Republic of the Philippines
ENERGY REGULATORY COMMISSION
San Miguel Avenue, Pasig City

ENERGY REGULATORY COMMISSION
Approved for Posting
www.erc.gov.ph

IN THE MATTER OF THE APPLICATION FOR APPROVAL OF THE INTERIM POWER SUPPLY AGREEMENT WITH SAN MIGUEL ENERGY CORPORATION, WITH PRAYER FOR PROVISIONAL AUTHORITY

ERC CASE NO. 2012-082 RC

CAGAYAN I ELECTRIC COOPERATIVE, INC. (CAGELCO I),
Applicant.
x - x

DOCKETED
Date: MAY 29 2018
By:

DECISION

Before the Commission for resolution is the application filed on 26 June 2012 by Cagayan I Electric Cooperative, Incorporated (CAGELCO I) for approval of its interim power supply agreement (PSA) with San Miguel Energy Corporation (SMEC), with prayer for provisional authority.

In the said application, CAGELCO I alleged, among others, that:

1. It is an electric cooperative duly organized and existing under the Philippine law with principal office address at Maddarulug, Solana, Cagayan. It is franchised to construct, own, operate and maintain an electric distribution network in the City of Tuguegarao and in the Municipalities of Rizal, Tuao, Piat, Sto. Niño, Solana, Enrile, Peñablanca, Iguig, Amulung, Alcala and Baggao, all in the Province of Cagayan;

2. It currently sources bulk of its power supply requirements from SN Aboitiz Power-Magat, Incorporated (SNAP-MAGAT) under a three (3)-year PSA, which provisionally approved by the Commission in an Order dated July 20, 2009 issued under ERC Case No. 2009-037 RC. Its PSA with SNAP-MAGAT is due to expire on July 25, 2012;

3. It has also entered into a fifteen (15)-year PSA with GNPower Limited Company (GNPOWER) that was approved by the

Commission on October 3, 2007 under ERC Case No. 2007-121 RC. Under this agreement, GNPOWER is to construct a 2 x 300 MW coal plant in Mariveles, Bataan and was proposed to commence commercial operations in January 2012. However, due to unforeseen delays, commercial operation of GNPOWER's coal plant is now estimated to commence on December 26, 2012;

4. Due to the delay in the commercial operation of GNPOWER's coal plant, it had to look for replacement power to bridge the gap in its contracted power supply from the time the PSA with SNAP-MAGAT expires on July 25, 2012 until the commercial operation of GNPOWER's coal plant on December 26, 2012;

5. Together with some other electric cooperatives similarly situated, it went out in September 2011 to jointly solicit offers from the power producers operating in Luzon, namely: a) SNAP-MAGAT; b) AES Masinloc; c) Green Core Geothermal Incorporated (GCGI); d) Team Energy (Sual); e) SEM Calaca Power Corporation; f) Sunwest Water and Electric Company, Incorporated; and g) SMEC;

6. Out of the seven (7) power producers invited to submit offers, only SNAP-MAGAT and SMEC responded to its solicitation. After evaluating the offers submitted, it found the offer of SMEC to be the most complying in meeting its power supply requirements;

7. On March 22, 2012, it signed an interim PSA with SMEC effective on March 26, 2012 until December 25, 2012 under a Time-of-Use Rate (TOU) Schedule, more particularly described as follows:

SMEC's TOU Rate Schedules, PhP/kWh
(December 26, 2011 to December 25, 2012)

Period	January to June		July to December	
	Monday to Saturday	Sunday and Holiday*	Monday to Saturday	Sunday and Holiday*
1:00:00 AM (0000-0100)	3.0300	3.0300	3.0300	3.0300
2:00:00 AM (0100-0200)	3.0300	3.0300	3.0300	3.0300
3:00:00 AM (0200-0300)	3.0300	3.0300	3.0300	3.0300
4:00:00 AM (0300-0400)	3.0300	2.5523	3.0300	2.5523
5:00:00 AM (0400-0500)	3.0300	2.5523	3.0300	2.5523
6:00:00 AM (0500-0600)	3.0300	2.5523	3.0300	2.5523
7:00:00 AM (0600-0700)	3.0300	2.5523	3.0300	2.5523
8:00:00 AM (0700-0800)	3.1896	3.0300	3.1896	3.0300
9:00:00 AM (0800-0900)	3.3130	3.0300	3.3130	3.0300
10:00:00 AM (0900-1000)	6.6746	3.1896	6.6746	3.1896
11:00:00 AM (1000-1100)	7.2157	3.1896	7.2157	3.1896
12:00:00 PM (1100-1200)	6.6746	3.1896	6.6746	3.1896
1:00:00 PM (1200-1300)	6.6746	3.1896	6.6746	3.1896
2:00:00 PM (1300-1400)	7.2157	3.1896	7.2157	3.1896
3:00:00 PM (1400-1500)	6.6746	3.1896	6.6746	3.1896
4:00:00 PM (1500-1600)	6.4664	3.1896	6.4664	3.1896
5:00:00 PM (1600-1700)	6.2355	3.1896	6.2355	3.1896

