

ANNEX “A”

Republic of the Philippines
ENERGY REGULATORY COMMISSION
Ortigas Avenue, Pasig City

IN THE MATTER OF THE AMENDMENT OF THE RULES FOR THE APPROVAL OF REGULATED ENTITIES’ CAPITAL EXPENDITURE PROJECTS

This is to amend Articles I, II, III, IV and VI of the Rules for the Approval of Regulated Entities’ Capital Expenditure Projects.

Article I of the said Rules is hereby amended to read as follows:

“Article I

GENERAL PROVISIONS

1.1 Xxxx

1.2 Xxx

1.3 Definition of Terms

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Electric Cooperative
Distribution Utility
Planning Manual
(ECDUPM)

The **Planning Manual** collaboratively crafted by NEA, PHILRECA, NAGMEC, AMRECO and ERC with the assistance of IFC that will provide guidance for the systematic and economic expansion and rehabilitation of distribution facilities and the acquisition of assets necessary to respond to the needs of the electric cooperative’s consumers and enable the ECs to meet safety performance standards and regulatory requirements and the structural and/or institutional planning and development of the ECs.

Xxx”

Article II of the said Rules is hereby amended to read as follows:

“Article II

CLASSIFICATION OF CAPITAL EXPENDITURE PROJECTS

2.1 Capital Asset Categories

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2.2 Planning Criteria of Capital Assets

2.2.1 Electric Cooperative Distribution Utility Planning Manual (ECDUPM)

The planning procedures shall be in accordance with the ECDUPM, hereto attached as addendum.

2.2.2 Planning Horizon

Proposed capital projects of Regulated Entities must be economically efficient and therefore must be planned and studied thoroughly. While it is prudent to install assets with some surplus capacity to cater to future growth in demand, it is not economically efficient to install assets where the capacity is so large that it would not be fully-utilized at the end of the assets' economic life.

The planning periods over which future load growth can be allowed for shall not exceed the following:

- a) Fifteen (15) years for high voltage (HV) lines or subtransmission lines, substations (excluding transformers), primary distribution circuits and points of connection to a transmission network;
- b) Ten (10) years for substation transformers; and
- c) Five (5) years for medium voltage (MV) and low voltage (LV) distribution, and other network assets.

Alternative planning periods may be adopted depending on the appropriate concentration of business districts, density of urbanized areas or geographic locations and conditions. Such planning periods must be properly justified.

The appropriate span of the planning period is a function of the following factors:

- a) The anticipated load levels at the end of the planning period.

- b) The forecasted growth rate of the system or major portions of the system;
- c) The age of the electrical supply facilities, both at the beginning and the end of the period. Particular attention must be given to the percentage of the facilities which are or will be beyond their useful life; and,
- d) The validity of the future economic factors, such as inflation rate, especially toward the end of the planning period, which are being used for the engineering economic analysis of the alternate plans in the study.

2.3 Capital Expenditure Project Type

- a) Safety;
- b) Capacity (including customer requirements);
- c) Power Quality;
- d) Rural electrification and other projects with funding subsidy;
- e) Reliability Improvements above performance standards; and
- f) System Loss Reduction above performance standards.

2.4 Capital Expenditure Project Categories

- a) Subtransmission Development;
 - Acquisition (of TransCo Subtransmission Lines);
 - Refurbishment (of acquired TransCo Subtransmission Lines);
 - and
 - Reinforcement (to meet capacity and reliability criteria).
- b) Substation Project;
 - Upgrading (of capacity of existing substation); and
 - New (substation in new location).
- c) Primary Distribution Project;
 - Network Expansion;
 - Safety and Protection; and
 - Power Quality Correction.
- d) Secondary Distribution Project;
 - Network Expansion; and
 - Rehabilitation.
- e) Reliability Improvement Projects;

- f) System Loss Reduction Projects;
- g) Other Network Requirements (Distribution Transformers, Secondary Lines, Customer Service Drops and Metering Equipment); and
- h) Non-Network Requirements (General Plant Assets, Vehicles, Tools, etc. needed for utility operation)

2.5 Capitalization of Operating or Maintenance Expenses

The International Accounting Standards (IAS) adopted in the Philippines will apply with regard to the capitalization of operating and maintenance expenses by Regulated Entities. In general, only those operating expenses incurred directly in the course of establishing capital assets can be capitalized to become part of the value of the associated assets and therefore to be included in the capital expenditure forecasts.

Cost components that can be capitalized are:

- purchase price, including import duties and non-refundable purchase taxes, and any directly attributable costs of bringing the asset to working condition for its intended use, e.g., cost of site preparation, initial delivery and handling costs, installation costs, professional fees such as for architects, engineers and project managers, and estimated cost of dismantling and removing the asset and restoring the site, and the estimated costs of dismantling and removing the asset as a provision under IAS 37, Provisions, Contingent Liabilities and Contingent Assets;
- borrowing costs allowed under IAS 23, to the extent that these are not already recovered through the CWIP factor;
- administration and other general overhead costs and start-up and similar pre-production costs which are directly attributed to the acquisition of the property, plant and equipment and/or bringing the asset to its working condition;
- major spare parts and stand-by equipment qualifying as property, plant and equipment;¹ and
- regulatory expense such as permit fees.

