

MSK RESPONSE TO

MERALCO COMMENT DATED MAY 18, 2015

ERC Case No. 2014-006-RM

The Crux of the Petition of MSK ( Matuwid na Singil sa Kuryente Consumer Alliance) is whether open competitive bidding as we propose or Meralco's practiced preferred negotiated bids will better serve the interest of the consumers. In this case, which one will bring lower cost in generation rates?

Corollary to this is whether there can be a truly competitive bidding if the sister company or even subsidiary of the DU can participate. **Opening the DU and Meralco market to true competitive bidding is actually the antidote to harmful monopolization of power generation.**

It is evident that Meralco, is attempting to obfuscate the real issue by anchoring the justification for their seizure of the opportunities to negotiate power supply agreements with their majority owned sister companies, on two strategies:

### **1. Raise the Specter of Power Shortage**

It is pathetic that 20 years after the power crisis of the early 1990's Meralco continues to try to justify the right to negotiate power supply contracts by always scaring the consumers of the horrors of a power shortage. In essence they are saying that if they are not allowed to negotiate the bilateral contracts, there will be a power shortage that will devastate and cripple the economy. Consumers deserve more respectful treatment from its public service provider.

The truth of the matter is Meralco had not facilitated the building of new capacity (negotiated or tendered) since the building of the First Gas Plants in mid 2006. That's almost ten (10) years ago. If they truly cared about assuring power supply, they had plenty of time to conduct an open bidding even if we assume that there is a one (1) year process to prepare for a truly open bidding.

The Metro-Pacific Group that now controls Meralco took over management on May 30, 2012. Within one year or May 2013 they could have held open competitive bidding for 2,000 mw of additional power that they claim they needed by 2015. Instead they negotiated 25 year power supply agreements for their majority owned 600mw Redondo Power in Subic and the 440mw expansion of Quezon Power facility in Mauban Quezon in partnership with a EGAT of Thailand. **Neither plant will be on line by 2015 which belies their claim that holding biddings will take longer and ergo their negotiated contracts are faster and will come on time to address power shortages.**

Meralco could have taken the same time by conducting an open bidding. And they could have gotten a better price for its consumers than the P4.30 per kwh they negotiated for Mauban.

Eight (8) electric coops in Northern Luzon held an open tender for 120mw and they got a price of P3.76 per kwh.

That's approximately 14% higher price or P1.5 billion more per year for Meralco consumers.

An analysis of Meralco's generation cost data for the months of October 2014 to January 2015 by consumer group Matuwid na Singil sa Kuryente Consumer Alliance.(MSK) showed that Meralco has been buying and passing on to consumers P13.68 billion more per year for the higher rates of its sister company generators compared to those of non-affiliated power generation companies.

From October 2014 to January 2015, Meralco's non-affiliated power generation suppliers averaged in price only at P3.4885 per kwh whereas Quezon Power in Mauban averaged P4.65 per kwh or P1.16 per kwh or 33% more.

Of the three (3) generators selling natural gas power to Meralco, San Miguel's 1,200mw SPPC Ilijan is non-affiliated and supplies power at P4.4542 per kwh. The Lopez owned First Gas Power are charging P5.4151 per kwh for 1,000mw Sta.Rita and P5.5182 per kwh for the 500mw San Lorenzo, for an average of P5.466 per kwh or a full P1.01 per kwh or 23% higher. They are all using the Malampaya Natural Gas at presumably the same fuel prices and terms.

The two First Gas plants supply 35.6% of the energy purchases of Meralco, an average of 17.8%. That translates to 3.394 billion kwh in the four months. At the higher rate of P1.0124 per kwh, the higher cost to the Meralco consumers is a whopping P3.346 Billion for October to January.

In total, the Meralco consumers have paid P4.56 billion more for the higher contracted rates for Meralco's sister company generators just for the four months from October 2014 to January 2015, or a total of P13.68 billion for 12 months.

These are irrefutable evidence that negotiated contracts between Meralco and its sister company generators are atrociously disadvantageous and damaging to Meralco captive consumers and certainly contrary to the idea of least cost power.

