



18 March 2021

HON. ALEXIS M. LUMBATAN
Commissioner
ENERGY REGULATORY COMMISSION
Pacific Center Building, San Miguel Avenue
Ortigas Center, Pasig City 1600

Attention: **Atty. Gregorio L Ofalsa**
Officer-in-Charge, Consumer Affairs Service

Subject: **Letter Consumer Complaints dated 17 July 2020, 07 October 2020, and 26 November 2020**

Dear Commissioner Lumbatan:

This is in connection with Letter Consumer-Complaints dated 17 July 2020, 07 October 2020, and 26 November 2020 (collectively, the "Letter Consumer-Complaints"), filed by Matuwid na Singil na Kuryente Consumer Alliance, Inc. (MSK), requesting an investigation on the alleged onerous contract between Quezon Power Phil. Ltd. Co. (QPPL) and Manila Electric Company (MERALCO), and further charging MERALCO among others, of increasing the generation rate, and over-recovery of Twenty Nine Billion Pesos (Php 29,000,000,000.00) in distribution charges from 2013 to 2018.

On 16 February 2021, MERALCO received an electronic copy of the Letter dated 15 February 2021 issued by this Honorable Commission, directing MERALCO to respond to the said Letter Consumer-Complaints. Upon verification with this Honorable Commission's Consumer Affairs Service Division, we confirmed that the Letter Consumer-Complaints have not yet been formally docketed, and had only been set for an informal hearing.

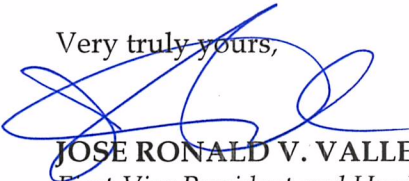
Nonetheless, we have noted the allegations in the Letter Consumer-Complaints, and respectfully manifest that there is no truth to the claim that MERALCO has been manipulating the cost of power sourced from QPPL. At any rate, we have already responded on a similar inquiry by the Honorable Commission on the same matter. If the Honorable Commission may recall, it previously required MERALCO to submit an explanation addressing the increase in generation rate involving QPPL. For easier reference, a copy of the Letter dated 22 December 2020, in compliance with such directive is attached hereto as Annex "A".

On the issue on the alleged over-recovery of Twenty Nine Billion Pesos (Php 29,000,000,000.00) in distribution charges from 2013 to 2018, MERALCO respectfully denies this baseless claim,

given that MERALCO has been applying the distribution rates approved by this Honorable Commission. Moreover, issues regarding the over/under recovery of MERALCO's distribution rates are currently pending resolution with this Honorable Commission. With respect to the other imputations, we are constrained to categorically deny the same given the patent absence of a cause of action and lack of evidentiary support to MSK's claims.

We hope that our letter response to this Honorable Commission dated 22 December 2020 sufficiently addresses the concerns and issues on the matter. Thank you very much.

Very truly yours,



JOSE RONALD V. VALLES
*First Vice President and Head,
Regulatory Management Office*

Copy furnished:

MATUWID NA SINGIL NA KURYENTE CONSUMER ALLIANCE, INC.
(MSK)
Suite 910, West Tektite Tower
Exchange Road, Ortigas Center
Pasig City



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22 December 2020

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/sf

Hon. AGNES VST DEVANADERA
Chairperson and CEO
Energy Regulatory Commission
 Pacific Center Building, San Miguel Avenue
 Pasig City

Dear Chairperson Devanadera:

We write in connection with your letter dated 10 December 2020, which we received on 15 December 2020, directing MERALCO to submit an explanation on the observation of the Commission on Quezon Power Philippines Ltd.'s (QPPL) generation rate in relation to the least cost principle required by the EPIRA.

We respectfully submit our compliance and explanation as follows:

1) *Lower dispatch in February and March 2020 supply months was due to Plant outage*

MERALCO would like to note that its energy utilization from QPPL decreased in the months of February and March 2020 due to shutdown of QPPL's power plant. For February 2020 supply month, its power plant was on planned maintenance outage from 17 January until 20 February 2020; while for March 2020 supply month, there were several forced outages due to plant tripping from 28 February until 1 March 2020 and from 2 March until 4 March 2020. The planned maintenance outage in February 2020 supply month was included in NGCP's Grid Operating and Maintenance Program (GOMP).

