

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



**IN THE MATTER OF THE JOINT
APPLICATION FOR APPROVAL OF THE
TRANSITION SUPPLY CONTRACT
BETWEEN THE NATIONAL POWER
CORPORATION AND MANILA ELECTRIC
COMPANY WITH PRAYER FOR
PROVISIONAL AUTHORITY**

ERC CASE NO. 2009-1370-ED

**NATIONAL POWER CORPORATION
(NPC) AND MANILA ELECTRIC
COMPANY (MERALCO),**

Applicants.

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Date: **JAN 20 2010**
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ORDER

For resolution by the Commission is the "Joint Motion for Partial Reconsideration and Clarification" filed by Manila Electric Company (MERALCO) and National Power Corporation (NPC) on September 4, 2009.

In the said Joint Motion, MERALCO and NPC pray for the following:

1. Reinstatement of Section 6.3, 6.4 and 6.5 of their Transition Supply Contract (TSC); and
2. Clarification that after considering the arguments presented, any Decision rendered imposing certain limitations or prohibitions on the exercise of the rights and obligations of the parties under the TSC, be applied or implemented prospectively.

Sections 6.3, 6.4 and 6.5 of the TSC read as follows:

"6.3 At the option of MERALCO, it may source power from NPC in excess of the Contract Energy by a quantity equivalent to not more than twenty percent (20%) thereof. Such excess energy does not refer to ODPS, CCP and other special NPC programs. MERALCO shall be liable to NPC for any excess consumption up to 120% of the Contract Energy, as may be extended pursuant to Section 5.2 and shall pay to NPC the excess energy above 100% based on an additional 20% "

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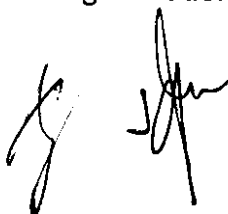
premium over and above of the Contract Energy Charge (inclusive of adjustments). Any energy consumption by MERALCO in excess of 120% of the Contract Energy shall be deemed taken from the WESM.

6.4 Upon request of MERALCO within twenty four (24) hours from occurrence of shutdown or inability of any or all of MERALCO's IPPs for any reason whatsoever, NPC shall furnish replacement power to MERALCO in case of (sic). Such replacement power supplied shall be priced at the true cost of generating such replacement power plus ten percent (10%), plus all applicable ERC-approved charges and fees.

6.5 If for a particular period where NPC cannot deliver the volume of electricity it commits to MERALCO, and MERALCO was able to source the equivalent quantity from another generator/generation company, NPC shall compensate MERALCO the incremental cost of replacement energy."

In support of the prayer for the reinstatement of Section 6.3 in their TSC, MERALCO and NPC contend, among others, that the additional twenty percent (20%) volume under the subject TSC is different from the 20% bandwidth referred to in Section 6.1 of the duly approved TSC Template. Instead, it is an additional volume which can be availed by MERALCO, at its option, whenever sourcing from the TSC, even at a premium, is cheaper than sourcing from the Wholesale Electricity Spot Market (WESM). Moreover, MERALCO and NPC aver that Section 6.3 essentially provides MERALCO an effective instrument to ensure that it will be able to continuously supply power at relatively stable prices to its end-users.

With reference to the premium charges equivalent to 20% of the Contract Energy, it was defined as the average cost that will be incurred by NPC when sudden changes in the demand forecast brought by tight supply-demand situations, transmission congestion incidents and other fortuitous events result in a corresponding adjustment in the generation mix. Allegedly, it covers the



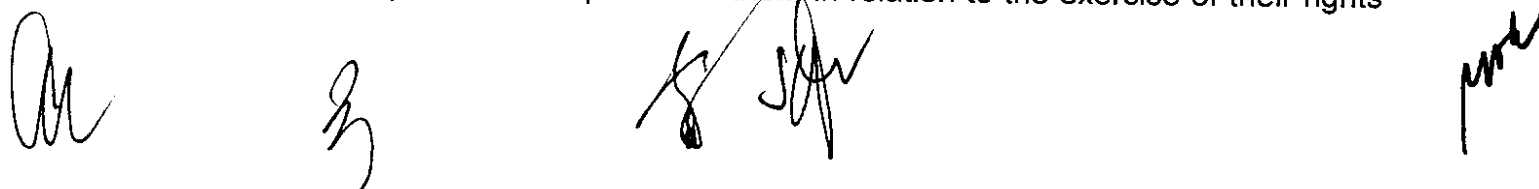
increase in fuel costs and other operational and administrative costs which was adopted by NPC in accordance with the TSC template for distribution utilities under Resolution No. 8, Series of 2005.

In Sections 6.4 and 6.5 of their TSC, MERALCO and NPC submit that the said stipulations are in line with the objective of reliable and adequate power supply, similarly intended for the protection and benefit of end-users. It is only prudent to provide contingency measures rather than be exposed to potentially higher WESM prices during occurrences contemplated in the subject provisions.

Moreover, it is argued that the inclusion of Sections 6.4 and 6.5 is practical, efficient, systematic and cost effective as unnecessary negotiations will be reduced including savings on additional time, effort, resources and costs to be incurred in coming up with a separate agreement which would again be subject to separate approval by the Commission.

MERALCO and NPC further qualify that in the situation being contemplated, they would need to exert additional effort and deploy additional resources, entailing additional cost, to compensate for the deficiency in the energy supply caused by circumstances beyond the reasonable control of the parties or even the Independent Power Producers (IPPs). The incremental cost incurred due to replacement power is stipulated to cover such additional and inherent cost. Premised on these, they submit that it is only fair and equitable that the ultimate beneficiaries, who are the end-users, bear the cost of an adequate and reliable supply of power.

