



Report to the Minister 2010

March 1, 2011



1 March 2011

The Honourable Ron Liepert
Minister of Energy
323 Legislative Building
1088 – 97 Avenue
Edmonton, Alberta T5K 2B6

Dear Minister:

RE: ANNUAL REPORT FOR 2010

It is my pleasure to submit the Annual Report of the Market Surveillance Administrator for 2010 pursuant to subsection 38(1) of the *Alberta Utilities Commission Act*.

2010 is the first full year since my appointment and I have enjoyed working with market participants and the broader stakeholder community in promoting the fair, efficient and openly competitive standard which is the centerpiece of Alberta's market.

Thank you for your support during the year.

Sincerely yours,

A handwritten signature in blue ink, appearing to read 'Harry Chandler', is written over a faint, light blue circular watermark that contains the MSA logo.

Harry Chandler
Market Surveillance Administrator

cc: Willie Grieve, Alberta Utilities Commission

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1 Introduction

This Annual Report for 2010 is pursuant to paragraph 38(1) of the *Alberta Utilities Commission Act* that asks 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 in one place the activities of the MSA throughout 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/>. The Report does not attempt to restate the content or findings of these documents but rather provides an inventory of activities and a brief synopsis of ‘what’ and ‘why’. The final section contains a brief description of the MSA’s financial state of affairs in 2010 and a copy of our year end financial statements audited by PricewaterhouseCoopers LLP.

At a high level many of the activities in 2010 were directed toward putting in place policies, procedures and guidance to equip market participants to self-regulate their behaviour. This is in keeping with tenets of regulatory efficiency and invites market participants to take action to support the integrity of the market. We consulted extensively with stakeholders before finalizing these instruments. An example of a major initiative in this regard was the articulation of comprehensive Offer Behaviour Enforcement Guidelines.

But, while structures were put in place to encourage market participants to look to themselves for compliance with the ISO rules, the Alberta Reliability Standards and support for the *fair, efficient, and openly competitive operation of the market*, this did not mean an end to active oversight or intervention as required by the MSA. For example, we saw a 40 percent increase in the number of rules matters addressed and we registered over \$750,000 in financial penalties during the year. The MSA worked in parallel with its partners, the Alberta Electric System Operator and the Western Electricity Coordinating Council, Inc. (WECC) to deploy expert monitoring of rules and standards. We also began the development of rigorous monitoring indices to assist in the identification of anomalous market outcomes and released comprehensive quarterly reports on what we saw in the marketplace.

The Annual Report is organized in the following manner. Section 2 describes our activities concerning the development of the Offer Behaviour Enforcement Guidelines. Section 3 provides a summary of the reports we published during the year and our activities related to development of market metrics and monitoring of the retail electricity and natural gas markets. Section 4 contains an overview of the MSA’s activities regarding compliance and enforcement of ISO rules and Alberta Reliability Standards. Section 5 provides details concerning the two investigations completed by the MSA in 2010. Section 6 provides a brief summary of budget highlights for the past year and includes the audited financial statements for the MSA.

2 Offer Behaviour

The *Fair, Efficient and Open Competition Regulation* introduced a number of specific prohibitions some of which have application to market participant offer behaviour in the Alberta electricity market. In the absence of jurisprudence, the MSA believed it would be helpful to stakeholders to explain our analytical framework and how we intend to enforce provisions in the Regulation with potential application to offer

behaviour. Following an extensive stakeholder consultation process throughout 2010, including the publication of two discussion papers - Foundational Elements and Analytical Framework - the MSA published the *Offer Behaviour Enforcement Guidelines* (OBEGs) on January 14, 2011. The guidelines strive to provide transparency and predictability regarding the MSA's assessment of market participant offer behaviour so that they can govern themselves accordingly.

3 Market Monitoring

The MSA sees the forward market as an important element in the overall electricity market structure. We routinely receive trade data from both brokers and companies operating electronic trading platforms. To promote greater understanding of the forward market, we published the Financial Electricity Market report on April 9, 2010. The report provides a general description of the market structure, the various reasons entities might trade and the different trading patterns, as well as an overview of the data that has been collected by the MSA over the past two years.