For subsequent expenditures on assets, capitalization shall be done only when it is probable that future economic benefits, in excess of the originally

¹ These qualify when the Regulated Entity expects to use them during more than one period. If the spare parts or servicing equipment can be used only in connection with an item of property, plant and equipment and their use is expected to be irregular, they are accounted for as property, plant and equipment and are depreciated over a time period not exceeding the useful life of the related asset.

assessed standard of performance of the existing asset, will flow to the enterprise. As such, the expenditure improves the condition of the asset beyond its originally assessed standard of performance, as follows:

- modification of an asset to extend its useful life, or increase its capacity;
- upgrade of assets to achieve a substantial improvement in the quality of output; and
- adoption of new production processes enabling a substantial reduction in previously assessed operating costs.

The following items are to be excluded from capitalized costs:

- any trade discounts and rebates given in relation to the asset;
- initial operating losses incurred prior to an asset achieving planned performance;
- applicable government grants in accordance with IAS 20 (Accounting for Government Grants and Disclosure of Government Assistance); and
- expenditure on repairs or maintenance of property, plant and equipment made to restore or maintain the future economic benefits that an enterprise can expect from the originally assessed standard of performance of the asset. For example, the cost of servicing or overhauling plant and equipment is usually a maintenance expense since it restores, rather than increases, the originally assessed standard of performance.

Regulated Entities have to describe their general approach to capitalization of expenses. Any administrative, management, governance or other overhead costs to be capitalized must be separately identified to the ERC in the capital expenditure forecasts, together with the justification for this decision and the manner in which the costs involved are calculated. The ERC may decide to accept the reasonableness costs as part of the capital expenditure forecasts, or may decide to reclassify them as operating and maintenance costs (if deemed efficient and reasonable).”

Article III of the said Rules is hereby amended to read as follows:

“Article III

FILING OF THE APPLICATION

3.1 Time of Filing of Capital Expenditure Program

A Regulated Entity shall submit its proposed ~~three (3)~~ five (5) year capital expenditure program in accordance with the prescribed groupings and schedule. The grouping and schedule is appended as Annex A and is hereby made an integral part of this Rule.

The succeeding capex applications shall be filed by DUs, depending on their grouping in Annex A, on the first quarter or 3rd quarter of the year before the start of the next 5-year period capex application.

Capital Expenditure Projects involving joint ventures/consortium of Distribution Utilities or Regulated Entities shall be filed one (1) year before the project is implemented through a joint application by the concerned Regulated Entity.

3.2 Requirements for Filing the Application of Capital Expenditure Program

3.2.1 Filing Requirements

A Regulated Entity shall submit to ERC its capital expenditure program for a period of five (5) years. The periodic filing of these proposed capital expenditure projects shall be made for review and approval of the ERC. Proposed capital projects must be categorized in accordance with Article II. This expenditure program also includes the capital projects that form part of the system loss reduction program.

The three (3) year capital expenditure program shall be consistent with the five (5) year rolling DDP submitted by the Regulated Entity to the DOE.

The application for the approval of the three (3) year capital expenditure program shall be verified by an authorized representative of the Regulated Entity, which has to present either a Board Resolution or Secretary's Certificate to show proof of his / her designation as a representative of the Board of Directors and shall be filed with the ERC together with properly labeled three (3) hard copies and three (3) electronic copies. The capital expenditure program shall be accompanied by the following documents:

3.2.1.1 Title of the project;

3.2.1.2 Type of the projects in accordance with Section 2.3;

- 3.2.1.3 Category of the projects in accordance with Section 2.4;
- 3.2.1.4 Description of each capital project (Detailed description of the Project);
- 3.2.1.5 Gantt Chart Schedule of the proposed capital expenditure projects;
- 3.2.1.6 Project Justifications (Describe the problem being addressed by the project and consequences if the project is not pursued);
- 3.2.1.7 Project Cost Estimates which has to be in reference to the submitted engineering design and bill of materials;
- 3.2.1.8 Technical Analysis² (Summary of Options / Alternatives considered. Simulation and interpretation of results showing the electrical effects of the proposed project/s such as power transformer loadings, voltage drop, power quality, power factor, system loss, frequency, harmonics, load / phase balancing etc. Criteria and System Performance without and with the proposed project);
- 3.2.1.9 Economic Analysis (Summary of technically feasible projects that are evaluated, the present value of life cycle costs of each project alternative, and the financial indices (NPV and B/C). Mandatory project must be marked as least-cost);
- 3.2.1.10 Annexes (Data and assumptions used in technical and economic analysis, calculation sheets, simulation reports, and other relevant information such as diagrams, drawings and pictures);
- 3.2.1.11 Regulated Entity's Distribution Development Plan;
- 3.2.1.12 Project Financing Plan³ (the MC/CAPEX fund, in the case of Electric Cooperatives, shall be utilized to finance the proposed capital expenditure projects and also for the payment of amortization in the case of project financing loans);
- 3.2.1.13 Board Resolution or Secretary's Certificate approving the proposed Projects;
- 3.2.1.14 Sworn Statement from the authorized representative of the Regulated Entity that an application for approval from the concerned agencies that may have interest in the proposed project has been filed / or shall be filed by the Regulated Entity