Lastly, MERALCO and NPC cite that a prospective application of any limitation or prohibition imposed on them in relation to the exercise of their rights

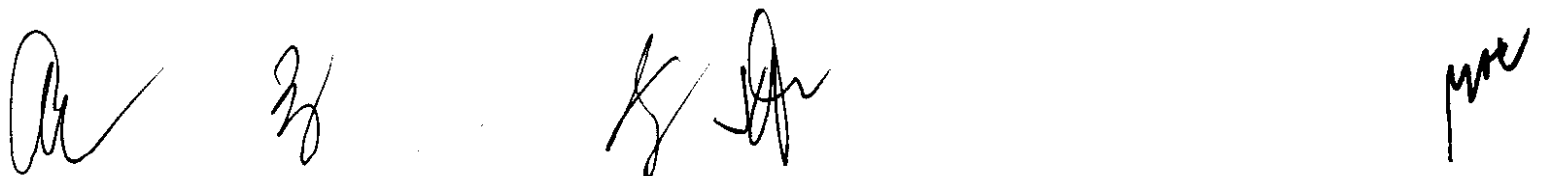
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and obligations under the TSC would be consistent and in line with due process and fairness. Since the Commission has held that the TSC is reasonable and will benefit MERALCO's end-users, they pray that the TSC be allowed to be implemented in *toto*, including Sections 6.3, 6.4 and 6.5, in accordance with the Commission's Order dated January 22, 2007.

DISCUSSION

After due consideration of the issues raised by MERALCO and NPC, the Commission is convinced that the additional 20% volume referred to in Section 6.3 (in excess of the 100% contracted energy) is distinct from the 20% bandwidth contemplated in Section 6.1 of the TSC Template. The Commission acknowledges that the additional 20% provides MERALCO a mechanism by which it would be able to cope with the changing customer demands and hedge against exposure from the volatile spot market prices, for the protection of the end-users.

However, in implementing the said provision, MERALCO must observe its obligation to supply electricity in the least cost manner to its captive market pursuant to Section 23 of Republic Act No. 9136. Thus, the implementation of Section 6.3 should be subject to the condition that the cost of the excess supply equivalent to the National Power Corporation-Time of Use (TOU) rate plus the 20% premium must be lower than the hourly equivalent settlement price in the WESM or cost of replacement power. Therefore, the recoverable cost by MERALCO from its end-users, in this respect, shall be the TOU rate plus 20% premium or the equivalent settlement price in the WESM or cost of replacement power, whichever is the lowest among the three (3) rates. Further, in the event that MERALCO exercises the said option contained in Section 6.3 of the TSC, it

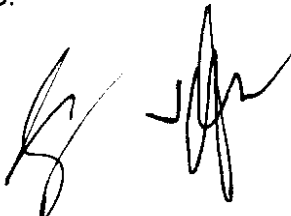


should submit a report to the Commission of its implementation including the particular hourly rates prevailing in the WESM when the same was availed of.

As regards Sections 6.4 and 6.5, MERALCO and NPC assert that it is logical and expedient to include provisions in the TSC not related to the contracted supply but would address circumstances affecting the continuous delivery of electricity. Section 6.4 of the subject TSC contemplates a situation where MERALCO's IPPs are not able to supply power due to outages or other contingencies with NPC agreeing to augment the deficiency at an agreed price and Section 6.5 refers to an occurrence where NPC is unable to supply its contractual obligations to MERALCO and would source any replacement from the latter's IPPs with the incremental cost to be paid for by NPC.

The Commission maintains the deletion of Section 6.4 from the TSC as it contemplates concerns beyond the TSC transactions and therefore should be subject to a separate agreement between MERALCO and its supplier IPPs. On the other hand, the Commission is convinced that Section 6.5 can be reinstated as this still involves contracted supply drawn from NPC and thus can be included in the TSC. Moreover, Section 6.5 clearly establishes NPC's accountability with respect to the incremental cost that would be incurred if and when the scenario contemplated in Section 6.5 occurs. Relative to this, MERALCO must submit a report on instances where it has exercised the option to obtain replacement power to ensure that such replacement power is actually due to necessity and not merely to benefit the interest of any party.


WHEREFORE, based on the foregoing, the June 30, 2008 Decision is hereby modified as follows:



1. Sections 6.3 and Section 6.5 of the Transition Supply Contract (TSC) between Manila Electric Company (MERALCO) and National Power Corporation (NPC) are hereby reinstated;
2. In the implementation of Section 6.3 of the TSC, the recoverable cost from MERALCO's end-users shall be the NPC Time of Use (TOU) rate plus 20% premium or the equivalent settlement price in the Wholesale Electricity Spot Market (WESM) or cost of replacement power, whichever is the lowest among the three (3) rates; and
3. MERALCO shall submit reports on instances when the implementation of: a) Section 6.3 has been made, which shall include the particular settlement price in the WESM or cost of replacement power on the interval hour affected; and b) Section 6.5, which shall include reasons for the inability of NPC to supply its contractual obligations under the TSC.

SO ORDERED.

December 14, 2009, Pasig City


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Chairperson


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Commissioner


ALEJANDRO Z. BARIN
Commissioner


MARIA TERESA A.R. CASTAÑEDA
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