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PIPPA 2014-004

February 20, 2014

HON. REYNALDO V. UMALI
Chairperson, Committee on Energy
House of Representatives
CTSS I, Committee Affairs Department
3rd Flr. RVM Building
House of Representatatives
Constitution Hills, Quezon City

Dear Congressman Umali:

This is in response to your letter dated January 29, 2014, requesting for comments for various House Bills. We have attached, as Annex A of this letter, a detailed matrix of our comments on the following House Bills:

1. **HOUSE BILL NO. 3633*("An Act Declaring Any Electric Power Generation Company as Public utility, Amending for the Purpose Section Six (6) of Republic Act No. 9136 Otherwise known as the "Electric Power Industry reform Act of 2001");***

2. **HOUSE BILL NO. 3676*("An Act Amending Republic Act No. 9136, otherwise known as "Electric Power Industry reform Act of 2001, and for Other Purposes").***

We would like to thank you for the opportunity to state our position, and we hope that the same receives your favorable attention.

Very truly yours,

LUIS MIGUEL O. ABOITIZ
President

cc: Hon. Carlos Jericho L. Petilla
Secretary, Department of Energy

Annex A- PIPPA COMMENTS TO HOUSE BILLS
February 20, 2014

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HOUSE BILL NO. 3633 ***("An Act Declaring Any Electric Power Generation Company as Public utility, Amending for the Purpose Section Six (6) of Republic Act No. 9136 Otherwise known as the "Electric Power Industry reform Act of 2001"")***	
"Section 6. Generation Sector- Generation of electric power, a business imbued with public interest, IS HEREBY DECLARED A PUBLIC UTILITY. Upon the effectivity of this Act, before the commencement of operations, any new generation company shall secure: 1.) From THE CONGRESS OF THE PHILIPPINES A NATIONAL FRANCHISE, 2.) From the Energy Regulatory Commission (ERC) a certificate of compliance pursuant to the standards set forth in this Act, 3.) Health, safety and environmental clearances from the appropriate government agencies AND LOCAL GOVERNMENT UNITS under existing laws. ALL EXISTING POWER GENERATION COMPANIES ARE HEREBY ORDERED TO SECURE A NATIONAL FRANCHISE FROM THE CONGRESS OF THE PHILIPPINES." "Upon implementation of retail competition and open access, the prices charged by a generation company for the supply of electricity MUST NOT EXCEED THE TWELVE (12) PERCENT RETURN ON RATE	In the current Section 6 of the EPIRA states that: "SEC. 6. Generation Sector. – Generation of electric power, a business affected with public interest, shall be competitive and open. Upon the effectivity of this Act, any new generation company shall, before it operates, secure from the Energy Regulatory Commission (ERC) a certificate of compliance pursuant to the standards set forth in this Act, as well as health, safety and environmental clearances from the appropriate government agencies under existing laws…." Section 6 clearly provides that the generation sector is not an ordinary business, as it is a business affected with public interest. Thus, a generation company has to secure from the Energy Regulatory Commission (ERC) a certificate of compliance (COC), as well as other requirements. In securing a COC, a generation company shall comply with ERC rules and regulation necessary for the generation sector. Thus, the generation sector, although without a national franchise, is already subject to special regulations. On the other hand, according to the Supreme Court in National Power

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BASE (RORB) UNDER THE PUBLIC UTILITY LAW AND shall [not] be subject to regulation by the ERC [except as otherwise provided in this Act]. Pursuant to the objective of lowering electricity rates to end-users, sales of generated power by generation companies shall be value added tax zero-rated. The ERC shall [,in determining the existence of market power abuse or anti-competitive behavior,] require from generation companies the ANNUAL submission of [their] INDEPENDENTLY AUDITED financial statements."	Corporation vs. Court of Appeals, (G.R. No. 112702. September 26, 1997), a public utility should be for public use and public service: "A 'public utility' is a business or service engaged in regularly supplying the public with some commodity or service of public consequence such as electricity, gas, water, transportation, telephone or telegraph service. **The term implies <u>public use</u> and <u>service</u>.** [Emphasis supplied]" The same definition was reiterated in *Metropolitan Cebu Water District vs. Adala* (G.R. No. 168914, July 4, 2007). More specifically, in *Iloilo Ice and Storage Company vs. Public Utility Board* (G.R. No. L-19857, March 2, 1923), the Supreme Court stated that the criterion in determining a public service is whether its use is open to the indefinite public or if it is organized solely for particular persons under strictly private contracts: "Planting ourselves of the authorities, which discuss the subject of public use, **the criterion by which to judge of the character of the use is whether the public may enjoy it by right or only by permission.** (U. S. *vs.* Tan Piaco, *supra*.) **The essential feature of a public use is that it is not confined to privileged individuals, but is open to the indefinite public**. (Thayler and Thayler *vs.* California Development Company, *supra*.) The use is public if all persons have the right to the use under the same circumstances. (Fall brook Irrigation District *vs.* Bradley, *supra*.) If the company did in truth sell ice to all persons seeking its service, it would be a public utility. **But if on the other hand, it was organized solely for particular persons**