2) *QPPL rates are in accordance with previously approved formulae in the Power Purchase Agreement (PPA) approved by the regulator*

MERALCO's PPA with QPPL is duly approved by the Energy Regulatory Board (ERB) in a Decision dated 6 July 1995. As such, the terms and conditions of QPPL's electricity supply to MERALCO and rates thereunder are duly approved by the ERB. Notably, the PPA was executed and approved prior to EPIRA, and at a time when the introduction of a wholesale electricity spot market (WESM) was not yet envisioned. Since the PPA has been implemented for at least twenty years, foreign exchange (ForEx) and indices applied to rates thereunder have expectedly increased. Nonetheless, the calculation of payments in the PPA, as consistently implemented by the Parties, was recognized and approved by the ERB. In addition, the generation costs resulting from such calculation of payments have been consistently confirmed by the Commission in resolved/decided confirmation filing cases of MERALCO (as required under ERC Resolution #16, S. of 2009) up to year 2016.¹

¹ MERALCO's confirmation filing for years 2017 to 2019 was filed this year.

- 3) *In keeping with its least cost mandate, MERALCO employs bid variable strategy for QPPL*

Section 23 of EPIRA mandates DUs to supply electricity to their captive market in the least cost manner, "subject to the collection of retail rate duly approved by the ERC".

As to compliance with the least cost mandate upon DUs, this should be considered vis-à-vis the introduction of WESM under EPIRA. WESM is a gross pool market, where even energy quantities subject of bilateral contracts between generation company (GenCo) and DU (i.e., bilateral contract quantities or BCQs) are traded, although prices for such energy are settled outside WESM (i.e., in accordance with prices approved by the regulator for a specific contract). The WESM uses price and volume bids provided by GenCo participants in determining real-time dispatch of all power plants to meet the demand in the grid, and only plants that have price bids lower than the WESM's clearing price can be dispatched at a particular trading interval. In order to ensure least cost power supply mix under the WESM environment, MERALCO uses the variable costs of the contracted power plants as basis for nominations to the WESM (i.e., bid variable strategy) since the fixed charges can be considered as sunk costs in the optimization. Note that the fuel costs are the main component of the variable costs of power plants contracted by MERALCO. This way, if a power plant is not dispatched based on nomination pegged at its variable costs, then it means that buying electricity from WESM is more cost efficient than buying the same from such GenCo at contract price.

As to the corresponding rates to be collected by MERALCO, it is reiterated that the rates under the PPA had previously been approved with finality by the regulator. The ERB in its Decision dated 6 July 1995 recognized that under the PPA, QPPL "shall procure coal and supplemental fuel in order to operate the Plant in accordance with the terms set forth in the contract".

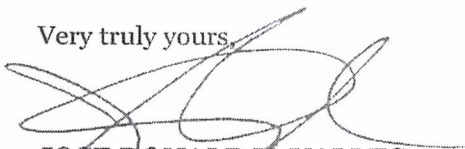
Specifically, the fuel supply contracts of QPPL were procured following Section 12.4 of the PPA. QPPL entered into long-term contracts for coal to ensure adequacy and stability of fuel supply. Although many GenCos in the country index coal to globalCoal Newcastle (NEWC), the QPPL fuel contracts are annually set and indexed to Indonesia's Harga Batubara Acuan (HBA) reference price and Japan Power Utility (JPU) Reference Price. Nevertheless, these are similarly acceptable indices globally. Notably though, since NEWC went down from July to Dec 2020, this has had the effect of bringing down fuel costs for MERALCO's other coal-fired GenCo power plants while QPPL maintained relatively stable coal prices.

- 4) *Unlike other pre-EPIRA supply contracts, the fuel take-or-pay provision in the QPPL PPA is not being implemented, to benefit customers*

Lastly, pre-EPIRA supply contracts typically have a fuel take-or-pay provision, which means that even if these power plants are not dispatched, the corresponding unused fuel will have to be paid for even if not actually used or consumed by customers. The QPPL PPA has this similar provision on fuel take-or-pay, yet parties have agreed that implementation shall only be on take-and-pay basis. This means that MERALCO only pays for fuel that is actually utilized by the QPPL power plant to generate and deliver electricity, which ultimately redounds to the benefit of the consumers and is consistent with the least cost mandate to DUs.

We hope and trust that the foregoing explanation is to the satisfaction of the Commission.

Very truly yours,

A handwritten signature in black ink, appearing to read 'Jose Ronald V. Valles', written over the typed name below.

JOSE RONALD V. VALLES
First Vice President and Head
Regulatory Management