6:00:00 PM (1700-1800)	6.6746	3.3130	6.6746	3.3130
7:00:00 PM (1800-1900)	7.2157	6.2355	7.2157	6.2355
8:00:00 PM (1900-2000)	6.6746	6.2355	6.6746	6.2355
9:00:00 PM (2000-2100)	6.4664	3.3130	6.4664	3.3130
10:00:00 PM (2100-2200)	3.3130	3.1896	3.3130	3.1896
11:00:00 PM (2200-2300)	3.1896	3.0300	3.1896	3.0300
12:00:00 AM (2300-0000)	3.0300	3.0300	3.0300	3.0300

* Holidays shall refer to those that are celebrated nationwide

8. The energy contracted from SMEC for the period March 26, 2012 to July 25, 2012 is meant to cater to its load growth which is already in excess of the energy contracted from SNAP-MAGAT and was being procured from the Wholesale Electricity Spot Market (WESM);

9. The energy contracted from SMEC for the period July 26, 2012 to December 25, 2012 is also meant to bridge the gap from the time the PSA with SNAP-MAGAT expires on July 25, 2012 and the commercial operation of GNPOWER's coal plant on December 26, 2012;

10. Simulations of the rate impact of the proposed interim PSA with SMEC on its generation costs disclosed the following:

SNAP-MAGAT (Actual)				**SMEC with Re-nomination Simulation**				
Particulars	**kWh**	**Effective Rate**	**Amount (PhP)**	**kWh**	**Avg. TOU Rate**	**Amount (PhP)**	**%**	**Difference**
Bilateral Contract	10,636,814	5.2935	56,306,077.25	10,636,814	4.8662	51,761,229.64	77%	(4,544,847.61)
WESM	3,246,920	3.6050	11,705,027.72	3,246,920	2.9385	9,541,099.62	23%	(2,163,928.10)
Total	**13,883,733**	**4.8986**	**68,011,104.97**	**13,883,733**	**4.4154**	**61,302,329.26**	**100%**	**(6,708,775.71)**
Line Rental			1,210,736.52			4,686,800.77		3,476,064.24
Total	**13,883,733**	**4.9858**	**69,221,841.49**	**13,883,733**	**4.7530**	**65,989,130.02**		**(3,232,711.47)**
Rate Impact (PhP/kWh)					**(0.2328)**			

SNAP-MAGAT (Actual)				**SMEC 88% and 12% WESM Simulation**				
Particulars	**kWh**	**Effective Rate**	**Amount (PhP)**	**kWh**	**Avg. TOU Rate**	**Amount (PhP)**	**%**	**Difference**
Bilateral Contract	10,636,814	5.2935	56,306,077.25	12,217,685	4.8662	59,454,122.05	88%	3,148,044.80
WESM	3,246,920	3.6050	11,705,027.72	1,666,048	0.3586	597,498.24	12%	(11,107,529.48)
Total	**13,883,733**	**4.8986**	**68,011,104.97**	**13,883,733**	**4.3253**	**60,051,620.29**	**100%**	**(7,959,484.68)**
Line Rental			1,210,736.52			5,383,365.63		4,172,629.11
Total	**13,883,733**	**4.9858**	**69,221,841.49**	**13,883,733**	**4.7131**	**65,434,985.92**		**(3,786,855.57)**
Rate Impact (PhP/kWh)					**(0.2727)**			

11. In view of the urgency that it must have an approved PSA in place before its PSA with SNAP-MAGAT expires on July 25, 2012, it seeks provisional approval of the proposed interim PSA it entered into with SMEC so as to protect its member-consumers from the price volatility of the WESM; and

12. Thus, it prays that:

12.1 A Decision be rendered approving the interim PSA it entered into with SMEC; and

12.2 Upon filing of the application, an Order be issued provisionally approving the implementation of the interim PSA it entered into with SMEC.