Market metrics are used by the MSA to assess the competitive performance of the Alberta market. We utilize different metrics to determine if there is evidence of healthy supplier on supplier competition and whether Alberta's energy only market is functioning properly. During the consultation process on offer behaviour, a number of stakeholders expressed interest in the monitoring methods used by the MSA. The MSA responded by providing stakeholders with detailed explanations for two market metrics we are employing to assess competition: the supply cushion – pool price relationship which was published in the MSA 2010 Third Quarter Report; and, the residual supply index which we described in the MSA 2010 Fourth Quarter Report.

The MSA published the Alberta Wholesale Electricity Market report in September 2010 as part of our on-going effort to provide reports of an educational nature to Albertans. The report describes the general structure and operation of Alberta's wholesale energy market. Over the past several years, the MSA has published a number of these types of reports covering various sub markets that collectively constitute the Alberta electricity market. The Wholesale Electricity Market report completes that series.

The *Fair, Efficient and Open Competition Regulation* came into force on September 1, 2009. The Regulation requires that the MSA collect offer control information from all market participants with a market share more than 5 percent and calculate the percentage of offer control held by those market participants. We published the Market Share Offer Control 2010 report on June 28, 2010 which is the result of that exercise. The function of assessing offer control is an important one because the control of offers is more relevant to price formation in the Alberta electricity market than ownership of the asset.

In the second half of 2010 the MSA began to focus more resources on assessing competition in Alberta's retail electricity and natural gas markets. In addition, we initiated a project to develop an analytical framework based on competition law and economics that will be used to assess issues in the retail markets. We also began developing market metrics to enhance our oversight abilities.

4 Rules Compliance and Enforcement

During 2010, the MSA implemented a revised compliance process in consultation with market participants and stakeholders. In this regard, we published the Compliance Process document on October

25, 2010 which describes the revised process. Efficiencies gained through the revised process allowed the MSA to address a greater number of compliance matters in 2010 and in a timelier manner. In 2010, the MSA addressed 141 ISO rules matters relative to 101 in 2009. Despite the increase in number of files reviewed, the average time to resolution of compliance matters was reduced to 76 days from 132 days in 2009. The new framework was designed to promote the development of robust internal compliance programs in industry by offering the prospect of favourable treatment and, in certain cases, assured forbearance when participants identify their own contraventions and self report them to the MSA. The increase in file count in 2010 was largely attributed to an increase in self reporting.

The MSA issued a significant financial penalty to a single market participant comprised of 332 notices of specified penalty totaling \$655,000 for infractions of the ISO's dispatch rules. The MSA issued 46 other notices of specified penalty totaling \$75,000. No notices of specified penalty issued in 2010 were disputed or remained unpaid. The AUC approved 7 MSA negotiated settlements applicable to ISO rules compliance in 2010 totaling \$26,000. The MSA addressed an additional 27 matters related to Alberta Reliability Standards including the submission of mitigation plans concerning 19 cases.

With respect to negotiated settlements, the MSA initiated and finalized a number of matters with market participants in cases where a specified penalty was not available to the MSA. This approach resulted in the expeditious resolution of matters and saved the parties and agencies significant time and money. In April 2010, the MSA entered into a Services Agreement with the Western Electricity Coordinating Council, Inc. (WECC). The Services Agreement provides that WECC will monitor compliance of the AESO with the Alberta Reliability Standards under the auspices of the MSA. WECC will refer any suspected contraventions of Alberta Reliability Standards to the MSA for enforcement or other action and will provide a technical resource for the MSA on reliability issues. The Services Agreement requires no payment of fees by the MSA to WECC, but the cost of services is included as part of the WECC fees already assessed to the AESO as part of its membership in WECC.

5 Investigations

During 2010, the MSA concluded two investigations into complaints we received in 2009. One investigation concerned a complaint pertaining to a long term Energy Services Agreement (ESA) between ENMAX Energy Corporation (ENMAX Energy) and The City of Calgary and the other complaint dealt with certain financial transactions of ENMAX Power Corporation (ENMAX Power).

