

Matuwid na Singil sa Kuryente Consumer Alliance Inc. (MSK)

Comments on the Draft Implementing Guidelines of Section 3 of the DOE
Department Circular No DC2015-06-0008

1 October 2015

The Matuwid na Singil sa Kuryente Consumer Alliance respectfully submits its Comments on the Draft Implementing Guidelines.

1. Premises

We agree with the invocation of the Policy of the State set down by the Epira Law of 2001 under its Section 2.

c) A mandatory Competitive Selection Process will *"ensure transparent and reasonable prices of electricity in a regime of free and fair competition and full public accountability"*.

Negotiated contracts between a DU and its sister company generator are non-transparent, bereft of public accountability, stifles free and fair competition, and certainly result to unreasonable prices of electricity. A Regulatory review by the ERC is only a safeguard but should not be a substitute for fully transparent and competitive bidding process to truly protect the public interest.

d) A mandatory CSP will open the currently closed generation market and will *"enhance the inflow of private capital and broader the ownership base of the power generation sector"* and not just the affiliated generators of the DU.

f) Certainly, a mandatory CSP will *protect the public interest*.

2. Mandates of the Department of Energy under Section 37 of the EPIRA

We agree that the Circular and Mandatory CSP would be in long overdue compliance with the following mandates of the DOE

(i) *"Develop policies and procedures and, as appropriate, promote a system of energy development incentives to enable and encourage electric power industry participants to provide adequate capacity to meet demand including among others reserve requirements."*

Mandating CSP for bilateral contracts, especially base-load power supply" will enable the DOE to promote a critical incentive to energy development by

providing "access to the generation market" 75% of which is closed due to the control of the Metro Pacific and Aboitiz groups.

- e(iii) *"promote a system of incentives to encourage industry participants, including new generating companies and end-users to provide adequate and reliable electric supply". A Mandatory CSP will encourage the entry of new generating companies and create more supply to assure adequate and reliable electric supply.*

3. Mandates of the Energy Regulatory Commission under the RA 9136, EPIRA Law of 2001

The Draft needs to more completely state the mandates of the ERC as to its obligation to the consumers under the EPIRA Law.

- 1) *Section 41 Promotion of Consumer Interest – The ERC shall handle consumer complaints and ensure the adequate promotion of consumer interest.*
A Mandatory CSP will promote consumer interest
- 2) *Section 43 of the EPIRA mandates that the "ERC shall promote competition, encourage market development, ensure customer choice, and penalize abuse of market power...."*

Sub-section "t" of Section 43 is a generic mandate and we suggest that the following mandates of the ERC be cited in the Implementing Rules

"(o) Monitor the activities in the generation and supply of the electric power industry with the end in view of promoting free market competition and ensuring that the allocation or pass through of bulk purchase cost by distributors is transparent, non-discriminatory and that any existing subsidies shall be divided pro-rata among all retail suppliers; "

There is preponderant evidence that the prices of generation supply that are passed on to captive consumers from sweetheart negotiated contracts are neither fair and reasonable nor least cost and negotiation hinders free market competition.

"(k) Monitor and take measures in accordance with this Act to penalize abuse of market power, cartelization, and anti-competitive or discriminatory behavior by any electric power industry participant; "

Negotiation of Bilateral contracts by a DU with its sister company generator is cartelization and abuse of market power and anti-competitive behaviour by the DU as an electric power industry participant.

3) Section 45 *The ERC shall, within one (1) year from the effectivity of this Act., promulgate rules and regulations to ensure and promote competition, encourage market development and customer choice and discourage/penalize abuse of market power, cartelization and any anti-competitive or discriminatory behavior, in order to further the intent of this Act and protect the public interest. Such rules and regulations shall define the following:*

(a) the relevant markets for purposes of establishing abuse or misuse of monopoly or market position;

Mandating CSP to prevent misuse of monopoly or market position by the DU is a long overdue action by the ERC.

4. Mandatory or Voluntary CSP?

There is preponderant empirical data that negotiated power supply contracts with affiliated generators have higher pass-on generation rates than those from non-affiliated companies.

From Meralco's record of purchases of power in 2013, 2014, and 2015, MSK had discovered that the higher prices amounted to billions per year. In 2013, the difference in the generation rates of affiliated vs non-affiliated amounted to P5.5 billion. In 2014 it went up to P10 billion, and so far in 2015 for the nine (9) months from January to September 2015, it is P4.8 billion. These only show the sweetheart price premiums paid to affiliated generators and still do not factor in the benefits of true competition.