Having found said application sufficient in form and in substance with the required fees having been paid, an Order and a Notice of Public Hearing, both dated 5 July 2012, were issued setting the case for jurisdictional hearing, expository presentation, pre-trial conference, and evidentiary hearing on 24 August 2012.

CAGELCO I was directed to cause the publication of the Notice of Public Hearing, at its own expense, twice (2x) for two (2) successive weeks in two (2) newspapers of general circulation in the Philippines, with the date of the last publication to be made not later than ten (10) days before the scheduled date of initial hearing. It was also directed to inform its member-consumers, by any other means available and appropriate, of the filing of the application, its reasons therefor, and of the scheduled hearing thereon.

The Office of the Solicitor General (OSG), the Commission on Audit (COA) and the Committees on Energy of both Houses of Congress were furnished with copies of the Order and Notice of Public Hearing and were requested to have their respective duly authorized representatives present at the initial hearing.

Likewise, the Offices of the Mayors of the City and Municipalities within CAGELCO I's franchise area and the Provincial Governor of Cagayan were furnished with copies of the Order and Notice of Public Hearing for the appropriate posting thereof on their respective bulletin boards.

On 15 August 2012, CAGELCO I submitted its "Pre-Trial Brief".

During the 24 August 2012 initial hearing, only CAGELCO I appeared. No intervenor/oppositor appeared nor was there any intervention/opposition registered.

At the said hearing, CAGELCO I presented its proofs of compliance with the Commission's posting and publication of notice requirements which were duly marked as Exhibits "A" to "B-16"[1], inclusive.

Thereafter, CAGELCO I made an expository presentation of its application. At the termination of the expository presentation, the Commission conducted a pre-trial conference.

---

[1] The Notice of Public Hearing was published in *The Manila Times* dated 20 July 2012 and 27 July 2012, and in *The Malaya Business Insight* dated 20 July 2012 and 27 July 2012.

Subsequently, CAGELCO I presented its lone witness, Engr. Hilario Mabborang, its Corporate Planning/Information Technology and Energy Trading Department Manager, who testified, among others, that: a) CAGELCO I solicited offers from various power suppliers; b) the offered terms of SMEC were found to be most advantageous; and c) the proposed power supply rates are just and reasonable.

In the course of his direct examination, the witness identified various documents which were duly marked as exhibits.

The said witness was, likewise, required to address the clarificatory questions propounded by the Commission.

On 10 September 2012, the Commission issued an Order provisionally approving the application, the dispositive portion of which reads as follows:

> *"**WHEREFORE,** the foregoing premises considered, the Commission hereby **PROVISIONALLY APPROVES** the interim power supply agreement (PSA) between Cagayan I Electric Cooperative, Incorporated (CAGELCO I) and San Miguel Energy Corporation (SMEC), subject to the following conditions:*
>
> *a. The Hourly Basic Energy Rate (exclusive of Basic Energy Rate Adjustment Factor formula) shall be as follows:*

(intentionally left blank.)

Period	*(January to June)*		*(July to December)*	
	Monday to Saturday	***Sunday and Holiday***	***Monday to Saturday***	***Sunday and Holiday***
1:00:00 AM (0000-0100)	2.1426	2.3022	2.1426	2.1426
2:00:00 AM (0100-0200)	2.1426	2.1426	2.1426	2.1426
3:00:00 AM (0200-0300)	2.1426	2.1426	2.1426	2.1426
4:00:00 AM (0300-0400)	2.1426	2.1426	2.1426	1.6649
5:00:00 AM (0400-0500)	2.1426	2.1426	2.1426	1.6649
6:00:00 AM (0500-0600)	2.1426	2.1426	2.1426	1.6649
7:00:00 AM (0600-0700)	2.1426	2.1426	2.1426	1.6649
8:00:00 AM (0700-0800)	2.4256	2.1426	2.3022	2.1426
9:00:00 AM (0800-0900)	5.5790	2.1426	2.4256	2.1426
10:00:00 AM (0900-1000)	6.3283	2.3022	5.7872	2.3022
11:00:00 AM (1000-1100)	6.3283	2.3022	6.3283	2.3022
12:00:00 PM (1100-1200)	6.3283	2.3022	5.7872	2.3022
1:00:00 PM (1200-1300)	6.3283	2.3022	5.7872	2.3022
2:00:00 PM (1300-1400)	6.3283	2.3022	6.3283	2.3022
3:00:00 PM (1400-1500)	6.3283	2.3022	5.7872	2.3022
4:00:00 PM (1500-1600)	6.3283	2.3022	5.5790	2.3022
5:00:00 PM (1600-1700)	5.7872	2.3022	5.3481	2.3022
6:00:00 PM (1700-1800)	5.7872	2.3022	5.7872	2.4256
7:00:00 PM (1800-1900)	6.3283	5.5790	6.3283	5.3481
8:00:00 PM (1900-2000)	6.3283	5.5790	5.7872	5.3481
9:00:00 PM (2000-2100)	5.7872	3.0594	5.5790	2.4256
10:00:00 PM (2100-2200)	3.0594	2.4256	2.4256	2.3022
11:00:00 PM (2200-2300)	2.4256	2.3022	2.3022	2.1426
12:00:00 AM (2300-2400)	2.3022	2.1426	2.1426	2.1426