The MSA published its ESA investigation report on September 28, 2010. The investigation looked into an allegation that the ESA contravened sections 5(c), 6 and or 95(10) of the EUA. The complainant alleged that the ESA unduly supported ENMAX Energy's interests in several wind farms. Following a detailed analysis, the MSA concluded that there was no basis for moving forward in regard to the complaint. The ESA investigation report serves as a broad guide for stakeholders to the MSA's enforcement approach by demonstrating how we applied the analytical framework of competition law and economics to the allegations.

The MSA released its second investigation report in November 2010 concerning a complaint alleging that certain financial transactions by ENMAX Power may have contravened sections 5 (c), 6 and/or 95(10) of the EUA. Our review of the legislation and recent jurisprudence confirmed that section 5 of the EUA is not capable of contravention, and that MSA involvement is not contemplated in issues concerning section 95. The investigation concluded that there was no violation of section 6 of the EUA.

6 Budget Highlights

The economic climate in Alberta during 2010 underlined the need to exercise restraint in our costs of operations. Accordingly, the MSA's expenditures came in under budget for 2010 by approximately \$100,000. The savings were achieved primarily by reducing outside consulting and legal fees and by utilizing existing staff resources in a more efficient manner.

For the coming year, the MSA plans to maintain the same staff complement as in past years. We will continue our efforts throughout 2011 to manage costs in a prudent manner and to look for areas in which we can realize more internal efficiencies and attempt to do more with our existing complement.

Attached to this summary of the MSA activities over 2010 are the audited statements for the corporation for the calendar year. No significant issues were brought to our attention.

MSA 2010 Financial Statements

Market Surveillance Administrator Financial Statements

Twelve Months Ended December 31, 2010



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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, 2010 and the statements of operations and cash flows for the year then ended, and the related notes including a summary of significant accounting policies.

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, 2010 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 16, 2011
 Calgary, Alberta

"PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership, or, as the context requires, the PricewaterhouseCoopers global network or other member firms of the network, each of which is a separate legal entity.

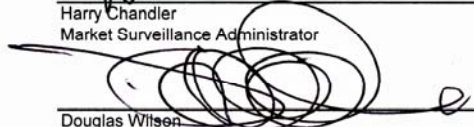
**Market Surveillance Administrator
Balance Sheet
As at December 31,**

	2010	2009
	\$	\$
ASSETS		
Current Assets		
Cash	1,035,760	810,156
Accounts receivable	13,660	-
Prepaid expenses and deposits	50,819	42,973
	<u>1,100,239</u>	<u>853,129</u>
Capital Assets (note 3)	<u>42,894</u>	<u>13,238</u>
	<u><u>1,143,133</u></u>	<u><u>866,367</u></u>
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	821,076	353,507
Deferred revenue (note 4)	322,057	512,860
	<u>1,143,133</u>	<u>866,367</u>
EQUITY (note 1)	<u>-</u>	<u>-</u>
	<u><u>1,143,133</u></u>	<u><u>866,367</u></u>

On behalf of the corporation:



Harry Chandler
Market Surveillance Administrator



Douglas Wilson
Legal Counsel & Secretary

Market Surveillance Administrator		
Statement of Operations		
For the Twelve Months Ended December 31, 2010	2010	2009
	\$	\$
Revenue		
Alberta Electric System Operator (note 4)	3,267,316	3,239,426
Interest & Other Income	10,000	114
Total Revenue	3,277,316	3,239,540
Expenses		
Salaries and benefits	2,644,079	2,217,802
Consultants, legal & audit	241,572	601,231
Operating, office and administrative	382,090	412,328
Amortization	9,575	8,179
Total Expenses	3,277,316	3,239,540
Net Earnings (note 1)	-	-