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	under strictly private contracts, and never was devoted by its owners to public use, it could not be held to be a public utility without violating the due process of law clause of the Constitution. (Producers Transportation Co. *vs.* Railroad Commission, *supra*.) And the apparent and continued purpose of the Iloilo Ice and Storage Company has been, and is, to remain a private enterprise and to avoid submitting to the Public Utility law." In *Bagatsing vs. Committee on Privatization* (G.R. No. 112399, July 14, 1995), the Court emphasized that a public utility must be one for public service which the public has the right to demand: Implementing Section 8 of Article XIV of the 1935 Constitution, the progenitor of Section 5 of Article XIV of the 1973 Constitution, is Section 13(b) of the Public Service Act, which provides: The term "public service" includes every person that now or hereafter may own, operate, manage, or control in the Philippines, for hire or compensation, with general or limited clientele, whether permanent, occasional, or accidental and done for general business purposes, any common carrier, railroad, street railway, . . . and other similar public services: . . . . xxx xxx xxx A "public utility" under the Constitution and the Public Service Law is **<u>one organized "for hire or compensation" to</u>**

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	serve the public, which is given the right to demand its service. PETRON is not engaged in oil refining for hire and compensation to process the oil of other parties. For electricity, transmission and distribution sector are considered public utilities since they are natural monopolies. Distribution utilities deal with the public directly. Moreover, they have captive customers, which include the household sector. By captive, it means that the customers cannot choose any other distribution utility. Thus, the transmission and distribution utilities have their rates reviewed and approved by the ERC. These rates also produce guaranteed profits. Even though the EPIRA acknowledges that the generation sector is affected with public interest, it is worth noting that the generation sector does not serve the public directly. Generators only deal with the transmission, distribution and supply sectors. They do not sell their power supply to the indefinite public. Rather, they do so under private contracts. Based on the above decisions of the Supreme Court, generators are not public utilities which require the issuance of a franchise. This is only logical, considering that generators do not supply the general public. The customers of generators are free to decide whether or not to purchase supply from any generator. Moreover, the profits of a generation company are not guaranteed. Investments in the generation sector depend on economic principle of price signals under a competitive environment. The major difference of the current methodology as per EPIRA and the proposed House Bill is that investment in generator will require a franchise from Congress. This will make investment in generation harder. It will be an additional barrier to the entry of new players, which will result to even more

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	supply deficit and higher prices. Thus, what will be the additional benefit to the public if generators will be required to have a national franchise? In addition, the proposed amendment should consider the reality that, in the Luzon Grid alone, supply deficiency had been projected if committed power projects would not be on-line as scheduled in 2015. Building of new plants already triggers enormous permitting requirements, not to mention involved government bureaucratic processes. Requiring a national franchise will be an additional requirement which may cause delays. Classifying power generation as a public utility will also subject the activity to nationality restrictions and may lead to divestment of already invested foreign funds, if they are in excess of 40% capital. This may not only dampen the atmosphere for needed investments, but also invite violation of Philippine treaty obligations that facilitate flow of foreign investments. It may be noted that EPIRA was passed with the intent of allowing entry of new players – including foreign players – in the generation sector as NPC was to be privatized. The policy to make power generation a competitive sector was a product of numerous debates and studies. EPIRA was lengthily discussed for about three congressional terms. As such, the sound policy should not be changed as a knee-jerk reaction to recent issues involving Meralco's power rate increase which is an entirely different concern. Considering time and capital needed to put up, operate and maintain a power generating plant, the focus must be on how to timely attract, secure and protect needed investments in the generation sector. With the growing demand for electricity, a competitive generation sector may yield long-term benefits that will redound to the welfare of consumers.