b. In the event that the rates provisionally approved are found to be higher than the final rates, the amount corresponding to the excess shall be refunded by CAGELCO I to its member-consumers by crediting the same in their electric bills over a period to be determined by the Commission.

*CAGELCO I is hereby directed to **PASS ON** to its member-consumers fifty percent (50%) of the Prompt Payment Discount (PPD) availed from SMEC and fifty percent (50%) of the Collection Efficiency Discount granted to it."*

On 26 September 2012, CAGELCO I filed its "Formal Offer of Evidence".

On 22 November 2012, CAGELCO I filed an "Urgent Manifestation with Motion".

On 12 February 2013, the Commission issued an Order extending the provisional authority granted to CAGELCO I in the Order dated 10 September 2012 until revoked or made permanent since it was still in the process of evaluating the application.

On 25 November 2013, the Commission issued an Order admitting CAGELCO I's formal offer of evidence for being relevant and material in the evaluation of the application.

On 17 August 2015, the Commission deliberated and decided the instant Application. However, due to supervening events[2], the Decision could no longer be promulgated without undergoing reconfirmation by the Commission *En Banc*. Thus, the Commission resolved to reconfirm the Decision on 15 June 2017.

DISCUSSION

1. SMEC's Proposed Rates

The proposed rates of SMEC with various distribution utilities (DUs) were structured as Time-of-Use (TOU) Rates at the following Basic Energy Rates (BER):

SMEC Basic Energy Rate, PhP/kWh						
Year 2010 to 2011, PhP/kWh			Year 2012 Onwards, PhP/kWh			
4.1648	4.2648	4.3248	4.5448	5.0522	5.2522	5.4656
			5.5317	5.6261	5.9287	5.9739

SMEC opted to maintain the design of the National Power Corporation (NPC) TOU rates by simply deducting or adding, as the case may be, the difference between its BER and NPC Average Generation Rate on top of each hourly rate interval. Thus, similar with the NPC TOU design, SMEC was able to establish four (4) sets of hourly TOU rate schedules with similar Dry and Wet as well as Weekday and Weekend rates.

SMEC averred that the PhP4.1648/kWh initial rate it offered to distribution utilities during the period December 2009 to January 2010, is based on projected operating cost considering that it is relatively new to the industry and its operating cost is not yet fully established. The PhP4.1648/kWh initial rate, which is lower than NPC's then prevailing Basic Generation Rate by PhP0.20/kWh, was offered to attract potential buyers.

For its subsequent offers to other DUs, SMEC, in calculating its proposed average BERs of PhP4.2648/kWh, PhP4.3248/kWh and PhP4.5448/kWh - PhP5.9739/kWh for calendar years 2010, 2011 and 2012 onwards, respectively, considered the following assumptions and major cost components:

[2] The Chairman was placed on preventive suspension as per Order of the Office of the President (OP-DC Case No. 17-D-094) dated 2 May 2017 and received on 04 May 2017.

a. Average fuel and other variable costs at December 2009 base prices;

b. Estimated total annual operating, fixed, general and administrative costs; and

c. Reasonable margin that would allow it to operate viably and supply reliable electricity to its customers.

