

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

IN THE MATTER OF THE 12<sup>th</sup>  
APPLICATION FOR THE RECOVERY OF  
INCREMENTAL FUEL AND  
INDEPENDENT POWER PRODUCER  
(IPP) COSTS UNDER THE GENERATION  
RATE ADJUSTMENT MECHANISM  
(GRAM), WITH PRAYER FOR  
PROVISIONAL AUTHORITY

|                               |          |
|-------------------------------|----------|
| PSALM CORP.                   |          |
| OFFICE OF THE GENERAL COUNSEL |          |
| RECEIVED                      |          |
| BY:                           | R. ANDAM |
| DATE:                         | 1/14/09  |
| TIME:                         | 4:00 PM  |
| CONTROL NO.                   | 09-0014  |

ERC CASE NO. 2008-063 RC

NATIONAL POWER CORPORATION  
(NPC) AND POWER SECTOR ASSETS  
AND LIABILITIES MANAGEMENT  
CORPORATION (PSALM),

Applicants.

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**NOTICE OF PUBLIC HEARING**

DOCKETED  
Date: JAN 12 2009  
By: *WV*

**TO ALL INTERESTED PARTIES:**

Notice is hereby given that on December 16, 2008, the National Power Corporation (NPC) and Power Sector Assets and Liabilities Management Corporation (PSALM) filed with the Commission, pursuant to the provisions of Republic Act No. 9136, an application for the recovery of incremental fuel and Independent Power Producer (IPP) costs under the 12<sup>th</sup> Generation Rate Adjustment Mechanism (GRAM), with prayer for provisional authority.

In the said application, NPC and PSALM alleged, among others, the following:

1. NPC is mandated under its Charter to undertake the development of hydroelectric power generation and the production of electricity from nuclear, geothermal and other sources of energy in order to attain, among others, the objective of providing an adequate supply of electric power nationwide at a reasonable price;

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2. NPC is filing the instant application in its capacity as the owner of record of all existing generation assets and energy, and also as implementing agency for the unbundled generation rates as stated in the several Orders issued by the Commission. On the other hand, PSALM is filing the application in its capacity as transferee, owner and administrator of the generating assets of NPC pursuant to Section 49 of Republic Act No. 9136 (R.A. 9136);
3. The recovery of deferred charges were all consistent with the Order dated February 24, 2003 in ERC Case No. 2003-44 providing, among others, the required mechanism for the recovery of the deferred fuel and Independent Power Producer (IPP) costs;
4. The instant application covers the test/billing period from July 2008 to September 2008. NPC has fully complied with all the Commission's monthly reportorial requirements in support of the calculated allowable costs covering the said test period;
5. They propose to recover/(refund) as Deferred Accounting Adjustment (DAA), the difference between the allowable fuel and purchased power costs and the amounts recovered through the basic generation rate during the above-stated test/billing period and the remaining balance of the approved amount of under/over recoveries resulting from the Commission's issuance of the April 13, 2005 Final Decision on the RORB-TOU Rate application under ERC Case No. 2004-178;
6. The instant application does not include any un-recovered or un-refunded balance of the deferred costs under the 10<sup>th</sup> and 11<sup>th</sup> GRAM applications considering the fact that the same is still pending resolution by the Commission since its filing last July 29, 2008 and September 25, 2008, respectively;
7. Consistent with the previous GRAM applications, the instant application likewise excludes the costs of purchased power from four (4) IPP contracts under Rehabilitation-Operation-Maintenance and Management (ROMM), Build-Rehabilitation-Operation and Transfer (BROT) and Build-Operate-Transfer (BOT) arrangements covering the Malaya, Naga (Salcon), Caliraya-Botocan-Kalayan (CBK) and Mindanao Coal (STEAG) power plants pending the Commission's approval on the recovery of the same through power rates;
8. Similar to the calculation of allowable fuel costs in the previous GRAM applications starting the 7<sup>th</sup> GRAM Application and pending the Commission's resolution on NPC's "Motion for Reconsideration" filed with the Commission for disallowing the assumptions made pursuant to the Commission's Order dated February 7, 2007 and Decision dated June 12, 2007, granting provisional approval and final approval, respectively of the 7<sup>th</sup> GRAM DAAs, they maintain the following assumptions and modification:
  - a. Adjustment of the existing ERC-adopted heat rate caps.

