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MSA REPORT

Report to the Minister
2009

MARKET SURVEILLANCE
ADMINISTRATOR

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1 INTRODUCTION

Under section 38 (1) of the *Alberta Utilities Commission Act* the Market Surveillance Administrator (MSA) is required to provide to the Minister an annual report "(a) reporting on its activities in the fiscal year, and (b) containing its audited financial statements for the fiscal year". This document is that report. The MSA's Quarterly Reports already provide extensive information on our activities, so this report will highlight some of the key activities in each of the areas of responsibility under our mandate for the calendar year 2009.

2009 was a year of transition for the MSA. Martin Merritt retired as Administrator at the end of September and Harry Chandler was appointed effective October 1, 2009 for a five year term. The FEOC regulation was passed during 2009 adding new language to help guide the MSA in our interpretation of what constitutes a fair, efficient and openly competitive market. It also put new requirements on the MSA to collect and publish information related to the share of offer control that each asset holds in the province. The MSA was given one year to make that determination; however in 2009 we conducted a stakeholder consultation to lay out the process for collecting and calculating the offer control statistics. As well, *The Electric Statutes Amendments Act, 2009* (Bill 50) was passed in the fall. It added the enforcement of reliability standards to the MSA's responsibilities.

2 MARKET MONITORING

With respect to Alberta's real-time wholesale electricity market, 2009 started out with some very high priced days in January. In our first quarter report we provided an analysis of the events which led to these price, essentially that the market was particularly tight over the period January 21 to 23. The difference in pricing that occurred over those 3 days was a result of the portfolio offers of the participants, behaviour that is not offside the ISO rules. The MSA is embarking on a broad stakeholder consultation during 2010 on our approach to offer behaviour in the Alberta market.

In spite of this high price start to the year, the average spot market price for 2009 was \$47.81/MWh some 47% lower than the average for 2008 at \$89.95/MWh. The main driver of this was the relaxation of demand-supply conditions in the market. In 2009 the supply cushion was below 500 MW 3% of the time while in 2008 the supply cushion was below 500 MW 12 % of the time.

During 2009, we published two papers which were intended as educational pieces to help those Albertans who may not be well versed in all the intricacies of markets better understand a couple of aspects of the market.

The first was a paper entitled "Retail Review: Electricity and Natural Gas". This paper provided an update on the assessment of competition between retail electricity providers and assessed the state of competition in the retail natural gas market. The conclusion of the paper was that while 25 percent of the residential RRO eligible customers had switched to competitive electricity contracts; this is

relatively low compared to other markets. The paper did point out that all three large retailers have continued to experience market share growth since 2006, but it also suggested that it seemed unlikely that the majority of Albertans would switch to retailers in the near to medium term.

In addition to this report on the competitiveness of the retail market, in its Q2 report, the MSA did an analysis of the Regulated Rate Option (RRO) price. The conclusions of this analysis spoke to the fact that the RRO index has introduced some price volatility into RRO rates and still managed, on average, to converge with the settled Pool price. The weighted average post price and trade price for both flat RRO and extended peak RRO were virtually equal indicating no noticeable 'walking out' of the price. Also, looking at trading on both the Natural Gas Exchange (NGX) and Over the Counter (OTC) it was clear that the RRO index tracked both markets quite well. The RRO rates charged to residential customers by the providers were very comparable. Looking forward to 2010, when 100 percent of the RRO will be priced based on the prompt month forward price, the findings suggest that there are no major concerns.

The second stand alone educational piece was entitled "Operating Reserves Procurement – Understanding Market Outcomes". The purpose of this paper was primarily aimed at explaining some of the dynamics of the operating reserve market and why on occasion some outcomes are non-intuitive. The MSA believes that some persistent stakeholder concerns can be addressed by providing a better understanding of how small changes in market fundamentals can have a large impact on operating reserve prices. Compared to the energy market there is a relative absence of information about participant offers and market dynamics. While this may not restrict competition between sophisticated market participants it may not provide other stakeholders with sufficient confidence that the market is competitive. A better understanding of these factors should also assist market participants in understanding the AESO's proposed re-design of the operating reserves market.