Coefficients for Years, 2010, 2011, 2012, 2013, and Onwards

Coefficients	Years 2010 and 2011					
	(PhP/kWh)	%	(PhP/kWh)	%	(PhP/kWh)	%
A	2.0770	50.00	2.0770	48.70	2.0770	48.00
B	0.6066	15.00	0.5678	13.30	0.5257	12.20
C	1.4812	35.00	1.6201	38.00	1.7221	39.80
Total	**4.1648**	**100.00**	**4.2648**	**100.00**	**4.3248**	**100.00**

Coefficients	Years 2012, 2013, and Onwards							
	(PhP/kWh)	%	(PhP/kWh)	%	(PhP/kWh)	%	(PhP/kWh)	%
A	2.0770	45.70	2.8439	56.29	2.5456	48.50	2.5717	47.10
B	0.5257	11.60	0.4815	9.53	0.6872	13.10	0.7661	14.00
C	1.9421	42.70	1.7268	34.18	2.0194	38.40	2.1278	38.90
Total	**4.5448**	**100.00**	**5.0522**	**100.00**	**5.2522**	**100.00**	**5.4656**	**100.00**
A	2.5175	45.5	2.6723	47.50	2.5425	**42.90**	2.5467	**42.60**
B	0.8150	14.7	0.8582	15.20	0.9715	**16.40**	0.9890	**16.60**
C	2.1992	39.8	2.0956	37.30	2.4147	**40.70**	2.4382	**40.80**
Total	**5.5317**	**100.00**	**5.6261**	**100.00**	**5.9287**	**100.00**	**5.9739**	**100.00**

Where:

A = Fuel, Energy Fees and other variable operating costs

B = Fifty percent (50%) (Foreign) Component of Amortization of IPPA Fees

C = All Other Revenue Requirement including fifty percent (50%) (Local) Component of Amortization of IPPA Fees

SMEC submitted that its proposed annual average of PhP4.2648/kWh is lower than NPC's then prevailing Basic Generation Rate (PhP4.3648/kWh annual average) by PhP0.10/kWh. However, the PhP4.3248/kWh proposed BER for calendar year 2011 and PhP4.5448/kWh proposed BER for calendar year 2012 is PhP0.04/kWh lower and PhP0.18/kWh higher, respectively, than the then prevailing NPC Average TOU rate of PhP4.3648/kWh, as shown below:

Year	SMEC's BER (PhP/kWh)	NPC's Average TOU (PhP/kWh)	Difference (PhP/kWh)
2010	4.2648	4.3648	(0.1000)
2011	4.3248	4.3648	(0.0400)
2012	4.5448	4.3648	0.1800

SMEC further manifested that the PhP0.10/kWh and PhP0.04/kWh negative differences as well as the PhP0.18/kWh positive difference is neither a discount from nor a premium on top of the existing NPC TOU Rates since the average BERs of PhP4.3248/kWh for the contract period 26 June 2011 to 25 December 2011 and PhP4.5448/kWh for the contract period 26 December 2011 to 25 December 2012 were derived from its calculation of the estimated generation costs to supply a contracted customer.

Moreover, it averred that its calculations do not specifically identify the variance with any specific cost over and above the prevailing average NPC TOU Rates as the latter was computed based on NPC's financial costs for calendar year 2007, as provisionally approved by the Commission in its Order dated 16 February 2009 in ERC Case No. 2009-004 RC[3].

2. Evaluation of the Proposed Rates

To ensure that the base electricity fees would allow only for the recovery of prudent and reasonable costs incurred, the Commission made an evaluation of SMEC's true cost of generation by referring to the historical cost of operations as reflected in its 2010 to 2012 Audited Financial Statements (AFS). The figures reflected in the AFS represent the actual costs incurred which was objectively verified and validated by an Independent Third Party.

Using the audited data and other available information, the Commission made an evaluation to determine the reasonableness of SMEC' s proposed rates and approximate the same to its true cost of generation. Thus, in computing for the recoverable generation rate, the Commission considered the following rate components:

a. **Capital Recovery Fee (CRF)** - refers to the recovery of SMEC's invested capital as an IPPA plus a reasonable return;

b. **Operations and Maintenance (O&M) Fee** - refers to recovery of the general and administrative expenses incurred by SMEC in the performance of its functions as the IPPA of its contracted capacity;

[3] In the Matter of the Application for the Approval of the Proposed New Basic Generation Rates for Luzon, Visayas and Mindanao Grids with Prayer for Provisional Authority, NPC and PSALM – Applicants.

c. **Energy Fee** - refers to recovery of the monthly energy fees paid by SMEC to PSALM (equivalent to the amount paid by NPC/PSALM to the IPP). The energy fees, similar to the Monthly Capacity Fees, have a Peso and Dollar denominated base fees; and

d. **Fuel Cost** - refers to recovery of the cost of fuel used by the IPP to generate the contracted capacity. Under the IPPA Agreement, the Administrator has the obligation to supply and deliver the fuel requirement of an IPP for the contracted capacity in accordance with the specifications of the original Energy Conversion Agreement (ECA). It is a pass-through cost, subject to guaranteed heat rates under the said IPPA Agreement.

