

# ***Fair, Efficient and Openly Competitive***

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The agency that I head is staffed by about a dozen folks comprising legal, engineering, economist and commodity trading skill sets. We are keen students of both the market and of human behavior, My remarks today are based on those observations.

There is more than one model for structuring electricity markets. Regulated or competitive, both models can work, they both have features to commend them and neither are immune to the foibles of human nature. We have been regulating public utilities for 60 years and still we still have the odd train wreck... we have massive stranded/public debt in many N.A. jurisdictions for a variety of reasons. .... Been there done that, probably going to do it again.

Competitive markets have had their share of issues too and because those issues are more recent they are perhaps more prominent in our mind. Those who advocate putting the genie back in the bottle are poor students of history, economics and human nature in my view. In Alberta we've made our choice; 9 years ago we began the migration from good but less than perfect regulated model to a competitive model, I think the competitive model has served us well though it too is less than perfect.

It seems likely to me that if legislators, and we as implementing agencies are going to continue to improve the function and output our competitive market model we need to stay focused on the interaction between two drivers that are as reliable as death and taxes: self interest and public interest.

## MSA 2004 / 2005 (YTD)

- Normal course
    - Regular Quarterly and Monthly Summaries
    - 3x day outage reporting
  - Special Reports and Studies
    - Regulating Reserve Performance
    - Dispatch Compliance
    - PWX Spinning Reserve Review
    - Import/Export review
    - TMR Investigation and Recommendations
- ...and much more, see our website*

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Martin Merritt

The MSA doesn't make policy or design markets... We are charged by the EUA with promoting a fair, efficient and openly competitive market. We are an analytical, a surveillance and a prosecutorial agency. We are prolific publishers of most of what we survey and analyze. We comment on market design to the extent that it impairs fair, efficient or competitive outcomes. We also investigate participant behavior based on either complaints or concerns we develop through our own monitoring.

As a matter of course we do not usually disclose much about the existence, nature or target of our investigations unless they lead to a tribunal or (as is often the case) what starts out as a participant behavior concern turns into something more general and less nefarious and becomes a published report.

On the matter of Tribunals, the Act gave us this sanctioning body just over 18 mo ago, The MSA has not so far uncovered a transgression over which the tribunal would have jurisdiction and that demanded prosecution or redress through this channel.

However, In 2004 we identified and vetted a pool of prospective Tribunal panel members having a range of skills and experiences broad enough to cover any conceivable issue that the MSA might bring forward. So, while I don't look forward to our first Tribunal we will not be reluctant to call for one. When the circumstances warrant and the jurisdiction permits... we are ready.

On the slide behind me I have highlighted a cross section of the routine and not so routine work performed and published by the MSA since this time last year. If you are not a regular visitor to our website and are at all left brained I encourage you to check us out, I think you will find the site a real treasure trove.

## Thoughts on regulating competitive electricity markets

- Get the simple things right!
  - Information Rich
  - Level Field
  - High fidelity price signal
  - Allow competition to work
- Other
  - Rules are not a substitute for competitive behavior
  - Externally imposed discipline must backstop market discipline
  - Markets are always a “work in progress”

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As I suggested earlier, competitive markets exist at the intersection of public interest and self interest. The combination of market design, participant behavior and market monitoring must cause the pursuit of self interest to produce societal benefits. I'd like to share some thoughts with you on how I see these pieces fitting together.

First, I believe that the MSA does its best work preemptively, ensuring that regulating mechanisms are in place and working... if not competitive mechanisms then bureaucratic ones because there is no such thing as an unregulated market. In order to ensure the presence and health of competitive regulating mechanisms there really are a small number of things that we have to get right and in Alberta the MSA is dedicated to those things....

Good access to information,

a level playing field,

a decent price signal, and then

doing our best to stay the heck of the way where ever we convince ourselves that competitive regulating forces are at work!

