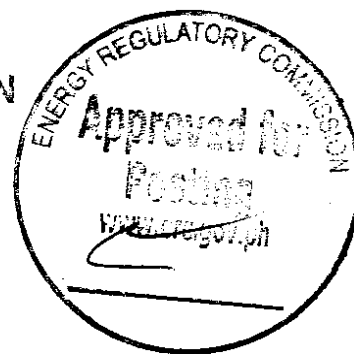


Republic of the Philippines
ENERGY REGULATORY COMMISSION
San Miguel Avenue, Pasig City



IN THE MATTER OF THE
APPLICATION FOR APPROVAL OF
THE AMENDED ELECTRICITY
PURCHASE AGREEMENT (AEPA)
ENTERED INTO BY AND BETWEEN
ANGELES ELECTRIC
CORPORATION (AEC) AND
ANGELES POWER, INC. (API), WITH
PRAYER FOR PROVISIONAL
AUTHORITY

ERC CASE NO. 2008-037 RC

ANGELES ELECTRIC
CORPORATION (AEC) and
ANGELES POWER,
INCORPORATED (API),

Applicants.

x-----x

D O C K E T E D
Date: MAR 30 2009
By: [Signature]

DECISION

On July 1, 2008, Angeles Electric Corporation (AEC) and Angeles Power Incorporated (API) filed a joint application for approval by the Commission of their Amended Electricity Purchase Agreement (AEPA) dated June 25, 2008, with prayer for provisional authority.

In the said joint application, AEC and API alleged the following:

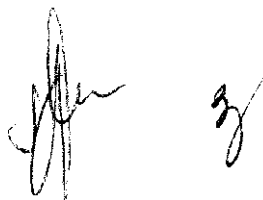

1. API is an Independent Power Producer (IPP) with a 30 MW Diesel Power Plant located at Angeles Park Special Economic Zone, Calibutbut, Bacolor, Pampanga;
2. AEC is the duly authorized operator of electric, light and power system in Angeles City;

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3. AEC sources forty percent (40%) of its power requirements from API and sixty percent (60%) from NPC;
4. From years 1993 to 2003, API sold electricity to AEC from its Calibu Power Plant pursuant to their Electricity Purchase Agreement (EPA), which was approved by then Energy Regulatory Board (ERB) per its Decision dated August 25, 1994 in ERB Case No. 93-109;
5. Said EPA was renewed under the same terms and conditions for another three (3) years, from January 1, 2004 to December 31, 2006;
6. On November 30, 2004, AEC and API entered into an Extended Electricity Purchase Agreement (EEPA) which extended the sale of electricity between AEC and API for another ten (10) years, from January 1, 2007 to December 31, 2016;
7. The EEPA was approved by the Commission in its Decision dated February 22, 2006 in ERC Case No. 2005-010RC, the dispositive portion of which reads:

*"WHEREFORE, premises considered, the application for the Renewal of the Electricity Purchase Agreement and Extension of the Electricity Purchase Agreement entered into by and between Angeles Electric Corporation and Angeles Power, Inc. is hereby **APPROVED** with modification to the effect that the Ceiling Rates provision of both contracts be limited to the Time-of-Use (TOU) rates imposed by the National Power Corporation (NPC) and the National Transmission Corporation (TRANSCO) wheeling rates. **HOWEVER, IN THE EVENT THAT THE NPC RATE IS NO LONGER APPLICABLE DUE TO THE ON-GOING PRIVATIZATION OF NPC AS WELL AS THE IMPENDING OPEN ACCESS AND WHOLESALE COMPETITION, AEC AND API MAY RENEGOTIATE THE PRICING SCHEME OF THIS CONTRACT TO REFLECT THE TRUE COST OF GENERATION SUBJECT TO THE APPROVAL OF THE COMMISSION.** The parties should take into consideration the dynamics of a competitive market place augured by the privatization of NPC's generating assets, the implementation of Open Access and Transmission Service (OATS), as well as the operation of the Wholesale Electricity Spot Market (WESM)."* (Emphasis supplied)

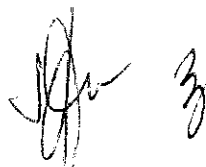
8. The rates of NPC are no longer reflective of the present true cost of generation;
9. The current scenario of high bunker fuel prices has fundamentally changed the viability of operating API's Calibutbut Power Plant under the current EPA, where the power rate charged by API is subject to a ceiling based on NPC + TRANSCO rate;