2.1 Capital Recovery Fee

In computing the applicable CRF, the Commission determined the capital cost for recovery, the return on working capital and the saleable generation (Billing Determinant) of the Sual Power Plant.

The Commission used the net amount of Property, Plant and Equipment (PPE) reflected in SMEC's 2012 AFS as the appropriate asset base.

In accounting for its IPPA Agreement, SMEC considered the same as an agreement that contains a lease since it has substantially acquired all the risks and rewards incidental to the ownership of a power plant. Accordingly, it accounted the said agreement as a finance lease and recognized the power plant in its books as non-current asset under PPE.

The power plant was valued equal to the present value of SMEC's future payments to PSALM using the Philippine peso and US dollar discount rates.

The use of net amount of PPE is similar with the methodology typically adopted by the Commission relative to IPPs where capital investment for construction of power plant is incurred at the beginning or to those that pay for the plant acquisition cost upfront.

The CRF was computed using an asset base equivalent to the net amount of PPE as reflected in SMEC's 2012 AFS and a return equal to the previously approved Weighted Average Cost of Capital (WACC) of 13.59%, as approved by the Commission in its Decision dated 30 July 2012 in ERC Case No. 2011-138 RC[4].

In computing the billing determinant, the Commission used the actual kWh sales of SMEC.

2.2 Operations and Maintenance Fee

For the O&M Fee computation, the Commission made reference to SMEC's actual cost of operations, as disclosed in its 2010, 2011 and 2012 AFS.

The Commission disallowed the Provision for Impairment Losses of Receivables since it is a non-recurring expense. Likewise, the Commission disallowed the cost corresponding to Donations (or charitable contributions) since these are typically classified as non-generation expense which are generally for the account of the company and not intended for recovery from the customers. The Commission also excluded the Depreciation Expense for Furniture and Fixtures and Equipment since the same were already included in the net amount of PPE used in the computation of the CRF.

2.3 Energy Fee

The Energy Fees were verified to be pass-through costs representing the monthly charges that an IPPA is required to pay PSALM under their IPPA Agreement. This is a "back-to-back" payment as defined in the ECA and which are charged, and payable to the IPP. The obligation of NPC/PSALM to pay Energy Fee to the IPP was basically transferred to its appointed IPP Administrator, in this case, to SMEC.

This cost component is for the recovery of the monthly energy fees that SMEC pays to PSALM for the actual energy delivered by the IPP (equivalent to the amount paid by NPC/PSALM to the IPP). The Energy Fee is similar to the Monthly Capacity Fee, which has both Peso and Dollar denominated base fees and are adjusted using the Philippine and US CPIs, respectively.

---

[4] In the Matter of the Application for Approval of the Power Sales Agreement, as Amended, Among South Cotabato II Electric Cooperative, Inc. (SOCOTECO II), Conal Holdings Corporation (CHC) and Sarangani Energy Corporation (SEC), SOCOTECO II and SEC - Applicants

In computing for the base Energy Fee, the Commission referred the same to the actual Energy Fees paid by SMEC to PSALM in years 2010, 2011, and 2012, as reported in its AFS for the said years.

The Commission computed the applicable Energy Fees based on the average actual energy cost from 2010 to 2012 and the average actual kWh generated by the Sual Power Plant in relation to the 1,000 MW contracted capacity during the relevant periods.

2.4 Fuel Fee

In the same IPPA Agreement, SMEC has the obligation to supply and deliver, at its own cost, all fuel requirements of the power plant in accordance with the specifications provided in the ECA.

In computing the base Fuel Fee, the Commission made reference to the actual Fuel Cost incurred by SMEC for the years 2010, 2011 and 2012, as reported in its AFS for the said years.

Similar with its derivation of the Energy Fees, the Commission computed the applicable Fuel Fee based on the average actual fuel cost from 2010 to 2012 and the average actual kWh generated by the Sual Power Plant in relation to the 1,000 MW contracted capacity during the relevant periods.

2.5 Rate Derivation

Based on the foregoing discussions, the Commission initially derived a levelized generation rate applicable for SMEC.

Subsequently, the Commission made a comparison between and among its computed levelized generation rate and SMEC's proposed rates with various DUs.