A voluntary CSP would make the DOE Circular only a pretension and would be a betrayal of the captive electric consumers.

A voluntary CSP does not improve on the current system and would only mislead the electric consumers into thinking that there is a DOE Circular that will protect their interest when it would actually be an effete and useless regulation.

The electric consumers have had enough of the hoodwinking by Meralco. We ask that in the least the DOE and ERC do not

become part of yet another hoodwinking if the CSP is made voluntary!

5. Far Reaching Benefits of the CSP

The benefits of a mandatory CSP for the people and country is far reaching.

- a) In addition to lower generation rates as opposed to negotiated sister company rates, mandatory CSP will open the generation market, 75% of which is controlled by the Metro Pacific and Aboitiz groups.
- b) Hence opened and levelled playing field, there will be more new investors of truly independent power generators which in the long run will assure the needed sustainable investments for additions to the country power supply.

Contrary to claims by groups claiming to represent consumer interests and with evident media connections, there is enough current players in the generation sector, local and foreign, to assure a competitive bidding. Once we open the generation market and create a level playing field, there will be more bidders.

- c) New and truly independent generators participating in a healthy competitive level market will encourage the influx of more efficient and environmentally compatible power generation technologies.
- d) Mandatory CSP will provide the DOE its long missing implementing power to influence the energy mix, locational, and environmental strategy for the country. Currently, the dominant DU's Meralco and Aboitiz groups determine the doable and convenient and most profitable power generation projects.
- e) A better coordinated locational strategy for power generation facilities can optimize the building of essential grid transmission facilities and eliminate unnecessary power lines whose cost are passed on to the electric consumers.
- f) Reduction of generation rates will not only come from true competition but from the elimination of the not commonly known "rent seeking" of DU's and its sister company from their partners in the generation projects. A Power Supply contract is a critical element of a power generation project. The party providing the guaranteed market for the project normally would get a compensation for that in terms of "carried interest" which is free equity. Since the sister company DU controls

the market, the sister generator gets this carried interest. The cost of the free equity is passed on to the electric consumers.

In one big coal project, the proponent IPP offered a price of P4.00 per kwh and even indicated willingness to go down to P3.80 per kwh. The price negotiated was eventually P4.30 per kwh with the sister company generator getting 51% of the common shares, which includes a portion of free equity or carried interest.

Consequently, the consumers will be paying P4.30 per kwh instead of P3.80 per kwh if it were an arms-length negotiation by a public service oriented DU, a difference of P0.50 per kwh. That's approximately P1.5 billion a year more of pass on charges to the consumers.

6. Suggestions on the Mechanics and Process

a. What will be Bid?

- 1) We propose that at least 90% of the base-load and reserve and peaking power requirements of the DU should be subjected to the CSP process.
- 2) DU's should be required to submit 120 days before the start of each planning year a 5-year forecast of their power supply needs, their current contracted capacities, and the uncontracted portion, and the capacity to be subjected to CSP.
- 3) Aggregation
We believe that aggregation to gain market leverage should be encouraged. However it should not be made mandatory as the current Draft apparently is seeking. Aggregation should be a result of the appreciation of the DU that it is to the benefit of their consumers and not due to forced requirement of law. Power supply contracts of 75mw and higher is sufficient volume to attract bidders.

b. Definition of CSP?

- 1) CSP would be a process of securing power supply through competitive selection. (yes!) The process should start with a formal competitive bidding for base-load requirements. Failing in that, it would shift to more informal "RFP" process of Request for Proposals from known viable sources. Failing in that, they can negotiate with the most responsive source.
- 2) Power Requirements for peaking, reserve, and ancillary can be through RFP.
- 3) The implementing rules should limit the use of "unsolicited proposals" and "swiss challenge" as a bonafide CSP method only to pioneering technologies not yet proven in the Philippines and reviewed and certified to be so by the CSP Committee. Otherwise this will be a loophole that the DU's will shift to. Swiss challenge on standard technologies is a pseudo CSP designed only to award to an anointed and preferred supplier.

c. Assuring Transparency and Fair bidding and Evaluation

The role of an independent Third Party is to assure properly determined capacity additions, balanced contract terms that protect both supplier and the consumer, and to transparently administer the bidding, evaluation, and award process.

