



Mr Thomas Quinn
Commission for Energy Regulation
The Exchange
Belgard Square North
Dublin

21 February 2017

Ms Karen Shiels
Utility Regulator
Queens House
14 Queen Street
Belfast

By email

Dear Mr Quinn and Ms Shiels

ESB Group fully supports the appointment of an Auditor and Monitor to provide independent assurance of the System Operators' capacity market systems and procedures. We are pleased to respond to the consultation (SEM-17-007) on the terms of reference for these roles. Our responses to the consultation questions are set out below. Our separate responses to the Capacity Market Code (CMC) consultation covers the Auditor and Monitor roles set out in section B.10 and B.11.

- For market participants the Auditor and Monitor roles aim to provide assurance the System Operators' systems and procedures are working properly in accordance with the CMC and if not, whether those systems and procedures need to change or whether a modification to the CMC is necessary. For the Regulatory Authorities (RAs) the Auditor and Monitor provides assurance with regard to compliance with the CMC.

ESB Group believe this compliance assurance should focus on the system and process design, operational effectiveness and the compliance by the System Operators with their requirements under the CMC and in that sense, the focus is not or should not be on market participants. This distinction is important and is not explicitly clear. To this end, the CMC should be amended to account for the statement in para 2.2.4 of the consultation that the role of the Monitor does not include market monitoring. A similar statement would be appropriate in relation to the role of the Auditor.

- The consultation appears to be seeking views on the merits of a single opinion from the Trading and Settlement Code (TSC) Market Auditor and capacity market Auditor. On one hand, there does not appear to a strong reason to combine the audits into a single opinion other than potential efficiencies in procuring these services. Carefully drafting the terms of reference will avoid duplication without detracting from the intent or effectiveness of each role. The TSC or CMC could set out the consultation requirements and communication protocols between the Auditors. On the other hand, there does not appear to be a strong reason to prevent a suitably qualified entity from performing both roles and producing a single opinion.
- The proposed standards, ISRS4400 for the Auditor and ISAE3000 for the Monitor, are reputable standards and appear suitable to apply to the respective roles.

- The capacity market auction seeks to procure a volume of reliability options to, at a minimum, satisfy the I-SEM reliability standard. As this is a volumetric procurement it is appropriate for the Auditor to report materiality on a volumetric basis.
- The consultation proposes to apply the market and participant level materiality thresholds in the TSC Market Audit to the capacity market Auditor role. This does not appear to recognise the challenges or implications of shifting to a volume based materiality threshold.
 - The terms of reference should specify that each threshold relates to the de-rated capacity requirement for the capacity auction or the capacity year. This is the baseline against which each threshold is applied.
 - At the market level, the proposed 0.25% threshold is around 18MW of de-rated capacity against the System Operators' indicative capacity requirement for 2018, 2019 and 2020.¹ The de-rated capacity requirement has the potential to fluctuate between capacity auctions and capacity years. This is due to the least-worst regrets analysis, if the auction format and winners determination changes due to inclusion or exclusion of locational capacity constraints or the future inclusion of any reserve requirement. This indicates a fixed MW market level threshold is more suitable and stable, especially in the early years of the new capacity market. A fixed threshold of 20MW is analogous with the 0.25% proposal.
 - This could similarly manifest itself at participant level. In the interests of clarity and consistency a fixed MW threshold is more desirable. One tenth of the market level threshold, 2 MW, is a suitable participant level threshold.
- The Report of Significant Issues should include all issues, regardless of materiality. ESB Group considers this will provide a complete picture of the System Operators' performance while helping prevent immaterial issues from becoming material issues in the future.
- We have two observations on the proposed governance and reporting framework.
 - The framework should require the Auditor and Monitor to consult and cooperate with one another should different entities perform the roles. This appears to be absent from the consultation paper and the CMC.
 - The consultation and CMC infers the Auditor may play a role in investigating market manipulation, anti-competitive behaviour or gaming concerns.² This would be highly inappropriate. Such matters are reserved tasks for the relevant competent authorities. It is not appropriate to devolve this to a third party. The Monitor's role is to report on the System Operators' compliance with the CMC processes and procedures and not directly on market participants' compliance. As such, there should be no requirement for the Monitor to request information from market participants. In the event the

¹ SEM-16-051, p. 35.

² SEM-17-007, para 2.6.4, 2.6.5 and 2.6.9, p. 15-16.



Monitor identifies a discrepancy in its report this would (or should) trigger further investigation by the relevant competent authority.

- ESB Group supports appointing the Auditor and Monitor for specific capacity auctions as the timelines do not neatly fit into a fixed 12 month period.
- A substantial number of milestones need to be met ahead of the first transitional auction on 15 December 2017. New and untested rules, systems and processes highlight the importance of the Auditor and Monitor roles. With the second auction scheduled for as early as August 2018 it is vitally important the System Operators can address any weaknesses identified from the first auction. ESB Group therefore supports the proposal to conduct an interim review along the lines of section 3.9 of the consultation. The scope of the interim review following the first transitional capacity auction could be limited to focus on key areas ahead of the 2018 capacity auction.
- ESB Group agrees that the determination of location capacity constraints is outside the Monitor's likely area of expertise. The RAs are responsible for the technical assurance in this area in the same way they assessed and approved of the System Operators' methodology to de-rate capacity and determine the capacity requirement. We would contend the determination of any locational capacity constraint should include a consultation with market participants either by the System Operators or the RAs.
- The draft terms of reference for the Auditor and Monitor are awkwardly set out in the consultation and increase the potential for confusion. Publishing each terms of reference as a standalone appendix to the consultation is preferable as is the case for the TSC Market Audit terms of reference. We'd ask the RAs to publish each final terms of reference in this format.
- ESB Group proposes the RAs adopt a similar enduring process to determine the terms of reference for the capacity market Auditor and Monitor to that followed for the TSC Market Audit. This involves a consultation on the terms of reference for each specific capacity auction. This would be helpful to all market participants ahead of the second and third I-SEM capacity auctions.

Should you wish to discuss this response further please contact Krystle Healy on (01) 70 27410.

Yours Sincerely

Krystle Healy

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