3 RULES COMPLIANCE AND ENFORCEMENT

A significant draw on the MSA resources over 2009 was its work on rules compliance. At the beginning of 2009 the MSA had 8 files under review that had carried over from 2008. During 2009 an additional 100 files were opened and 7 remain under review at the end of the year. Of the 101 files addressed during 2009, 57 resulted in notices of specified penalty and 35 files resulting in forbearance or a finding of no breach. As of the end of December 2009, all 57 notices had been paid (totaling \$149,000) and no notices had been disputed. We decided to seek administrative penalties pursuant to Section 51 of the *Alberta Utilities Commission Act* (AUCA) for the 9 remaining files,.

Based on a review of 2009 we believe that we can make, and where it is not under our control, advocate for, a number of enhancements that would enable matters to be dealt with as swiftly and efficiently as possible. Achieving additional efficiencies in 2010 is necessary for us to be able to absorb the additional

responsibilities associated with enforcement of reliability standards without recruiting new staff.

4 INVESTIGATIONS

During 2009 the MSA concluded its investigation of ENMAX. The subject of the investigation concerned the conduct of ENMAX Corporation and its affiliates in relation to importing activity during 2005. Although the scope of the investigation covered the period between January and the end of October 2005, the focus of much of the work related to ENMAX import trades that were negotiated between HE18 on September 27, 2005 and HE13 on September 28, 2005. After careful consideration we found no wrongdoing by ENMAX or any other Alberta market participant during the period under review. The investigation took approximately four years to conclude. This was due in part to certain procedural issues raised during the course of the investigation that are well known and on the public record. We believe that this experience and the resulting clear jurisprudence will allow us to manage future reviews in the efficient and expeditious manner expected by stakeholders.

While our investigation team undertook additional projects in 2009, none of them became public and as such can not yet be reported.

5 BUDGET

The MSA came in under budget for 2009 by about \$160,000. While we had budgeted to replace one staff member who left in late 2008 and to add an additional new staff position, the result was that we merely filled the one vacant position. The balance of the savings was realized as a result of not needing to use as much outside consulting assistance as originally budgeted.

Going into 2010, we recognize that the economic climate of Alberta requires that agencies like the MSA show a balance between the need to meet their mandate and to show restraint on the cost of running the agency. In this regard we hope to achieve more internal efficiencies in 2010 and attempt to do more with the existing complement.

Attached to this summary of the MSA activities over 2009 are the audited financial statements for the corporation for the calendar year 2009.

February 25, 2010

Auditors' Report to the Management of the Market Surveillance Administrator

We have audited the balance sheet of Market Surveillance Administrator as at December 31, 2009 and the statements of operations and cash flows for the year ended. These financial statements are the responsibility of the company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2009 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PriceWaterhouseCoopers LLP

Chartered Accountants
Calgary, Alberta

Market Surveillance Administrator

Financial Statements

Twelve Months Ended December 31, 2009 and 2008

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

	2009	2008
	\$	\$
ASSETS		
Current Assets		
Cash	810,156	983,483
Accounts receivable	-	-
Prepaid expenses and deposits	<u>42,973</u>	<u>49,532</u>
	853,129	1,033,015
Capital Assets (note 3)	<u>13,238</u>	<u>18,174</u>
	<u><u>866,367</u></u>	<u><u>1,051,189</u></u>
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	353,507	407,821
Deferred revenue (note 4)	<u>512,860</u>	<u>643,368</u>
	866,367	1,051,189
EQUITY (note 1)	<u>-</u>	<u>-</u>
	<u><u>866,367</u></u>	<u><u>1,051,189</u></u>

On behalf of the corporation:

"Original Signed"

Harry Chandler
Market Surveillance Administrator

"Original Signed"