- 1) A multi-sectoral CSP committee shall manage the competitive selection process. We propose the following composition as a concept:
 - (a) Chairman and Technical Working Group – by an Independent Third Party with knowledge of power planning, power supply contracts, and bidding procedures.
 - (b) Capacity Committee: Members: Representatives each from DOE, ERC, DU, PCCI, PIPPA, and Consumer Sector. This is the committee that will evaluate the proposed needs of the DU and whether the supply capacity proposed to be bid is reasonable and will address the needs of the electric consumers. They will also confirm if the process shall be Formal Bidding or RFP.
 - (c) Bid and Awards Committee:
Chaired by the Independent Third Party
Members: DOE, ERC, DU, NEDA
Observers for Transparency: PCCI, PIPPA, and Consumer Groups Rep
 - (d) Bid Evaluation
Chaired by the Independent Third Party and will consist of chosen engineers on the technical side and a finance evaluation team consisting of the representatives from DOF, DOE, ERC, NEDA, An Independent Auditing Firm not associated with any of the bidders, and Third Party Evaluation experts.
- 2) Standard Terms of CSP and Bilateral Contract

The CSP process should also assure fair and reasonable contract terms and avoid the sweetheart provisions in negotiated contracts. Each bid shall be fine tuned to be responsive to the unique requirements of the DU, its energy mix, and its area of service. The CSP Committee headed by the Independent Third Party shall prescribe standard mandatory contract terms to protect the public and assure fair and reasonable pricing for the long term.

This should cover:

 - (a) Reasonable downtime allowances for the supplier and replacement power in case of excessive downtime.
 - (b) Transparent and verifiable fuel pricing, indexing, and pass on formula
 - (c) Replacement Power in case of delay for any reason. Since Power supply is an essential commodity the availability of which should be assured by the contracting party.
 - (d) Validation of available capacity

- (e) There should be specific prohibition for the DU from communicating directly or indirectly with potential and participating bidders and provision for stiff penalties for interfering, or attempting to, with a truly competitive bidding process. The penalty should include cancellation of their DU public service franchise.
- (f) Other terms to assure a level playing field and transparent pass on charging to consumers.

3) Participation of Sister Generators in the CSP

DU's must be required to have separate organizations and manpower for the distribution and planning and the sister generator which shall be a separate corporate entity.

Before a Sister generator can participate in the CSP, it must seek the validation and confirmation by the DOE that even if it wins in the bidding, it will still not exceed the 50% limit on capacity and energy that it can contract with an affiliated DU and other market concentration limits set by the EPIRA Law and ERC.

Further, Current bilateral contracts and new contracts that will be won by the affiliated generator for its sister DU's shall be subject to independent monitoring with participation of bonafide consumer groups and accredited independent auditors.

(Related to this, we ask the DOE to repeal and amend the anomalous and illegal Rule 11 of its Implementing Rules and Regulations of RA 9136 which provided the current loophole to circumvent the 50% limit under Section 45 of the Epira Law and for the monopolization of the power generation sector by generation companies majority owned by the DU controlling stockholders.)

d. Cost of CSP and Compensation of the Independent Third Party

To protect the consumers, the total cost of the CSP shall not exceed the equivalent of P0.01 per kwh which is to be paid by the winning bidder as "transaction fee".

Considering that the price differential between a negotiated sweetheart contract of Meralco with a non-affiliated and affiliated company ranged from P0.38 to PP1.05 per kwh, a P0.01 per kwh additional cost is a very affordable trade-off and this is the kind of charge that the consumers will be happy to pay for.

e. Section 9 Repealing Clause

We wish to reiterate our request for clarification on the exact meaning and scope of this provision. We are concerned about the vagueness of the wordings specially the reference to “existing mechanisms”. What does “responsibilities already allocated and provided for under existing law, rule, or contract” mean?

A mandatory CSP will serve the public interest and country. We ask the DOE and ERC officials and the powers that be in Malacanang not to be spooked and tempted by the enticing influence of the vested interests and their media campaign. Electric Consumers have been neglected and made to suffer the high negotiated rates. *Ituwid natin ang Pagsingil sa Kuryente*. We ask President Pnoy to make this one of his lasting legacy.

Respectfully submitted,

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