The proposed rates of SMEC with said various DUs were designed to be competitive with the then prevailing prices in the market and to ensure that it will be able to pay the expected costs, specifically, its fixed monthly payment to PSALM as embodied in their IPPA Agreement. The said fixed monthly payments to PSALM are increasing throughout the term of the IPPA Agreement, or from January 2010 until October 2024. This is the main reason why the proposed rates vary depending on the cost assumptions of SMEC during the period of negotiation with its customers.

On the other hand, the Commission's computed generation rate is not reflective of SMEC's increasing monthly payments to PSALM. Instead, the rate was computed based on SMEC's levelized annual revenue requirement.

For purposes of determining the reasonableness of SMEC's proposed rates vis-à-vis the computed generation rate under the cost-based methodology, the Commission determined the former's weighted average rate based on the proposed rates under its ESCs and the expected electricity sales to its customers.

Moreover, the Commission considered the effects and benefits of implementing such rates to the end-consumers and the effects thereof on the financial viability of SMEC in providing reliable supply to its customers.

Based on its simulation, the Commission found that the weighted average of SMEC's proposed rates under its ESCs is reasonable as the same is within the level of the computed generation rate for SMEC. Thus, the Commission approves the proposed rates under the subject interim PSA as the same will redound to the benefit of CAGELCO I's member-consumers.

3. Evaluation of the Non-Rate Provisions of the Interim PSA

A thorough evaluation of the interim PSA entered into by and between CAGELCO I and SMEC disclosed that the non-rate provisions thereof are reasonable and in accordance with accepted industry practice, except the following provisions:

> *"2nd paragraph of Section 3.1 (Contract Duration and Effectivity)*
>
> *In the event that ERC issues an order, provisional or otherwise, disapproving any of the terms of the Contract that will effectively amend the agreement of the Parties, the Parties shall endeavor to renegotiate the Contract no later than sixty (60) days from effective date of such ERC approval/amendment. In the event that no such agreement is reached by the Parties within this period of sixty (60) days, the original terms of this Contract shall prevail. For the avoidance of doubt, until the Parties have mutually agreed on the*

> *amendment of the terms* of *this Contract, the terms and conditions* as *originally specified herein shall Prevail."*

The Commission believes that this Decision should bind both contracting parties and that their interim PSA shall not be rendered ineffective or nugatory by any termination or "walk-away" clause in the interim PSA by reason of this Decision. Thus, the Commission deems it prudent to disallow the foregoing provisions.

As regards the provision wherein a customer is not a direct WESM member, the interim PSA provides that:

> *"Section* 4.3.a *Customer is not* a *Direct WESM Member.*
>
> *Whenever available, in accordance with good utility practice, the SUPPLIER may, but shall not be obliged to provide electricity to the CUSTOMER in excess of Contract Energy, provided that for consumption in excess* of *one hundred twenty percent (120%)* of *the Contract Energy level, the basic energy charge to be applied shall be the Basic Energy Rate including but not limited to other adjustments or the WESM rate, whichever is higher, plus ten percent (10%)* of *such rate."*

The Commission finds the foregoing to be unreasonable. In this regard, the Commission deems it necessary to modify the same so that: *"In the event that the SUPPLIER provided electricity in excess of one hundred twenty percent (120%) of the contracted energy to the CUSTOMER, the basic energy rate shall be the actual cost incurred by the SUPPLIER in providing such additional energy. For electricity purchased beyond the contracted energy but within one hundred twenty percent (120%) thereof, the rate shall be the approved basic energy rate".*

The Commission has a mandate to protect the interest of the electricity consumers insofar as they are affected by the rates, by ensuring that the tariffs imposed are consistent with the principle of full recovery of prudent and reasonable costs.

After a thorough evaluation of the documents submitted and the testimonies of the witnesses presented, the Commission finds that the approval and implementation of the interim PSA will be beneficial to CAGELCO I's member-consumers by way of reliable, continuous and efficient supply of power within its franchise area at reasonable costs as mandated by the Electric Power Industry Reform Act of 2001 or the EPIRA *[Section 2. Declaration of Policy - (b) "to ensure the quality, reliability, security and affordability of the supply of electric power"].*

WHEREFORE, the foregoing premises considered, the provisional authority granted to Cagayan I Electric Cooperative, Incorporated (CAGELCO I) on 10 September 2012 in relation to this application, is hereby made **PERMANENT,** subject to the following modifications:

1. The applicable base rates shall be the Time-of-Use (TOU) rates provided under the interim PSA, which shall be adjusted in accordance with the Adjustment Formula stated therein; and

2. SMEC's actual cost of operation and construction shall be audited by an Independent Third Party, in accordance with the rules to be promulgated by the Commission, and the approved rates herein shall be adjusted, if warranted. The test of reasonability shall be *"whether or not such cost is incurred based on a good utility practice and comparable or within the level of the power plants similarly situated to that of SMEC"* and **NOT** the actual cost incurred. The cost of audit shall be shouldered by SMEC.