- a.1. In the determination of the allowable incremental fuel costs, a comparison is made between the actual average heat rates per fuel type during any given application test/billing period (July 2008 to September 2008 for the instant application) and the existing ERC-adopted heat rate caps per fuel type which were originally established and approved by the then Energy Regulatory Board (ERB) based on its actual results of operations in 1996 for Luzon grid and 1993 for Visayas and Mindanao grids. Recovery of incremental fuel costs is limited to the lower of the two (2) heat rate levels (actual versus cap) in order to protect NPC's customers from being burdened with unreasonable costs of fuel consumed. Although the intention of the Commission in applying the said methodology is clear and laudable, the same results to under-recovery of reasonable fuel costs given that the existing ERC-adopted heat rate caps are significantly incomparable with the actual average plant heat rates as of July 2008 to September 2008. The proposed adjustment of the heat rate caps includes the application of a reasonable heat rate degradation factor (based on actual test result from some of its contracted IPP plants as well as the heat rate degradation factor utilized in calculation of Long Run Avoidable Costs or LRAC in a number of Orders of the Commission in various rate cases) to bring the levels of the heat rate caps from 1996/1993 levels to 2007 levels. On the other hand, they considered an assumed system heat rate improvement resulting from a major plant maintenance which should be conducted at least every four (4) years. Although the heat rate degradation may actually vary on a per plant basis, the methodology employed (which is across all fuel and plant types within each grid) is but reasonable given that the existing ERC-adopted heat rate caps are likewise on a per-grid and per fuel type bases. The adoption of a heat rate degradation net of heat rate improvement is reasonable, and the same is further justified when the Commission recognized the need for the degradation of the Heat Rate caps when it issued its June 30, 2008 Decision on NPC's application for the adoption of System Heat Rate under ERC Case No. 2004-111. However, they are yet to adopt the new Heat Rate caps approved by the Commission in the said Decision when it files its succeeding GRAM applications as the test period for this instant application occurs prior to the effectivity of the said Decision. Although the test period for this 12<sup>th</sup> GRAM application is July 2008 to September 2008, the allowable incremental costs or savings that NPC is proposing to recover or refund for fuel and IPP costs are one-month and two-months' lag, respectively. Thus, the September 2008 effectivity of the new heat rate caps (succeeding month after receipt of the Decision) shall be applied in the succeeding GRAM applications for test periods starting October 2008.

- b. Calculation of the average heat rates per fuel type and per grid during May 2008 to June 2008 billing months.
- b.1. In the determination of the ERC-adopted heat rate caps, the then ERB included the volume of fuel reported as consumed but without any equivalent generation such as start-up fuel and heat run test fuel, among others. Thus, in the calculation of the average heat rates for each application's test period, the Commission and the applicants, continued the then ERB's calculation procedure for consistency purposes. Nonetheless, pending the Commission's resolution on the "Motion for Reconsideration" on the 7<sup>th</sup> GRAM DAA, they maintain their proposal in the instant application, with the assumption that the volume of fuel consumed without generation by plants that were commercially operated after the heat rate cap test year should be excluded considering that the inclusion of the same makes the comparison between the actual average heat rates and the heat rate caps irrelevant and unreasonable considering the numerous plants that operated after the heat rate cap test period. Nonetheless, the recovery of the corresponding fuel cost consumed by plants that were commercially operated after the heat rate cap test year should be separately determined from the cost of fuel consumed by plants that were already operational in Luzon during 1996 and in the Visayas and Mindanao grids during 1993. Further, the inclusion of the afore-stated fuel consumed distorts the resulting average heat rate during the pertinent test period of this instant application as fuel consumption without generation is not a measure of the plants' efficiency but rather an unavoidable fuel consumption necessary to put the plant in operation or ensure its operational safety.
9. Considering the foregoing and pursuant to all the relevant Decisions and Orders previously issued by the Commission, they calculated the total deferred costs for recovery under the instant application comprising of deferred fuel and IPP costs and the corresponding carrying charges for the Luzon, Visayas and Mindanao grids covering the test period from July 2008 to September 2008. The table below shows the summary of the total deferred fuel and IPP costs:

| GRID               | DAA, PhP             |
|--------------------|----------------------|
| LUZON              | 4,066,742,855        |
| VISAYAS            | 1,064,587,010        |
| MINDANAO           | 335,089,300          |
| <b>PHILIPPINES</b> | <b>5,466,419,165</b> |

10. Any balance that will be derived out of the implementation of the 10<sup>th</sup> and 11<sup>th</sup> GRAM DAAs should be added to the deferred costs that may be approved under the instant application. Adopting a spread in accordance with the test period, the proposed DAAs in the instant application in PhP/kWh shall be as follows:

Proposed DAA Charges, PhP/kWh

|              | <b>LUZON</b> | <b>VISAYAS</b> | <b>MINDANAO</b> |
|--------------|--------------|----------------|-----------------|
| <b>TOTAL</b> | 0.7456       | 0.8114         | 0.1590          |

The proposed DAA charges in PhP/kWh were derived using the projected energy sales under the proposed CY 2007-2010 budget.