10. The current bunker prices are about three (3) times the base fuel cost when the EPA was drafted almost three (3) years ago;
11. The increase in bunker price is expected to continue and for API to continue its operation based on the ceiling price imposed under the Decision dated 22 February 2006 in ERC Case No. 2005-010RC would surely lead to a cessation of its operations and eventually affect the economic activities within AEC's franchise area;
12. Moreover, the present transmission line constraints in Angeles City prevent AEC from sourcing all its power requirements from NPC;
13. API's embedded generation capacity, on the other hand, is readily available, provides valuable ancillary service, and contributes to the reduction of system losses while increasing system stability;
14. Although the rates of API are not pegged on the NPC + TRANSCO rate, it is undeniable that NPC rates would eventually be increased due to the continued rise in the price of fuel/coal, and to reflect the declining efficiency and economy of its residual generation mix as it divests its remaining hydro, geothermal and coal plants;
15. Pursuant to the aforementioned Decision of the Commission allowing AEC and API to renegotiate the pricing scheme in their Agreement to reflect the true cost of generation, AEC and API renegotiate the EPA and execute, in its stead, an Amended Electricity Purchase Agreement (AEPA);
16. Under the AEPA, letters "b" (Ceiling), "c" (Floor), "d" (Time-of-Use), d.i and d.ii all of Section 3, Sub-section 3.01 of the EPA were deleted while a provision on the Assignability under a new section (14-A) was added; and
17. The other provisions of the EPA as approved by the Commission on February 22, 2006 in ERC Case No. 2005-010 RC remain unchanged and in full force and effect.

Having found said application to be sufficient in form and substance with the required fees having been paid, an Order and a Notice of Public Hearing, both dated July 14, 2008, were issued setting the same for initial and evidentiary hearing on August 8, 2008.

In the same Order, AEC and API were directed to cause the publication of the Notice of Public Hearing, at their own expense, twice (2x) for two (2) successive weeks in two (2) newspapers of general circulation in the Philippines, with the date of the last publication to be made not later than ten (10) days before



the scheduled date of the initial hearing. They were also directed to inform the consumers within AEC's franchise area, by any other means available and appropriate, of the filing of the instant application, the reasons therefor, and of the scheduled hearing thereon.

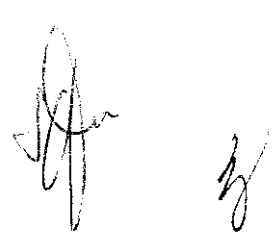
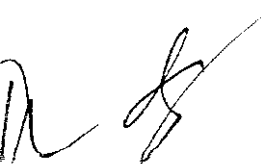
The Office of the Solicitor General (OSG), the Commission on Audit (COA) and the Committees on Energy of both Houses of Congress were furnished with copies of the Order and the attached Notice of Public Hearing and were requested to have their respective duly authorized representatives present at the aforesaid initial hearing.

Likewise, the Office of the Mayor of Angeles City was furnished with copies of the said Order and Notice of Public Hearing for the appropriate posting thereof on its bulletin board.

On July 31, 2008, AEC and API jointly filed their "Pre-Trial Brief".

During the August 8, 2008 initial hearing in Angeles City, Pampanga, AEC and API presented their proofs of compliance with the Commission's posting and publication of notice requirements as well as several witnesses who testified in support of the application. Various documents were also presented and marked as exhibits.

On August 21, 2008, AEC and API filed their "Formal Offer of Exhibits with Compliance and Manifestation", which are hereby admitted for being relevant and material to the resolution of the instant application.



On August 28, 2008, AEC and API filed a "Manifestation" stating that notwithstanding the testimony of their witness, Engr. Alberto R. Dalusung III, they were inclined to *"follow the computed Capacity Fee Multiplier of P807.47 per kW-month as embodied in Schedule 1, letter "A" of the Amended Agreement"* in as much as this *"will be more suitable to address the needs of API to keep up with the rising cost of imported spare parts as well as other operating costs (repairs and maintenance) which can be least described as volatile"*. On even date, the Commission issued an Order directing AEC and API to submit various documents.

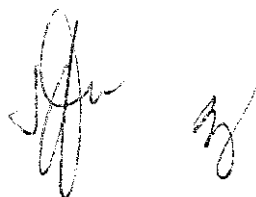
On September 3, 2008, AEC and API filed a "Supplemental Manifestation" where a correction was made on the aforementioned "Manifestation" to include "plus index" on their proposed computation as follows:

"That in order to be consistent with the Amended Agreement, said Manifestation should read: "follow the computed Capacity Fee of P804.47 per kW-month **plus index** as embodied in Schedule 1, letter "A" of the Amended Agreement ."