The Commission further **RESOLVES** to:

1. **DISALLOW** the termination or "walk-away" clause (2nd paragraph of Section 3.1) incorporated in the interim PSA;

2. **MODIFY** the provision of the interim PSA under Section 4.3.a (Customer is not a Direct WESM Member), so that: *"In the event that the SUPPLIER provided electricity in excess of one hundred twenty percent (120%) of the contracted energy to the CUSTOMER, the basic energy rate shall be the actual cost incurred by the SUPPLIER in providing such additional energy. For electricity purchased beyond the contracted energy but within one hundred twenty percent (120%) thereof, the rate shall be the approved basic energy rate";*

3. **DIRECT** CAGELCO I and SMEC to **SUBMIT,** within thirty (30) days from receipt hereof, their proposed refund or recovery scheme, as the case may be, for the difference between the final approved rates and the provisionally implemented rates; and

4. **DIRECT** CAGELCO I to **PASS ON** to its member-consumers fifty percent (50%) of the Prompt Payment Discount (PPD) availed from SMEC and fifty percent (50%) of the Collection Efficiency Discount (CED) granted to it.

SO ORDERED.

Pasig City, 15 June 2017.

JOSE VICENTE B. SALAZAR*
Chairman and CEO

ALFREDO J. NON
Commissioner

GLORIA VICTORIA C. YAP-TARUC
Commissioner

JOSEFINA PATRICIA A. MAGPALE-ASIRIT
Commissioner

GERONIMO D. STA. ANA
Commissioner

LS: ARC/LSB/ APV

TWG-B: LOC/AJMO/FCBD

*The Chairman was placed on preventive suspension as per Order of the Office of the President (OP-DC Case No. 17-D-094) dated 2 May 2017 and received on 04 May 2017.

Copy Furnished:

1. Atty. Ranulfo M. Ocampo
   Counsel for CAGELCO I
   8th Floor, STRATA 100 Bldg.,
   F. Ortigas Jr. Road, Pasig City

2. Cagayan I Electric Cooperative, Incorporated (CAGELCO I)
   Maddarulug, Solana, Cagayan

3. San Miguel Energy Corporation (SMEC)
   2nd Floor, 808 Building, MERALCO Avenue
   corner General Lim St., San Antonio Village, Pasig City

4. Office of the Solicitor General
   134 Amorsolo St., Legaspi Village, Makati City

5. Office of the Commission on Audit
   Don Mariano Marcos Avenue, Diliman, Quezon City

6. The Committee On Energy
   Senate of the Philippines
   GSIS Building, Roxas Blvd., Pasay City

7. The Committee On Energy
   House of Representatives
   Batasan Hills, Quezon City

8. Office of the Municipal Mayor
   Alcala, Cagayan

9. Office of the Municipal Mayor
   Amulung, Cagayan

10. Office of the Municipal Mayor
    Baggao, Cagayan

11. Office of the Municipal Mayor
    Enrile, Cagayan

12. Office of the Municipal Mayor
    Iguig, Cagayan

13. Office of the Municipal Mayor
    Peñeblanca, Cagayan

14. Office of the Municipal Mayor
    Piat, Cagayan

15. Office of the Municipal Mayor
    Rizal, Cagayan

16. Office of the Municipal Mayor
    Solana, Cagayan

17. Office of the Municipal Mayor
    Sto. Niño, Cagayan

18. Office of the Municipal Mayor
    Tuao, Cagayan

19. Office of the City Mayor
    Tuguegarao City, Cagayan

20. Office of the Provincial Governor
    Province of Cagayan

21. Philippine Chamber of Commerce and Industry (PCCI)
    3rd Floor, Chamber and Industry Plaza (CIP),
    1030 Campus Avenue corner Park Avenue,
    McKinley Town Center, Fort Bonifacio, Taguig City

22. PSA-TWG B
    Energy Regulatory Commission
    17th Floor, Pacific Center, San Miguel Avenue, Pasig City