**Meralco's concern for "time element" in assuring power supply is belied by their own failure to hold proactive biddings in sufficient advance timeframe. A multi-billion public service utility like Meralco that passes on to the consumers tremendous budgets for utility planning and engineering should have the expertise and foresight to plan ahead and procure in a timely basis.**

**Their claim for "urgency of need" is only an admission of their failure to plan ahead. Or a giveaway that they systematically create an "urgency of need" to justify an urgent power supply contract at high prices with a sister company. The now commonly used mantra "the most expensive power is being without power" is a perpetuation of the power crisis syndrome.**

**There is no power crisis now but there will be if Meralco continue refusing to open its power supply market and waiting for its own subsidiaries to find partners who will agree to be minorities in the IPP ventures and get the needed financing.**

## **2. Buttering Up the Regulators**

In Paragraphs 5, 8,9,10,11 of their Comments it is clear that Meralco is trying to butter up the Regulators by pointing out that it has the “technical expertise”, the “regulatory power”, the “rigorous evaluation” process, and its “power and duty to ensure a reasonable price of electricity”.

In a subtle way, Meralco is trying to incite the Honorable Commission against the Consumer Petitioners by practically saying “look it is your regulatory power and expertise that is being challenged here”. We hope the Honorable Commission does not fall for it.

***The issue here is neither the regulatory power nor the expertise of the ERC but the non-competitive and non-transparent process of negotiated buying power supply, especially between Meralco and its sister generator suppliers, that result to higher rates that are passed on to the consumers.***

## **3. “Least Cost power”**

Meralco in its comments is profuse in its mention of the word “least cost power”, which the Epira Law provided under Section 23 is its obligation to provide its consumers as a distribution utility. See Paragraphs 17, 18,21,22,23.

**Meralco, as a distribution utility that has never subjected its power requirements to open competitive bidding since the passing of the Epira Law in 2001 in a true search for “least cost power” has no right to now wave the flag of that sacred mandate for public services.**

Under Paragraph 25, Meralco apparently is attempting to obfuscate even the simple meaning of “least cost power” by supposing that “the deemed lowest bid is not the least cost that could be procured”. It is fundamental in power supply tendering that the lowest bid price is the lowest responsive bid that includes all factors and indices. The consumers would like to hear Meralco’s ingenious definition of “least cost power”.

When is the “lowest” not the “least”? There are many ambiguities in the Epira Law and the governments various rules, resolutions, and circulars. There are grey areas and

loopholes. But the meaning of “least cost power” for the consumers is one of those unassailable ones. It is eerie for the consumers that even this sacred and clear mandate is being muddled by Meralco.

***Other than that, Meralco had not really presented any reason why negotiating power supply contracts with its sister companies would be good for consumers and will give them least cost power, by its simple definition.***

DU’s like Meralco can likewise achieve optimum energy mix by carefully designing its tender terms of reference and defined scope of service. The competitive market should be allowed to come up with competitive solutions for base-load, mid-merit, and peaking requirements of Meralco.

***MSK submits that the only way to really achieve “least cost power” for the DU is to conduct its procurement of power supply in a way that is devoid of conflict of interest, on arms-length basis, and under a truly open and competitive bidding exercise, where the market forces of supply, demand, and transmission access truly interplay to result to the least cost power to the consumers.***

***It is time that the true pursuit of “least cost power” defines Meralco as a public services provider. They only have been using it as lip service, public relations tagline, and a convenient byword.***

#### **4. Deceptive Comparisons**

Under Paragraph 7, Meralco attempted to explain away its higher sweetheart prices for the First Gas Sta. Rita and San Lorenzo natural gas plants by comparing them to the Calaca, Masinloc, Pagbilao, and Sual plants which are all coal.

Meralco should be comparing the prices of First Gas Sta. Rita (1,000mw) and San Lorenzo (500mw) with a similar natural gas plant which is the Ilijan 1,200mw natural gas plant owned and operated by Kepco and now under the IPPA of San Miguel. The two (2) First Gas plants averaged in priced at P5.47 per kwh compared to only P4.45 per kwh for the Ilijan plant which was subjected to open competitive bidding. That’s a difference of P1.02 per kwh.

If Meralco wishes to compare coal plants with coal plants, then they should realize that the average of the coal power plants in Calaca, Masinloc, Pagbilao, and Sual was P3.49 per kwh for the four months October 2014 to January 2015 compared to the negotiated Quezon Power price of P4.65. That’s a 33% price difference even after the Board

Committee Review that is claimed by Meralco to have reduced the rates to the consumers.