On September 4, 2008, AEC and API filed their "Compliance" with the Commission's directive in its Order dated August 28, 2008.

On September 9, 2008, AEC and API filed their "Urgent Ex-Parte Motion for Early Resolution".

Upon evaluation of the submissions made by AEC and API, it was revealed that API has been suffering substantial loss of income since March 2008 attributable to the significant increase in fuel cost and its inability to recover



the same from AEC due to the ceiling provision in the EPA pegged by the Commission at the TOU rates of NPC and the wheeling rates of TRANSCO.

Thus, on September 15, 2008, the Commission issued an Order provisionally approving the instant application.

On October 30, 2008, the Commission conducted another hearing and propounded clarificatory questions to the witnesses of AEC and API. AEC and API were then directed to submit supplemental documents.

On November 10, 2008 and December 4, 2008, respectively, AEC and API submitted its "Supplemental Offer of Exhibits and Compliance" and "Urgent Motion for Rendition of Decision".

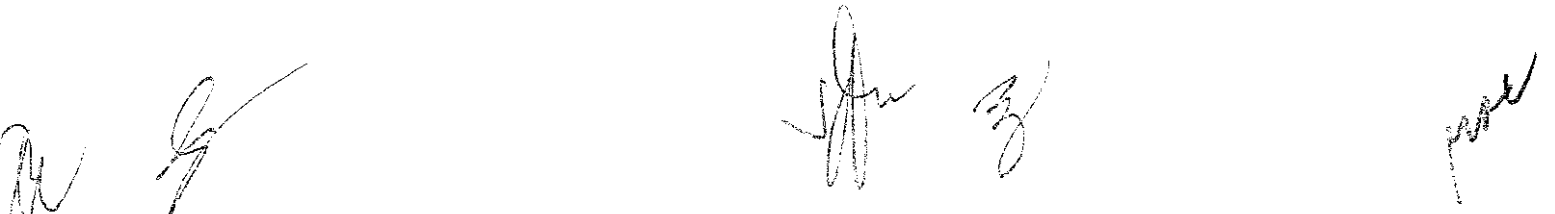
DISCUSSION

The salient features of the AEPA between AEC and API are as follows:

AEC's Power Requirements (2009-2012)

In Kilowatt-hour (kWh)			
YEAR	TOTAL	NPC	API
2009	374,655,070	242,655,070	132,000,000
2010	380,274,896	248,274,896	132,000,000
2011	385,979,020	253,979,020	132,000,000
2012	391,768,705	259,768,705	132,000,000

Based on the foregoing table, API's load was calculated at 11,000,000 kWh-month which is twenty-four percent (24%) lower than the contracted energy of 14,520,000 kWh-month as stipulated in the AEPA.



Procurement Process

There was no procurement process conducted by AEC and API as attested to by Mr. Geromin T. Nepomuceno, President of AEC, due to the urgency of the relief being sought and the critical financial situation being experienced since April 2008.

With the operational constraint of TRANSCO, the only feasible alternative is another embedded diesel plant. However, it will take at least two (2) years to construct another power plant.


Fuel Procurement Process

API has been procuring its fuel requirement on a month-to-month (spot) basis for the past two (2) years. The Commission made a comparative analysis of these spot purchases vis-à-vis the fuel purchases of an IPP based on long term contracts. It yielded an average of 3.72% savings, as follows:

Comparative Bunker Fuel Purchase Costs from Petron Corporation
API Spot Bunker Purchase (WPP Pricing) versus IPP Power (Term Bunker Purchase
Based on MOPS Pricing)

Effective Cost (Php/Liter)	Feb. 2008	Mar. 2008	Apr./May 2008	Average
API	21.0976	21.5228	23.3295	21.8463
IPP	20.3122	20.1811	22.6969	21.0634
Variance	3.87%	6.65%	2.79%	3.72%

API should have considered the feasibility of a contracted fuel purchase and conducted transparent competitive fuel procurement under the Mean of



Platts Singapore (MOPS) pricing formula on kiloliter basis (not time bound) based on the estimated requirements for the next three (3) years.