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Sec. 2. Transitory Provision. – All existing electric power generation companies are given one (1) year to secure a national franchise from the Congress of the Philippines after the effectivity of this Act.	What will happen if existing generation companies would not be able to get a national franchise? This provision may be unreasonable considering that power generation companies will merely follow the processes and priorities of Congress and the Executive. Even if a bill is filed within the one (1) year period, there is no assurance that the bill will become a law within the same period.
<u>HOUSE BILL NO. 3676</u> ***("An Act Amending Republic Act No. 9136, otherwise known as "Electric Power Industry reform Act of 2001", and for Other Purposes)***	
SECTION 1. Section 45 of the Republic Act No. 9136 is hereby amended to read as follows: "Sec. 45. Cross Ownership, Market Power Abuse and Anti-Competitive Behavior – No participant in the electricity industry or any other person may engage in any anti-competitive behavior including, but not limited to, cross-subsidization, price or market manipulation, or other unfair trade practices detrimental to the encouragement and protection of contestable market. NO DISTRIBUTION UTILITY, OR ITS RESPECTIVE SUBSIDIARY OR AFFILIATE OR STOCKHOLDERS OR OFFICIAL OR DIRECTOR OR ANY OF THEIR RELATIVES WITHIN THE FOURTH CIVIL DEGREE OF CONSANGUINITY OR AFFINITY, SHALL BE ALLOWED TO HOLD ANY INTEREST, DIRECTLY OR INDIRECTLY, IN ANY GENERATION COMPANY. LIKEWISE, NO GENERATION COMPANY, OR ITS RESPECTIVE SUBSIDIARY OR AFFILIATE OR STOCKHOLDERS OR OFFICIAL OR DIRECTOR OR ANY OF THEIR RELATIVES WITHIN THE FOURTH CIVIL DEGREE OF CONSINGUINITY OR AFFINITY,	Section 31 of the EPIRA states that: "Upon the initial implementation of open access, the ERC shall allow all electricity end-users with a monthly average peak demand of at least **one megawatt (1MW)** for the preceding twelve (12) months to be the **contestable market**. Two (2) years thereafter, the threshold level for the contestable market shall be reduced to **seven hundred fifty kilowatts (750kW).** At this level, aggregators shall be allowed to supply electricity to end-users whose aggregate demand within a contiguous area is at least seven hundred fifty kilowatts (750kW). Subsequently and every year thereafter, the ERC shall evaluate the performance of the market. On the basis of such evaluation, it shall gradually reduce threshold level **until it reaches the household demand level**. In the case of electric cooperatives, retail competition and open access shall be implemented not earlier than five (5) years upon the effectivity of this Act." [Emphasis supplied]

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SHALL BE ALLOWED TO HOLD ANY INTEREST, DIRECTLY OF INDIRECTLY, IN ANY DISTRIBUTION COMPANY: PROVIDED, THAT THE DISTRIBUTION UTILITY, ITS RESPECTIVE SUBSIDIARY OR AFFILIATE OR STOCKHOLDER OR OFFICIAL OF A DISTRIBUTION UTILITY HOLDING AN INTEREST IN ANY GENERATION COMPANY, AND VICE VERSA, AT THE TIME OF THE PASSAGE OF THIS ACT, SHALL BE REQUIRED TO DIVEST THE SAME WITHIN ONE (1) YEAR FROM THE EFFECTVITY OF THIS ACT. No generation company or distribution utility, or its respective subsidiary or affiliate or stockholder or official of a generation company or distribution utility, or other entity engaged in generating and supplying electricity specified by ERC shall be allowed to hold any interest, direct or indirect, in TRANSCO or its concessionaire. Likewise, the TRANSCO, or its concessionaire or any of its stockholders or officials or any of their relatives within the fourth civil degree of consanguinity or affinity, shall not hold any interest, whether direct or indirect, in any generation company or distribution utility. Except for government-appointed representatives, no person who is an officer or director of TRANSCO or its concessionaire shall be an officer or director of any generation company, distribution utility or supplier. A GENERATION COMPANY MAY BE PERMITTED TO HOLD INTEREST, DIRECTLY OF INDIRECTLY, IN ANOTHER GENERATION COMPANY; PROVIDED, THAT THE EXTENT OF SUCH INTREST SHALL BE LESS THAN THE AMOUNT OF SHARES NEEDED TO VOTE ONE MEMBER OF THE BOARD OF DIRECTORS.	The EPIRA envisions an Open Access sector down to the household level. The Open Access will enable the contestable customers to choose their supplier. The distribution and transmission services will still be provided by the utility in a specific franchise area. However the generation or supply side will be competitive. The current status of Open Access is that contestable customers are customers with demand of one (1) MW monthly average peak demand. In June 2015, the level is expected to go down to 0.75MW. Open Access shall continue up to the household level, as may be determined by ERC. The EPIRA allowed the cross-ownership for generation and distribution, with a limit of up to 50% contracting because there will be Open Access. There will come a time that the distributor will not have any captive customers for passing on its generation charges. If passing-on the generation costs of distributors to their captive customers is the issue, then the easier and quicker way to solving it is bringing down the level or threshold to be considered contestable customers. The second and succeeding phases of Open Access should be implemented as scheduled or even accelerated. From the point of view of preventing accumulation of market power, EPIRA already imposes very high market share restrictions, such as prohibiting ownership or control of more than 30% of the installed generating capacity of a grid and/or 25% of the national generating capacity, and limiting to 50% of total demand the capacity that may be sourced from a bilateral contract with an affiliated company. Imposing cross-ownership restrictions may not be the right solution as this may delay or discourage needed investments in the power sector. Also, limiting

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	allowable investments of a generation company in another (generation company) only restricts needed capital-flow in a very capital intensive industry. As such, it may even end up being a barrier to entry of new players, instead of fostering competition. The existing safeguards in the EPIRA are sufficient and sound policies, which must not be disturbed overnight without much thought and deliberation. Impact on the entire power industry must also be carefully considered, as well as any effect on the power supply needs of the country and the welfare of consumers. It may be recalled that, while EPIRA was being deliberated in the House of Representatives, it was discussed that some countries do not even have cross-ownership restrictions. Lastly, the proposed cross-ownership restrictions and divestment of interest may be constitutionally challenged as it amounts to arbitrary taking of private property or impairment of obligations.