The First Gas Plants enjoy MEOT capacity payments so their dispatching level actually do not matter to its owners because they get paid, dispatched or not. On comparative Asset Lives (Par. 7.3) of these Meralco generators, records will show that all three natural gas plants running on Malampaya gas were built at about the same time frame. Similarly, the QPL Mauban plant was built in the mid 1990's as the Sual and Pagbilao coal plants. Asset life should not be an excuse for higher rates. The price disparity can be attributed to the fact that the First Gas Plants (Sta.Rita and San Lorenzo) and QPL were affiliated generators at the time their sweetheart contracts were negotiated and the rest of the plants under PSA are not related to Meralco.

**We are submitting as Attachment A the tabulation of the Meralco generation buying rates for the four month period October 2014 to January 2015. These prices can be validated by Meralco from its own generation cost data. Contrary to their claim that MSK had not submitted any supporting data, these were presented during the ERC hearing for this application last March 23, 2015.**

**5. EPIRA Laws Provision of Manner of Procuring Power Supply and Legality of ERC's mandating competitive bidding for power supply for the captive customers.**

We take exception to Meralco's claim under its Paragraph 12 that the "EPIRA gives DU's freedom to choose the best means of procuring supply for their captive customers". Section 45(b) of the Epira while allowing the DU's contracting with an affiliated company up to a maximum of 50% of its power requirements, is actually silent on the issue of how the procurement will be undertaken.

***It should be noted that for all those who truly care about public interest, the Epira Law premises the implementation of these rules to be "in the public interest". This we submit can only mean lower rates (least cost power).***

**The Epira Law specially Section 45(b) does not prohibit the ERC from requiring open competitive bidding of power supply contracts specially for those intended to serve the captive customers, who have no benefit at all of competition in their generation rate as compared to the large users who are contestable customers.**

Meralco has highly publicized programs to reduce the power cost of large commercial and industrial users. However, they have nothing for the captive customers which comprise at least 60% of their revenue. In fact, **by their opposition to MSK's petition to subject power supply for the captive customers to open competitive bidding, Meralco is actually trying to deny its preponderant captive customers this benefit and to allow their good times of negotiated sweetheart bilateral contracts to roll for their sister company generators.**

**We ask that the ERC does not participate in the continuation of injustice to these captive customers that compromise 45% of Meralco customers but pays more than 60% of their revenue.**

**The much ballyhooed "Retail Competition and Open Access" or RCOA is again designed only for the contestable customers.** Even in this market segment, Meralco's competitive position can be strengthened by them procuring more competitively by bidding the generation supply and offering lower rates to the contestable customers. For example, instead of negotiating a rate of P4.30 per kwh for the 440mw Mauban coal expansion, had they conducted a competitive bidding, they could have gotten say P3.75 per kwh and offered their contestable customers say P3.95 per kwh.

## **6. Reasonable Reliance on the WESM**

Contrary to Meralco's assertions under Paragraph 19 as to their **reasonable reliance** on the WESM, Meralco has been being unreasonably reliant on the WESM as the default excuse for their rate increases since the Spot market was born in 2006. Records will show, especially in the fiasco of December 2013, that Meralco has always been blaming the WESM (that and Malampaya supply interruptions) as their convenient excuse for periodic spikes in rates. In those fateful months, it turned out that the reason they had to buy a disproportionate amount of power from the WESM was because of the failure of their power generators to deliver power including their sister company generators. We are submitting herewith as Attachment B our analysis of the behavior of the Meralco power generators during the fateful months of November and December 2013 as summarized in our article "Is Meralco Telling Whole Story?". It was clear that Meralco's reasonable reliance on WESM did not serve the consumers well and in fact turned out to be very costly and certainly contrary to the words and spirit of "least cost power".

***WESM has a role in the power supply system of the country but Meralco must assure sufficient and reliable contracted bilateral contracts. That can be achieved only if they***

*open their market to the resources and technology expertise of outside investors. By forming their own Meralco PowerGen and openly declaring they will take advantage of the opportunities in the power generation sector by supplying the next 3,000mw of Meralco's power supply, their intent to negotiate and monopolize power generation is clear and should alarm the electric consumers, and the Honorable Commission who has the mandate to protect the public interest.*

*Faithfulness to "least cost power" not only means buying power at the lowest price possible but also managing its systems and administering their power supply contracts in ways that reduce the actual pass on charge to the electric consumers.*

## **7. True Competition Should be the Primary Protection for Consumers, Regulation only as Safeguard.**

Meralco negotiated a 460mw bilateral contract for the expansion of the Mauban coal power complex. The company will be majority owned by Meralco PowerGen with minority partner EGAT of Thailand as operator.