Contracted Capacity and Energy vis-à-vis Plant Factor

A five (5) year review of API's electricity sale to AEC disclosed a range of 6% to 51% reduction from its contracted energy of 14,520,000 kWh. On the other hand, 65% to 77% of API's electricity sales came from the One-Day Power Sales (ODPS) program of NPC which account for the 11.3% to 27.9% capacity utilization of API's generating units. Shown below are the data on its contracted energy:

YEAR	GENERATION (kWh)	ELECTRICITY SALE (kWh)	GENERATION* (kWh) – MAXIMUM CAPACITY	CAPACITY UTILIZATION FACTOR (%)
2004	67,297,048	243,737,698.00	240,900,000	27.9
2005	41,083,950	164,049,837.91	240,900,000	17.1
2006	33,050,300	129,259,379.03	240,900,000	13.7
2007	42,110,250	185,109,370.70	240,900,000	17.5
2008	27,275,266	80,865,814.12	240,900,000	11.3

* As per Maximum Cap.- 27.5 MW

For a contracted energy of 14,520,000 kWh, the plant is expected to have a 72% capacity utilization to fully serve the contracted energy requirement.

Purchase Power

For a ten (10) year period from the start of the renewal date, AEC shall purchase from API a minimum of 14,520,000 kWh per month contracted energy and a minimum capacity of 22,000 kW contracted demand. API shall charge AEC with a Capacity Fee, an Energy Fee and a Service Fee with the Ceiling, Floor and TOU Tariff deleted from the EPA signed last November 30, 2004.

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The Capacity, Energy and Service Fees are all adjusted with the respective escalation formulae and shall be applied monthly or as mutually agreed upon by AEC and API, depending on the availability of official government statistics.

The formula in the ERB-approved contract between AEC and API and the computed values from July 25, 2004 to August 25, 2004 power bill and plant operations reports were used as reference values.

a. Capacity Fee (CF)

$$\text{CF} = \left[\frac{\text{Fuel, Light and Water Component of Consumer Price Index}}{190.10} \right] \times \text{P804.47 per kW-month} \times \text{Registered Maximum Demand}$$

where:

The FLW is the Fuel, Light and Water component of the Consumer Price Index (CPI). The base FLW Index is 190.10 for July 2004 based on information from the National Economic Development Authority (NEDA).

The PhP804.47 per kW-month is the computed CF multiplier based on the previous contract. This multiplier has local (PhP502.26 per kW-month) and foreign components (PhP302.21 per kW-month).

The foreign component shall be adjusted regularly for escalation as follows: *The US Dollar component shall be converted to the Peso equivalent at the prevailing selling rate for the US Dollar. Under*



this renewal contract, AEC recognizes the impact of this under-recovery by adjusting the base foreign exchange rate to PhP50.00/US\$. Any change in the value of the Peso relative to the US Dollar will proportionally affect the foreign exchange component of the CF.

The Registered Maximum Demand is equal to the actual metered kW consumption or the guaranteed minimum off-take of 22,000 kW per month.

b. Energy Fee (EF)

$$EF = \frac{[(\text{Actual Cost of Bunker, PhP/Liter}) / 12.8206] \times 3.6282 \times \text{Actual kWh}}{\text{Actual kWh}}$$

where:

The actual cost of bunker, PhP/Liter is the delivered cost of bunker fuel to the Calibutbut Power Plant.

The PhP12.8206 per liter is the reference cost of bunker fuel.

The PhP3.6282/kWh is the Energy Fuel Multiplier which is equal to the actual metered kWh consumption or the guaranteed minimum off-take of 14,520,000 kWh per month.

c. Service Fee (SF)

$$SF = \frac{[(\text{Fuel, Light and Water Index}) / 190.10] \times 0.2504 \times \text{Actual kWh}}{\text{Actual kWh}}$$



where:

The FLW Index is the same index used for the CF which shall be adjusted based on the FLW component of the CPI.

The PhP0.2504 is the computed Service Fee multiplier using the previous contract.

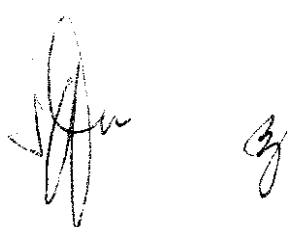
The actual kWh is equal to the actual metered kWh consumption or the guaranteed minimum off-take of 14,520,000 kWh per month.