11. As authorized under the Implementing Rules of the GRAM, they utilized the following carrying charge interest rates:

Allowable Carrying Charge Interest Rates

| Test/Billing Months | Prevailing 91-day T-Bill Rate | Authorized Allowance | Allowable Rate |
|---------------------|-------------------------------|----------------------|----------------|
| July 2008           | 2.6990%                       | 3%                   | 5.6990%        |
| August 2008         | 2.6990%                       | 3%                   | 5.6990%        |
| September 2008      | 2.6990%                       | 3%                   | 5.6990%        |

1. Source: Bangko Sentral ng Pilipinas
2. As authorized in the GRAM Implementing Rules
3. There was No Issue (NI) T-Bill Rate for the month of August 2008 and September 2008, hence, the rate was computed based on the average T-Bill Rates for the preceding of the said months.

12. The proposed GRAM DAA is fair and reasonable as it allows the recovery of deferred costs consistent with the principle of a free and competitive electricity market as provided under R.A. 9136;
13. They propose to recover/refund the above-stated deferred costs for test periods July 2008 to September 2008 only over the following recovery periods:

Proposed Spread (No. of Months)

| <b>Luzon</b> | <b>Visayas</b> | <b>Mindanao</b> |
|--------------|----------------|-----------------|
| 3            | 3              | 3               |

They emphasized that the total deferred accounting adjustments under the instant application represents the deferred fuel and IPP costs for the billing period July 2008 to September 2008 only. The balance resulting from the implementation of ERC Order dated November 24, 2008, where NPC was directed to continue collecting/(refunding) the amount previously authorized by the Commission under ERC Case Nos. 2008-031 RC and the balance from the implementation or non-implementation of GRAM applications (10<sup>th</sup> and 11<sup>th</sup>) to cover the test period from January 2007 to June 2008 pending with the Commission, is being proposed under the instant application to be spread over the remaining number of months when incremental costs or savings were deferred, to

reflect a reasonable monthly power rate. For clarity, assuming the 10<sup>th</sup> and 11<sup>th</sup> GRAM applications which covered a total of eighteen (18) months cost is only implemented for two (2) months then the balance of the 10<sup>th</sup> and 11<sup>th</sup> GRAM applications to be added in this application should be spread for sixteen (16) months.

Should there be a single ruling on the said applications, including the instant application, they proposed that the corresponding GRAM DAAs be broken down on a per rate case application basis; and

14. They pray that consistent with ERC Case No. 2003-44 adopting the Implementing Rules for the Recovery of Fuel and Independent Power Producer Costs: GRAM and the amended Section 4 (e) Rule 3 of the IRR of R.A. 9136 or EPIRA, the amounts of deferred costs and the proposed DAA charges of PhP0.7456/kWh for the Luzon Grid, PhP0.8114/kWh for the Visayas Grid and PhP0.1590/kWh for the Mindanao Grid be approved or provisionally approved and that corresponding balances from the previously approved GRAM applications including 10<sup>th</sup> and 11<sup>th</sup> GRAM which are currently pending resolution, be integrated on top of the said charges. They further pray for the approval of the proposed determination of the appropriate DAA charges for the balances as stated in this instant application including the breakdown of the GRAM DAAs on a per rate application basis, in the event that the Commission issues a consolidated resolution on the 10<sup>th</sup> and 11<sup>th</sup> GRAM applications.

The Commission has set the application for hearing on February 4, 2009 at ten o'clock in the morning (10:00 A.M.) at the ERC Hearing Room, 15<sup>th</sup> Floor, Pacific Center Building, San Miguel Avenue, Pasig City.

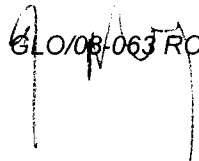
All persons who have an interest in the subject matter of the proceeding may become a party by filing, at least five (5) days prior to the initial hearing and subject to the requirements in the ERC's Rules of Practice and Procedure, a verified petition with the Commission giving the docket number and title of the proceeding and stating: (1) the petitioner's name and address; (2) the nature of petitioner's interest in the subject matter of the proceeding, and the way and manner in which such interest is affected by the issues involved in the proceeding; and (3) a statement of the relief desired.

All other persons who may want their views known to the Commission with respect to the subject matter of the proceeding may file their opposition to the application or comment thereon at any stage of the proceeding before the applicants conclude the presentation of their evidence. No particular form of opposition or comment is required, but the document, letter or writing should contain the name and address of such person and a concise statement of the opposition or comment and the grounds relied upon.

All such persons who may wish to have a copy of the application may request the applicants, prior to the date of the initial hearing, that they be furnished with a copy of the application. The applicants are hereby directed to furnish all those making such request with copies of the application and its attachments, subject to reimbursement of reasonable photocopying costs. Likewise, any such person may examine the application and other pertinent records filed with the Commission during the usual office hours.

**WITNESS**, the Honorable Chairperson, **ZENAIDA G. CRUZ-DUCUT**, and the Honorable Commissioners, **RAUF A. TAN**, **MARIA TERESA A.R. CASTAÑEDA** and **JOSE C. REYES**, Energy Regulatory Commission, this 7<sup>th</sup> day of January 2009 at Pasig City.

  
**ATTY. FRANCIS SATURNINO C. JUAN**  
Executive Director III

  
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