Wayne Silk
Deputy Administrator

**Market Surveillance Administrator
Statement of Operations**

For the Twelve Months Ended December 31, 2009

2009

2008

	\$	\$
Revenue		
Alberta Electric System Operator (note 4)	3,239,426	3,056,314
Interest & Other Income	<u>114</u>	<u>29,431</u>
Total Revenue	<u>3,239,540</u>	<u>3,085,745</u>
Expenses		
Salaries and benefits	2,217,802	2,057,675
Consultants, legal & audit	601,231	601,161
Operating, office and administrative	412,328	409,349
Amortization	<u>8,179</u>	<u>17,560</u>
Total Expenses	<u>3,239,540</u>	<u>3,085,745</u>
Net Earnings (note 1)	<u><u>-</u></u>	<u><u>-</u></u>

**Market Surveillance Administrator
Statement of Cash Flows**

For the Twelve Months Ended December 31, 2009

2009

2008

\$

\$

Cash provided by (used for):

Operations

Net earnings

-

-

Item not involving cash:

Amortization

8,179

17,560

Change in non-cash operating items:

(Increase) decrease in accounts receivable

-

-

Increase in prepaid expenses and deposits

6,559

(682)

Increase in accounts payable and accrued liabilities

(54,315)

(17,410)

Increase (decrease) in deferred revenue

(130,508)

602,822

(170,085)

602,290

Investing

Expenditures on capital assets

(3,242)

(3,720)

Increase in cash

(173,327)

598,570

Cash, beginning of the period

983,483

384,913

Cash, end of the period

810,156

983,483

Market Surveillance Administrator

Notes to the Financial Statements

For the Twelve Months Ended December 31, 2009

1 Nature of Operations

The Market Surveillance Administrator was incorporated as an independent, stand-alone entity on June 1, 2003 under the Electric Utilities Act of the Province of Alberta. With the Alberta Utilities Commission Act coming into force as of January 1, 2008, the corporation known as the Market Surveillance Administrator established by the Electric Utilities Act was continued.

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.

The mandate of the Market Surveillance Administrator, as set out in the Alberta Utilities Commission Act, is to carry out surveillance and investigation in respect of activities in the electric industry and Retail Natural Gas in the Province of Alberta. Those activities include the supply, generation, transmission, distribution, trade, exchange, purchase or sale of electricity, electric energy, electricity services or ancillary services.

The objective of carrying out surveillance and investigations are to assess whether or not:

- The conduct of market participants is consistent with the fair, efficient and openly competitive operation of the electricity related markets in Alberta;
- Legislation and market rules are being complied with;
- The market rules are sufficient to discourage anti-competitive practices in the electric industry; and
- The market rules facilitate fair, efficient and openly competitive electricity related markets.

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

The financial statements of the Market Surveillance Administrator have been prepared by management in accordance with Canadian generally accepted accounting principals.

Cash

Cash consists of cash in the 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

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.

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.

The fair values of the financial instruments approximate their carrying amounts due to the short-term nature of these instruments.

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.

3 Capital Assets

	2009			2008
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
	\$	\$	\$	\$
Computer Hardware	66,170	61,702	4,468	8,176
Computer Software	26,963	26,626	337	50
Furniture & Equipment	93,415	84,982	8,433	9,948
	<u>186,548</u>	<u>173,310</u>	<u>13,238</u>	<u>18,174</u>

4 Deferred Revenue

	2009	2008
	\$	\$
Alberta Electric System Operator		
Opening balance, January 1	643,368	40,546
Collection for February to December 2009	2,850,492	3,400,000
Less: 2009 Revenue	<u>(3,239,426)</u>	<u>(3,056,314)</u>
	254,434	384,232
Collection for January 2009	258,426	259,136
Closing balance, December 31	<u>512,860</u>	<u>643,368</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>
2010	202,634
2011	204,421
2012	213,354
2013	213,354
2014	177,795

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 of interest plus 0.75%. No pledges of security are required from the corporation for the facility and no amount was drawn on this facility at year-end.