The following table shows the resultant power rate based on the simulation of API for the period 2008-2012:

POWER RATE	2008	2009	2010	2011	2012
Capacity Fee (P/kW-Mo.)	743.0500	765.3400	788.3000	811.9500	836.3100
Energy Fee (P/kWhr.)	7.0208	7.0208	7.0208	7.0208	7.0208
Service Fee (P/kWhr.)	0.5573	0.5740	0.5912	0.6089	0.6272

The Proposed Purchase Power Rate

In line with the manifestation to delete the ceiling price pegged on the NPC-TOU tariff less ten (10) centavos per kilowatt-hour to be applied on API's electricity sale to AEC, and to determine the reasonableness of API's proposed power rate, the Commission computed the cost of generation by using an annuity of the historical cost of the Property Plant and Equipment (PPE) as converted in its appropriate peso equivalent and adopted the 15% cost recovery mechanism as provided for by API in its submitted financial model for the duration of the remaining economic life of the plant.



All data were sourced from API's Audited Financial Statements (2006 and 2007) with reference to the various documents submitted by the parties.

API's proposed power rate was determined as follows:

COMPONENT	RATE
Capacity Fee (PhP/kW-Mo.)	247.34
Energy Fee (PhP/kWh)	*
O & M Fee (P/kWh) ¹	0.33

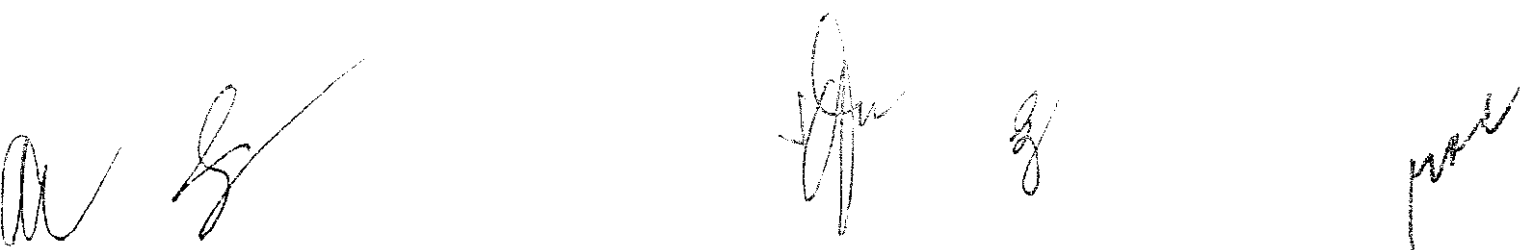
* Energy Fee will be based on a fuel consumption rate of 0.2597 liters/kWh
¹Subject to escalation using CPI

a. Capital Recovery Fee

The Capital Recovery Fee (CRF) refers to the cost of the Contractor's recovery of capital investment, including a return on its investment over its remaining useful life. As defined, CRF is an investment recovery fee intended for non-volatile and stable project cost and not elastic or moving.

The Financial Model submitted by API and AEC yielded a derivation of Capacity Fee which includes labor costs and fixed operation costs escalated by using the FLW index.

The updated net carrying amount of the item Property Plant and Equipment (PhP365,540,204.70) as of September 2008 was utilized and reconciled with the 2007-2006 AFS.



The Labor Costs and Fixed Operations Cost which were already considered in the computation of API's Capital Recovery Fee were excluded.

To determine the PhP/kW annual capital recovery fee, the Commission used the billing determinant of 270,000 kW-month which was derived by multiplying the 75% capacity factor by the generation capacity of 30 MW or 22.5 MW. It was converted to kW by multiplying 1000 and further multiplying its product by twelve (12) months.

Tabulation of the CRF computation:

PPE (As of September 8, 2008)	PhP365,540,204.70
Annuity Return (15% rate over the useful life of the asset)	PhP66,782,873.15
Billing Determinant Used	270,000 kW-Month
Levelized Cost (PhP/kW-Month)	P247.34

b. Energy Fee

A simulation of the formula for the Energy Fee as reflected in the AEPA for the cost of bunker fuel to Calibu Power Plant yielded a fuel consumption of 0.2830 liter/kWh.

On the other hand, the provisional authority issued by the Commission in its Order dated September 15, 2008 authorized API to utilize a 0.2597 liter/kWh fuel consumption as established during the August 8, 2008 hearing in the instant application.