The negotiated price was P4.35 per kwh. After "rigorous regulatory review" the ERC reportedly reduced the rate to P4.29.

Comparatively, a group of eight (8) electric cooperatives who distribute power in the Northern provinces, aggregated their 125mw power requirement and undertook a competitive bidding. They got P3.78 per kwh.

The 12% price difference will translate to an additional cost to Meralco consumers by at least P1 billion a year.

**True competition should be the primary protection for consumers, regulation should only be a safeguard.**

## **8. Department of Energy circular DC2015-06-0008 Mandating All Distribution Utilities to Undergo Competitive Selection Process (CSP) in Securing Power Supply Agreements (PSA).**

On June 30, 2015 the Department of Energy issued this Circular mandating all distribution utilities to undergo competitive selection process in securing power supply agreements. It covers all the requirements of the distribution utilities not yet applied for or approved by the ERC.

We are presuming that this covers Meralco's future requirements unless secretly the 3,000mw of Meralco PowerGen have been filed with the ERC.

This DOE circular establishes a new government policy in line with the Epira to require competitive bidding for power supply contracts by distribution utilities, including Meralco.

**We beseech the Honorable Commission to expedite the passing of the enabling regulatory rule to provide teeth and meaning to this circular that can finally usher in an era of true competition in the power generation sector.**

**9. Meralco's issues on the Mechanics of the Competitive Bidding rules as contained in their Annex "A".**

We believe the Honorable Commission should rule first on whether open competitive bidding will be required for bilateral power supply contracts specially those intended to serve the captive customers before we tackle the details of the mechanics.

The concepts submitted by the MSK are only ideas to get the process started. The mechanics and procedures can be worked out in the next stage for which purpose the ERC can form a technical working group including the IPP's and Meralco on the specific rules for the biddings.

Nonetheless, we would like to comment on some of the assertions:

**A) Impact of RCOA**

It is inconsistent for Meralco to raise the issue of impact of a possible significant customer migration under RCOA on its contracted bilateral contracts when asked that they submit these bilateral contracts to open competitive bidding. However, they don't exhibit any qualms about this issue when announcing their 3,000 mw target of bilateral contracts with Meralco PowerGen. Meralco should not use the same argument as both "shield and saber" whenever and wherever convenient.



Having said that, **our proposal for mandatory competitive bidding would be for the power supplies intended for the captive customers who are anyway not eligible for RCOA.**

Meralco can hold biddings for a level of “revisable” contracts where the contracted capacities or energy can be revised as a result of RCOA. Let the open competitive market also decide on the price of such revisable contracts.

**B) Submission of Energy Mix**

The proposed submission of the Energy Mix to the DOE is for the purpose of allowing a proper assessment of a proposed power supply contract on how it fits into the energy mix. Obviously, the bidding will not be for the energy mix or “portfolio of plants” as interpreted by Meralco.

**C) Locational Strategy**

Grid congestions are not “invisible” to Meralco. We propose that Meralco consider locational strategy of power sources in holding biddings. For example, it is clear that transmission capacities in the Batangas to Manila corridor is already reaching its physical limits. Meralco then should identify where in general new sources can be located. Directly or through the DOE it can coordinate with the NGCP on transmission capacities and advisable power generation locations.

This is as opposed to the current situation where Genco’s locate wherever convenient for them giving the burden of building new transmission facilities to NGCP. Even if the connection line is built by the Genco it still represent additional charges to consumers.

**10. A minimum Compromise for the Consumers**

**Consumers will be happy if the era of true competition in the generation market is ushered in. As a compromise we are willing to accept that the competitive bidding program start first with the base-load and intermediate requirements of Meralco.**

**PRAYERS**

1. For the Honorable Commission to urgently issue a Resolution adopting competitive bidding for bilateral power supply contracts for base-load and intermediate requirements of Meralco and other Distribution Utilities on the national grid consistent with the Department of Energy Circular DC2015-06-0008. Implementing guidelines can follow after the issuance of a similar implementing guidelines from the Department of Energy. To order the creation of a consultative group to finalize the framework of the bidding within 60 days to include stakeholders PIPPA, Meralco, DU's, EC's, MSK, and PCCI.
2. For the Honorable Commission to require all DU's specially Meralco to submit for the record their new bilateral power supply contracts that have been approved by or applied with the Energy Regulatory Commission as of June 30, 2015. We request that consumers and MSK be furnished copies of such new contracts and ERC applications.

MSK

