. Once approved, the Alberta Electric System Operator is required to pay the Market Surveillance Administrator the budgeted costs and expenses, net of any other revenues. The Market Surveillance Administrator is to be managed so that no profit or loss results on an annual basis from its operation.

2 Significant Accounting Policies

Cash

Cash consists of cash in bank less outstanding cheques.

Capital Assets

Capital assets are stated at cost. Amortization is provided using the following methods and annual rates:

| | | |
|------------------------|---------------|------------|
| Computer Hardware | Straight-line | 3 Years |
| Computer Software | Straight-line | 3 Years |
| Furniture & Equipment | Straight-line | 5 Years |
| Leasehold Improvements | Straight-line | Lease Term |

Income Taxes

No provision has been made for income taxes as the Market Surveillance Administrator is a not-for-profit organization as set out in the Alberta Utilities Commission Act of the Province of Alberta.

Financial Instruments

The Company's financial instruments consist of cash, accounts receivable and accounts payable and accrued liabilities. It is management's opinion that the Company is not exposed to significant interest rate, currency or credit risks associated with these financial statements.

Revenue Recognition

Consistent with the requirements of the Alberta Utilities Commission Act that the Market Surveillance Administrator operate with no annual profit or loss, collections from the Alberta Electric System Operator are recognized as revenue to the extent of annual operating costs including amortization of capital costs. In circumstances where annual collections are in excess of annual costs, the excess is deferred and recognized in future periods. In the event of a shortfall between collections and costs, the shortfall in revenue will be accrued and be collected in a subsequent period from the Alberta Electric System Operator.

Measurement Uncertainty

These financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. Because the precise determination of many assets, liabilities, revenues and expenses are dependent on future events, the preparation of financial statements for a period necessarily includes the use of estimates and approximations which have been made using careful judgement. Actual results could differ from those estimates.

3 Capital Assets

| | 2011 | | | 2010 |
|------------------------|----------------|-----------------------------|-------------------|-------------------|
| | Cost | Accumulated Amortization | Net Book Value | Net Book Value |
| | \$ | \$ | \$ | \$ |
| Computer Hardware | 113,718 | 84,327 | 29,391 | 33,933 |
| Computer Software | 31,742 | 29,132 | 2,610 | 4,277 |
| Leasehold Improvements | 11,033 | 2,844 | 8,189 | - |
| Furniture & Equipment | 105,106 | 92,063 | 13,043 | 4,684 |
| | <u>261,599</u> | <u>208,366</u> | <u>53,233</u> | <u>42,894</u> |

4 Deferred Revenue

The collections from the Alberta Electric System Operator are set to recover the operating and capital costs of the Market Surveillance Administrator. Any excess or shortfall in collections is deferred to or accrued for future years.

| | 2011 \$ | 2010 \$ |
|--------------------------------------|--------------------|--------------------|
| Alberta Electric System Operator | | |
| Opening balance, January 1 | 322,057 | 512,860 |
| Collection for February to December | 2,572,060 | 2,842,688 |
| Less: Revenue recognized in the year | <u>(2,848,766)</u> | <u>(3,267,316)</u> |
| | 45,351 | 88,232 |
| Collection for January | <u>289,379</u> | <u>233,825</u> |
| Closing balance, December 31 | <u>334,730</u> | <u>322,057</u> |

5 Commitments

The Market Surveillance Administrator is committed under a lease agreement for its current premises until October, 2014. Total lease costs including estimated operating costs are approximately as follows:

| | <u>\$</u> |
|------|-----------|
| 2012 | 256,362 |
| 2013 | 257,654 |
| 2014 | 214,711 |

The Market Surveillance Administrator has entered into a service agreement with the Alberta Electric System Operator, under which the Market Surveillance Administrator receives certain information technology and office services. These services are provided for a monthly fee of \$3,500, plus an hourly fee for special projects.

6 Credit Facility

The Market Surveillance Administrator has a demand operating facility. Under the terms and conditions of this facility, the corporation can borrow up to \$300,000 at the prime rate plus 0.75% of interest. No pledges of security are required from the corporation for the facility and no amount was drawn on this facility at year-end.

6 References

Market Surveillance Administrator

MSA First Quarter Report

<http://albertamsa.ca/uploads/pdf/Reports/Quarterly%20Reports/2011/MSA%202011%20First%20Quarter%20Report%20051011.pdf>

MSA Second Quarter Report

[http://albertamsa.ca/uploads/pdf/Reports/Quarterly%20Reports/2011/MSA%202011%20Second%20Quarter%20Report%20\(081811\).pdf](http://albertamsa.ca/uploads/pdf/Reports/Quarterly%20Reports/2011/MSA%202011%20Second%20Quarter%20Report%20(081811).pdf)

MSA 2010 Third Quarter Report

<http://albertamsa.ca/uploads/pdf/Archive/2011/MSA%20Q3-11%20Report%20113011.pdf>

MSA 2010 Fourth Quarter Report

<http://albertamsa.ca/uploads/pdf/Archive/2012/MSA%20Q4-11%20Report%20020212.pdf>

Compliance Review 2011

http://albertamsa.ca/uploads/pdf/Archive/2012/Compliance%20Review%202011_final%20020912.pdf

Consultant's Report on Market Data Transparency

<http://albertamsa.ca/uploads/pdf/Archive/2011/Market%20Data%20Transparency/CRA%20Report%20for%20MSA%2011-22%202011.pdf>

Alberta Legislation

Alberta Electric Utilities Act, Chapter E-5.1 (2003)

http://www.qp.alberta.ca/574.cfm?page=E05P1.cfm&leg_type=Acts&isbncln=9780779747542

Alberta Utilities Commission Act, Chapter A-37.2 (2007)

http://www.qp.alberta.ca/574.cfm?page=A37P2.cfm&leg_type=Acts&isbncln=9780779747580

Fair, Efficient, Open Competition Regulation, AR 159/2009

http://www.qp.alberta.ca/574.cfm?page=2009_159.cfm&leg_type=Regs&isbncln=9780779747719

Code of Conduct Regulation, AR 160/2003

http://www.qp.alberta.ca/574.cfm?page=2003_160.cfm&leg_type=Regs&isbncln=9780779728824



The Market Surveillance Administrator is an independent enforcement agency that protects and promotes the fair, efficient and openly competitive operation of Alberta's wholesale electricity markets and its retail electricity and natural gas markets. The MSA also works to ensure that market participants comply with the Alberta Reliability Standards and the Independent System Operator's rules.