Market Surveillance Administrator		
Statement of Cash Flows		
For the Twelve Months Ended December 31, 2010	2010	2009
	\$	\$
Cash provided by (used for):		
Operations		
Net earnings	-	-
Item not involving cash:		
Amortization	9,575	8,179
Change in non-cash operating items:		
Increase in accounts receivable	(13,660)	-
(Increase) decrease in prepaid expenses and deposits	(7,846)	6,559
Increase (decrease) in accounts payable and accrued liabilities	467,570	(54,315)
Decrease in deferred revenue	(190,804)	(130,508)
	<u>264,835</u>	<u>(170,085)</u>
Investing		
Expenditures on capital assets	<u>(39,231)</u>	<u>(3,242)</u>
Increase (decrease) in cash	225,604	(173,327)
Cash, beginning of the period	<u>810,156</u>	<u>983,483</u>
Cash, end of the period	<u>1,035,760</u>	<u>810,156</u>

Market Surveillance Administrator

Notes to the Financial Statements

For the Twelve Months Ended December 31, 2010

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

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. These financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

3 Capital Assets

	2010			2009
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
	\$	\$	\$	\$
Computer Hardware	100,690	66,757	33,933	4,468
Computer Software	31,674	27,397	4,277	337
Furniture & Equipment	93,415	88,731	4,684	8,433
	<u>225,779</u>	<u>182,885</u>	<u>42,894</u>	<u>13,238</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.

	2010 \$	2009 \$
Alberta Electric System Operator		
Opening balance, January 1	512,860	643,368
Collection for February to December 2010	2,842,688	2,850,492
Less: 2010 Revenue	<u>(3,267,316)</u>	<u>(3,239,426)</u>
	88,232	254,434
Collection for January 2011	233,824	258,426
Closing balance, December 31	<u>322,056</u>	<u>512,860</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:

	\$
2011	247,170
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 \$2,900, 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.

References

Market Surveillance Administrator

ACFA Report (November 2010)

<http://albertamsa.ca/uploads/pdf/Reports/Reports/ACFA%20Report%20110910.pdf>

Alberta Wholesale Electricity Market (September 2010)

<http://albertamsa.ca/uploads/pdf/Reports/Reports/Alberta%20Wholesale%20Electricity%20Market%20Report%20092910.pdf>

Analytical Framework for the Monitoring of Bids, Offers, and Market Health (June 2010)

http://albertamsa.ca/uploads/pdf/Archive/MSA_Discussion_Paper2_061710.pdf

Compliance Process (October 2010)

<http://albertamsa.ca/uploads/pdf/Compliance/Compliance%20Process%20102510.pdf>

Electricity Services Agreement (September 2010)

<http://albertamsa.ca/uploads/pdf/Reports/Reports/Electricity%20Services%20Agreement%20092810.pdf>

Financial Electricity Market Report (April 2010)

http://albertamsa.ca/files/Financial_Electricity_Market.pdf

Foundational Elements Shaping the Market Surveillance Administrator's Approach to Bids and Offers (April 2010)

http://albertamsa.ca/uploads/pdf/Archive/Foundational_Elements_100427.pdf

Market Share Offer Control (June 2010)

http://albertamsa.ca/files/MSOC_2010_062810.pdf

MSA First Quarter Report (April 2010)

http://albertamsa.ca/files/O1_2010_Report_30_April_2010.pdf

MSA Second Quarter Report (August 2010)

<http://albertamsa.ca/uploads/Q2%202010%20Report%20090810.pdf>

MSA 2010 Third Quarter Report (November 2010)

<http://albertamsa.ca/uploads/pdf/Reports/Quarterly%20Reports/Q3%202010%20Report%20110510.pdf>

MSA 2010 Fourth Quarter Report (February 2011)

<http://albertamsa.ca/uploads/pdf/Reports/Quarterly%20Reports/Q4%202010%20Report%20021611.pdf>

Offer Behaviour Enforcement Guidelines (January 2011)

<http://albertamsa.ca/uploads/pdf/Consultations/Market%20Participant%20Offer%20Behaviour/Decide%20-%20Step%205/Offer%20Behaviour%20Enforcement%20Guidelines%20011411.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



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.