A comparison of the two (2) resultant fuel consumptions yielded a variance of 0.0233liter/kWh:



PARTICULARS	Fuel Consumption (liter/kWh)
Simulation of the formula	0.2830
PA issued 09/15/08	0.2597
Variance	0.0233

The Energy Fee as provided for in the said Order, which was used in the computation of API's Energy Fee, is as follows:

$$EF = 0.2597 \text{ liter/kWh} \times \text{Actual kWh} \times \text{Actual Cost of Bunker, PHP/liter.}$$

where:

The 0.2597 liter/kWh is the fuel consumption of the Calibu Power Plant as established during the August 8, 2008 hearing

The actual cost of Bunker is the delivered cost of bunker fuel to the Calibu Power Plant

The actual kWh is equivalent to the actual metered kWh consumption

c. Service Fee

Since the computation of API's capital cost recovery has already been incorporated in the rate of return as indicated in the model, except for the 15% IRR, the Commission finds the service fee to be redundant.

d. Operation and Maintenance (O & M) Fee

During the confirmation of the Capital Recovery Fee in API's financial model, the Commission noted that the Labor Costs and Fixed Operations Cost (Operations and Maintenance) were integrated in API's computation of Capital Recovery Fee and subsequently, excluded in the determination of API's Capital Recovery Fee.

However, cognizant of the value of these costs to API's rate structure, the Commission computed its allocation and inflation factors to account for the variation in the value and purchasing power of the peso throughout the contract period.

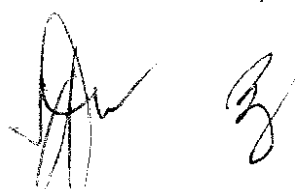
A total of PhP65,164,499.93 administrative cost in API's YTD 2007-2006 AFS was calculated to be directly attributable to the power plant operation. To come up with an O & M fee, the billing determinant of 270,000 kW-month was adopted divided by 720 hours per month for its conversion to kWh or a resultant value of PhP241.35/kW-Month or PhP0.33/kWh.

These O & M fees shall be adjusted to the monthly CPI for the Philippines for All Income Households (All Items), as reported by the National Statistics Office (NSO), based on the following formula:

$$\frac{CPI_B}{CPI_A} \times \text{PhP}0.33/\text{kWh}$$

where:

CPI_B = Monthly Consumer Price Index for the Philippines for All Income Households (All Items) as reported by the



National Statistics Office (NSO) for the month immediately before the billing month

CPI_A = Monthly Consumer Price Index for the Philippines for All Income Households (All Items) as reported by the National Statistics Office (NSO) on the date the Extended EPA was made and entered into last July 2004

To determine the reasonableness of the computed O & M for API, the Commission made a comparison among the approved O & M for Diesel-Fired Power Plants, as follows:

PARTICULARS	API	PANAY POWER	CAPELCO
Capacity	30 MW	72 MW	20 MW
Location	Luzon	Visayas	Visayas
O & M Fee (P/kWh)	0.33	1.25	0.17
ERC Case No.	-	2005-043 RC	2007-096 RC
Date of Decision	-	Dec. 14, 2005	Mar. 12, 2008

To determine the effect of inflation in the base rate, a simulation was done on the adjustment for the O & M fee using the Economist Intelligence Unit (EIU) average annual inflation forecast for the Philippines covering the period 2009 to 2012, to wit:

COST COMPONENT	2008	2009	2010	2011	2012
	-	3.1%	2.4%	2.5%	2.4%
O & M Fee (subject to inflation factor)	0.43	0.443	0.454	0.465	0.476

• Escalated to December 2008 CPI

The simulation yielded minor changes in terms of the effect of inflation to the computed O & M component on the proposed rate.

WHEREFORE, the foregoing premises considered, the provisional authority granted to Angeles Electric Corporation (AEC) and Angeles Power Incorporated (API) on September 15, 2008 is hereby made PERMANENT subject to the following modifications:

1. The base rate shall be as follows:

FEES	RATE
Capacity/Capital Recovery Fee (PhP/kWh-Mo.)	247.34*
Service Fee (PhP/kWh)	-
O & M Fee (PhP/kWh)**	0.33
Energy Fee (PhP/kWh) ***	-

* Fixed

** To be escalated based on CPI

*** Energy Fee will be based on a fuel consumption rate of 0.2697 liters/kWh

API is hereby directed to conduct a transparent competitive fuel procurement under MOPS pricing formula on kiloliter basis (not time bound) based on estimated requirements for three (3) years. AEC and API are further directed to review the guaranteed off-take stipulation in the AEPA and reconcile it with the forecasted power requirement of AEC for 2009-2012.

SO ORDERED.

Pasig City, March 2, 2009.


ZENAIDA G. CRUZ-DUCUT
Chairperson


RAUF A. TAN
Commissioner


ALEJANDRO Z. BARIN
Commissioner


MARIA TERESA A.R. CASTAÑEDA
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