I don't mind admitting a bias for less rules, as I love to say “the best regulators I ever had were customers and competitors”... but there is a quid for having less prescriptive rules. I acknowledge the desire for certainty but I think that in some quarters the expectation is that express rules will preclude the requirement for fair, efficient or ethical conduct... that in an ultra prescriptive environment anything that is within the letter of the rules will fly. Well I'm sorry, rules abidance is not a “get out of jail free” card for anti competitive behaviour. I hear two pleas from industry regularly each of which I am sensitive to:

“just tell me the rules” and

“stop making rules”

Sometimes I even hear both pleas from the same participant. We are dreaming if we think we could ever create (or would ever want) an environment that is so prescriptive that we have obviated the need for any sense of right, wrong or accountability by participants. We have a benchmark for conduct in our market, “Fair, Efficient and Openly Competitive” it's a standard that is very appropriate even if it is a little less B&W than some might like.

So, For participants who bring judgement and accountability to their game the MSA is working hard to keep the rule book clear, as thin as possible and enforced in an even handed way... that we might all enjoy the fruits of less fettered competition. For those who want a line in the sand for everything I say be careful what you wish for.

Now, working to help the market regulate itself does not mean that the market monitor is passive or asleep at the switch! there will be bad guys out there and the MSA's job is to detect and prosecute them ...or in the event of a market design flaw, work with policy makers and the market operator to close the barn door. Both wrong doers and people who are not as smart as they need to be are frequently disciplined by the market itself, but at other times regulators have to step in to ensure market integrity. There is no rule against either creativity or stupidity but criminal, fraudulent or anti competitive behavior is monitored for and will be detected and prosecuted.

Finally, I believe it is not possible to get a market design correct, straight out of the box, regulated or unregulated it will always be an adjust-as-you-go exercise. So now that we have a little breathing room in terms of capacity is precisely the time we need to be considering market amendments; what if any they should be, will be a matter of discussion, but the time to reflect on such questions is now.

## Issues to Shape 2005

- Market Design
- Rule Compliance
- Treatment of imports and exports
- Retirements?
- Emerging Market Power

I'd like to close with a few thoughts on the issues that I think will shape the market and the MSA's work in 2005.

The roll out this past week of the DOE's discussion paper on market design has to top the list. Not only will debate over the paper dominate the next quarter but once the direction becomes clear we will all, you as participants and me as market monitor have to learn some new dance steps.

I spoke earlier about rules and my bias toward less not more... well the flip side of that coin is to enforce the ones we have and the MSA expects to work much closer with the AESO in doing this in 2005.

I could leave the import/export issue on this slide for ever... in fact I can't remember a time when the tie lines to our neighboring jurisdictions were not an issue of some sort. On this year's list we have:

seams issues that prevent counter flowing uneconomic imports, the lack of ability for ties to set price, the night time losses figures, ATC determination... have I forgotten any?

I was pleased to see most of these issues contemplated in the DOE's paper.

What's the life of a thermal generator? 40 years? I've been in the Alberta electricity industry for 10 years so simple math would suggest that about ¼ of what I saw when I got here should be retired by now.... Even if I grant you an average 50 yr life then maybe I should have seen 20% of the old fleet retire in fact I've seen only a few MW of very old coal fired capacity actually retire in the 10 years I've been around. This is even more surprising given the run up in fuel costs that might arguably cause older units to retire sooner not later. I was very encouraged to see the DOE's paper express the principle that economics be allowed to dictate the future of Cloverbar. Its certainly a principle supported by the MSA.

It's normal in any industry that during profitability troughs the strong get stronger, the weak get acquired and people do what they need to do to survive economically. The emergence of market power can be a byproduct of such times and so it is very appropriate that the DOE undertake the study work with London Economics that it referenced in the discussion paper. Clear, comprehensive and preemptive guidance on concentration issues will be as fundamental to where the industry goes next as the holding restrictions were to the original PPA auction.

I'm sure there will be many other key issues but I'm going to cut it off there,

Thank you, I look forward to the panel discussion and questions from the floor