² Updated System Loss segregation data shall be included together with other parameters deemed relevant in the conduct of the technical analysis.

³ In the case of project financing loans, the cost of money should not be greater than the prevailing market rate.

(specify date of filing and furnish ERC a copy within five (5) days upon filing);

3.2.1.15 Proof/s that public information dissemination of the proposed capital expenditure program was conducted by the Regulated Entity. At the minimum, the Regulated Entity should show proof of posting in at least three conspicuous places within its franchise area, of a notice containing the following: 1) the proposed projects; 2) the reasons for proposing said projects; 3) the source of fund for the said projects; and 4) indicative rate impact of the said projects, if any; and

3.2.1.15 Approval to secure loans sourced from NEA may be filed together with the capex application.

Subsequent filing of capital expenditure applications shall be based on the capital expenditure projects as indicated in the rolling DDP submitted by the Regulated Entity.

Any petition, application or action to be filed herein shall be governed by the provision of Rate Case (RC) application as provided for in the existing Rules of Practice and Procedure Governing Hearings before the ERC, the pertinent provisions of the Act or its IRR and other related laws.

3.2.2 Project Justification Templates⁴

For purposes of uniformity, a project justification form or template is provided herewith as Annex B and shall be accomplished upon filing of the proposed capital projects. Content of this template is discussed in the ECDUPM.

3.3 Force Majeure or Fortuitous Event Capital Expenditure

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Article IV of the said Rules is hereby amended to read as follows:

“Article IV

EVALUATION AND APPROVAL OF THE APPLICATION

4.1 Evaluation of Capital Expenditure Program

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4.2 Permit Fees

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⁴ See Annex A – Justification for Capital Project.

4.3 Cost of Suit

All ECs shall bear the regulatory implementation cost or costs associated with the implementation of this Rules, including but not limited to, cost attendant to the public hearings in the EC's localities."

Article VI of the said Rules is hereby amended to read as follows:

"Article VI

FINAL PROVISIONS

6.1 Administrative Sanctions

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6.2 Transitory Provision

The initial capex application shall be filed in accordance with the Table below. Grouping is based on geographic regions and the regular CAPEX filing will be every five (5) years

Group (Region)	No. of ECs	Deadline of CAPEX Submission	Initial CAPEX Plan Coverage	Period	Subsequent Filing of CAPEX and every 5-years thereafter
X and X1	20	March 2010	2010 – 2012	3 years	1 st Quarter of 2012
I	9	May 2010	2010 – 2012	3 years	3 rd Quarter of 2012
II	9	June 2010	2010 – 2013	4 years	1 st Quarter of 2013
III	13	July 2010	2010 – 2013	4 years	3 rd Quarter of 2013
IV	14	August 2010	2010 – 2014	5 years	1 st Quarter of 2014
V	11	Sept. 2010	2010 – 2014	5 years	3 rd Quarter of 2014
VI	10	Oct. 2010	2011 – 2015	5years	1 st Quarter of 2015
VII	10	Nov. 2010	2011 – 2015	5 years	3 rd Quarter of 2015
VIII	11	Dec. 2010	2011 – 2016	5 years	1 st Quarter of 2016
IX and XII	14	Jan. 2011	2011 – 2016	5 years	3 rd Quarter of

Thereafter, the proposed five (5) year capital expenditure projects as indicated in the rolling DDP of the Regulated Entity shall be filed for approval in accordance with Section 3.1.

Capital projects which have already been included in the applicant's rate base, as approved by the ERC, or those that were already filed for evaluation, or those that were already filed for inclusion in the rate base and presently being evaluated by the ERC shall be excluded from the application of these Rules.

Capital projects which should be implemented before the deadline should be filed separately before implementation.

6.3 Separability Clause

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6.4 Repealing Clause

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6.5 Effectivity

These Rules shall take effect upon its publication in a newspaper of nationwide circulation."

Pasig City, December ____, 2009.

ZENAIDA G. CRUZ-DUCUT
Chairperson

RAUF A. TAN
Commissioner

ALEJANDRO Z. BARIN
Commissioner

MARIA TERESA A.R. CASTAÑEDA
Commissioner

JOSE C. REYES
Commissioner

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