

PAC-ANREP-2015

PEM Audit Committee 2015 Annual Report

January 2015 to December 2015

Market Assessment Group
2-29-2016

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The PEM Audit Committee (PAC) submits this Annual Report covering the activities undertaken and accomplished by the PAC for the year 2015. This report also presents the proposed activities of the PAC for the year 2016.

I. 2015 ACCOMPLISHMENTS

A. Submission of PEM Audit Committee Reports

In accordance with the PEM Audit Market Manual, the PAC submitted to the PEM Board the following reports:

1. 2014 Annual Report

This report provides a summary of the accomplishments of the PAC in 2014, the highlights of which include the following: completion of the 4th Independent Audit of the Systems and Procedures on Market Operations (MO Audit); completion of the selection process and subsequent awarding of contract for audit services to RSM Bird Cameron in partnership with Reyes Tacandong & Co., for the 5th MO Audit; and the submission of the proposed Terms of Reference (TOR) to the ERC for the proposed 1st Systems Operations Review.

The report was submitted to the PEM Board on 16 February 2015.

2. 5th Independent Audit of the Systems and Procedures on Market Operations Summary Report

This provides a synopsis of the audit findings and recommendations submitted by RSM Bird Cameron covering the period 26 June 2013 to 25 December 2014. This document was published in the WESM Market Information Website.

Together with the audit report, the Software Certification by the External Auditor was also submitted to the PEM Board, DOE and ERC.

B. 2nd Metering Arrangements Review (AP2014-01)

This review commenced on 21 July 2014 covering the period 26 December 2011 until 25 December 2013. A total of 196 metering installation sites located in Luzon and Visayas were reviewed by Intelligent Energy Systems (IES).

The PAC and WESM-TWG, headed by the Department of Energy (DOE) with members from PEMC, National Transmission Corporation (TransCo) and Technical Committee (TC), conducted close-out meetings with Angeles Electric Cooperative (AEC) and San Fernando Electric Light & Power Company (SFELAPCO) on 18 May 2015; Manila Electric Company (MERALCO) on 19 May 2015; National Grid Corporation of the Philippines(NGCP) on 20 May 2015; and PEMC-Billing, Settlement and Metering on 25 May 2015.

As a matter of procedure, the PAC, WESM-TWG together with the External Auditor reviewed the audit findings on 21 October 2015. Comments and suggestions relative to the level of classification of non-conformance were submitted by the Committee and TWG for External Auditor's consideration. The draft final report will be submitted to the Auditees for their comment. The audit project is expected to be completed by 1Q 2016.¹






C. 5th Independent Audit of the Systems and Procedures on Market Operations

After the successful selection process was undertaken in October 2014, the audit service contract was awarded to RSM Bird Cameron in partnership with Reyes Tacandong & Co. The audit proper started on 21 February 2015 and was concluded on 08 September 2015 with the presentation of the audit results and recommendations of the External Auditor before the ERC en banc meeting.




The 5th Market Operations Audit was conducted using a risk and compliance approach. The risk and compliance ratings applied to assess the issues identified are described below:

¹ The project was expected to be completed by 1Q 2015, but due to the setbacks experienced by the External Auditor in human resources, the project completion timeline was reset.

Risk Rating

Rating		Description
Extreme		Issues which may have a catastrophic impact on WESM operations if they are not addressed immediately and require executive action with regular reporting at Board level.
High		Issues which may have a major impact on WESM operations if they are not addressed as a matter of priority. These issues require senior management attention with regular monitoring and reporting at executive and Board meetings.
Medium		Issues which may have a moderate impact on WESM operations if they are not addressed within a reasonable timeframe. These issues require management attention with regular ongoing monitoring.
Low		Issues which may have a minor impact on WESM operations if they are not addressed in the future. These issues are the responsibility of management with regular monitoring and reporting at staff meetings.
Efficiency/ Opportunity		Housekeeping matters and opportunities for improving internal controls and procedures and efficiency relating to WESM operations.

Compliance Rating

Rating		Description
Level 1		Evidence of non-compliance with review criteria. These should be addressed as a matter of high priority.
Level 2		Issues which could possibly result in non-compliance with review criteria, but where no evidence of actual non-compliance was found. However, there is considered to be insufficient formal evidence of controls in place or being actioned in relation to these issues. These should generally be addressed within 1-2 months.
Level 3		Housekeeping matters and opportunities for improving internal controls and procedures relating to electricity market operations. These should be addressed within 3-6 months.

In accordance with International Standard on Assurance Engagements (ISAE) 3000, the External Auditor rendered a reasonable assurance conclusion for Market

Software and Systems Review, by certifying that the Market Dispatch Optimization Model (MDOM) Software, and Billing and Settlements Software used by PEMC will substantially perform in compliance with the WESM Rules, RCOA Rules and the associated Market Manuals.

Further, the External Auditor rendered a qualified limited assurance conclusion for the following tasks: a) Information Security and Technology Review; b) Process and Compliance Review; c) Bid-to-Bill Analysis; and d) Review of Rules and Manuals. The conclusion was made considering the following: a) one (1) High Risk finding with Level 1 non-compliance regarding the trading of WESM members during the effectivity of its suspension; b) two (2) Low Risk Level 1 non-compliances pertaining to the development of the Central Registration Body Performance (CRB) Standards and annual reporting; c) inconsistency in the timing of registration fee payments in the WESM Rules vis-à-vis the internal business procedure; and d) other issues ranging from Low Risk to High Risk where internal controls in relation to the operation of the WESM can be improved. The External Auditor also based its conclusion on the scope limitation that existed with respect to procedures that were intended to be performed on critical IT controls, which resulted in their inability to obtain appropriate evidence.

Findings identified in this review as well as the corresponding action plans are monitored by the PEMC WESM Compliance Officer. A monitoring report which includes the updates on the developments of the action plans is submitted to the PEM Audit Committee for review and assessment.

D. Proposed Rules Changes to the WESM Rules and Market Manuals

The proposed rules changes to WESM Rules and Market Manuals previously submitted by the PEM Audit Committee in 2008 and 2012 were revisited by the PAC to address the challenges of the Committee in performing its responsibilities.

In the process of its review, the PAC agreed to revise its proposed amendments to the WESM Rules and Market Manuals as follows:

- 1) Replaces PEM Auditor with the PEM Audit Committee in recognition that the function of the PEM Auditor is now being performed by the PEM Audit Committee, as provided for by the Guidelines Governing the Constitution of the PEM Committees;
- 2) Clarifies that the frequency of the audit is annually or as often as necessary, to be determined by the PEM Board and upon the request of the Enforcement and Compliance Office (ECO). The quarterly audit was proposed to be changed drawing from the PAC's experience in the past five (5) market operations audit and two (2) metering arrangements review. The PAC, besides overseeing the audit also undertakes the process of selecting the External Auditor.
- 3) Dedicates a chapter for the different kinds of audits that the Committee has to undertake, in order to consolidate the different audits mentioned in the various chapters of the PEM Audit Committee Market Manual proposed to be revised
- 4) Harmonizes the proposed amendments made in the WESM Rules pertaining to the audit procedures with the PEM Audit Market Manual and the Guidelines Governing the Constitution of the PEM Committees.

E. Meetings and Other Activities

For CY 2015, the PAC conducted sixteen (16) meetings, seven (7) of which are special meetings, while nine (9) are regular meetings. In furtherance of their responsibility to oversee the audit, members of the PAC and TWG also actively participated in the series of close-out meetings with the Auditees of the 2nd Metering Arrangements Review.

PAC also attended the 9th WESM Annual Participants Meetings in August 2015.

II. 2016 WORK PLAN

The PAC's work plan for CY 2016 contains the following activities:

Item	Activity	Tentative Timetable	Deliverables
1	Submission of 2015 Annual Report	1Q 2016	Report
2	Submission of 2 nd Metering Arrangements Review Report	1Q 2016	Report
3	Submission of the Proposed Rules Changes to the WESM Rules, Retail Manual and PAC Market Manual Issue 2.0	1Q 2016	Proposed Amendments
4	Joint Conduct of the 6 th Independent Operational Audit of the Systems and Procedures on Market Operations & 3 rd Review of Metering Installation and Arrangements	2Q to 3Q 2016	Reports & Software Certificate
5	Submission of Assessment Report	Quarterly	Report
6	Regular Conduct of Meeting	At least once a month	Resolutions/Minutes
7	Audits as may be requested in accordance to Compliance and Enforcement Market Manual and to the directive by DOE, ERC and PEM Board	As required	Report

III. MEMBERSHIP

The PEM Audit Committee is currently composed of the following experts in the fields of risk and financial management, information technology, and information systems:

Chairperson : Prof. Felixberto U Bustos, Jr.
Members : Mr. Eduardo Alejandro O. Santos
Engr. Christian M. Orias

Prof. Bustos was appointed as member of the Audit Committee on 27 April 2007 and was designated as the Chairperson. Mr. Santos and Engr. Orias were similarly appointed as members since 01 September 2011.

The Market Assessment Group (MAG) provides technical and administrative support to the PAC.

IV. RESPONSIBILITIES

Pursuant to WESM Rule 1.5.2, the responsibilities of the PEM Auditor² are as follows:

- (a) Conduct annual audits of the Market Operator and the settlement system and any other procedures, persons, systems or other matters relevant to the spot market;
- (b) Test and check any new items or versions of software provided by the Market Operator for use by WESM members;
- (c) Review any procedures and practices which are covered by the WESM Rules at the direction of the PEM Board;
- (d) Recommend changes to the WESM Rules where the PEM Auditor detects deficiencies as a consequence of an audit, review, test, check or other form of review; and
- (e) Publish on the market information website the results of any findings and recommendations under WESM Rule 1.5.1.

The PEM Auditor's main responsibility is summarized in the PEM Audit Committee Market Manual Clause 3.1, which states that it has to conduct, on his own or through an appointment of auditor, and to coordinate and supervise effective and independent audits of the operation of the spot market and of the Market Operator, in order to reinforce Trading Participants' confidence in the transparency and adequacy of the operation of the WESM.

Moreover, Clause 11.2.2 of the same manual provides that the PEM Auditor shall review the security arrangements and requirements of metering installations.

² Pursuant to Guidelines Governing the Constitution of PEM Committees, the PEM Auditor was already changed to constitute as PEM Audit Committee (PAC). The WESM Rules, PEM Audit Market Manual Issue 2.0 and Retail Market Manual are currently being revised in harmony with the existing guidelines.

Submitted By:

PEM AUDIT COMMITTEE

(signed)

Felixberto U. Bustos, Jr.
Chairperson / PEM Auditor

(signed)

Eduardo Alejandro O. Santos
Member

(signed)

Christian M. Orias
Member