

*mid: OKAL
9/25/06*

IN THE MATTER OF THE APPLICATION FOR APPROVAL OF 1) THE ANNUAL REVENUE REQUIREMENT 2) PERFORMANCE INCENTIVE SCHEME and 3) PROPOSED NEW RATE DESIGN, ALL IN ACCORDANCE WITH THE PROVISIONS OF THE RULES FOR SETTING DISTRIBUTION WHEELING RATES,

ERC CASE NO. 2006- 041 RC

CAGAYAN ELECTRIC POWER AND LIGHT CO., INC.
(CEPALCO),

Applicant,

PRE-TRIAL BRIEF

Applicant CAGAYAN ELECTRIC POWER & LIGHT CO., INC., by counsels, to this Honorable Commission respectfully submits this Pre-trial Brief and states: That –

SUMMARY OF ADMITTED FACTS

1. Herein applicant, CEPALCO, is the exclusive franchise holder to operate an electric light and power services in the City of Cagayan de Oro and the Municipalities of Tagoloan, Villanueva, and Jasaan, all in the Province of Misamis Oriental;
2. Herein applicant has selected to enter Performance-Based Regulation pursuant to the Commission's Resolution No. 12-02, "Adopting a Methodology for Setting Distribution Wheeling Rates (DWRG)";
3. The Honorable Commission has approved applicant's entry to a Performance-Based Regulation (PBR);

4. Applicant has filed an application before the Honorable Commission an application for the approval of is Annual Revenue Requirement (ARR) and Performance Incentive Scheme (PIS) for the Second Regulatory Period;
5. The application is sufficient in form and substance.

PROPOSED STIPULATIONS OF FACTS

1. Applicant has complied with the jurisdictional requirements mandated by this Honorable Commission;
2. CEPALCO's proposed application in all requirements is based on the parameters set forth in the Rules for Setting Distribution Wheeling Rates (RDWR);
3. That applicant is entitled to the relief sought for.

ISSUES TO BE RESOLVED

The issues to be resolved would be:

1. Whether or not the proposed figures or expenditures of the five building blocks for Applicant's proposed Annual Revenue Requirement are necessary and within reasonable magnitude.
2. Whether or not the proposed Annual Revenue Requirement and the resulting Maximum Annual Price will result to distribution wheeling rates that are reasonable
3. Whether or not the proposed Annual Revenue Requirement is in accordance with the Rules for Setting Distribution Wheeling Rates (RDWR) issued by the ERC
4. Whether or not the proposed Performance Incentive Scheme is reasonable
5. Whether or not the proposed Performance Incentive Scheme is in accordance with the RDWR
6. Whether or not the proposed Procedures to Convert the Maximum Annual Price into rates will result to distribution rates that are reasonable

7. Whether or not these proposed procedures are in accordance with the RDWR

DOCUMENTS OR EXHIBITS TO BE PRESENTED

Applicant will be submitting these documents, and that they be correspondingly marked as follows:

1. Acknowledgment of Receipt of the City of Cagayan de Oro- as Exhibit "A"
2. Acknowledgment Receipt of the Municipality of Tagoloan, Misamis Oriental, as Exhibit "A-1"
3. Acknowledgment of Receipt of the Municipality of Villanueva, Misamis Oriental, as Exhibit "A-2"
4. Acknowledgment Receipt of the Municipality of Jasaan, Misamis Oriental, as Exhibit "A-3"
5. Copy of the GoldStar newspaper, issue of August 29, 2006 – as Exhibit "B"
Pages 13-20 as Exh. "B-1" to "B-8"
6. Affidavit of Publication of the Manager of newspaper - as Exhibit "C"

Purpose of Exhibits "A" to "C" - *The Acknowledgment of Receipt documents are to prove that copies of the Application with all its annexes and accompanying documents were received by the legislative bodies of the above-mentioned LGU units, the areas where CEPALCO principally operates. Exhibits "B" and "C" are to prove that the Application was published in a newspaper of general circulation in the same areas. This is to prove compliance of the pre-filing requirements required under Sec. 4 (e) Rule 3 of the IRR of RA 9136.*

7. Certificate of Posting of the City of Cagayan de Oro, as Exhibit "D"
8. Certificate of Posting of the Municipality of Tagoloan, as Exhibit "D-1"
9. Certificate of Posting of the Municipality of Villanueva, as Exhibit "D-2"
10. Certificate of Posting of the Municipality of Jasaan, as Exhibit "D-3"
11. Copy of the Daily Tribune Newspaper, September 3, 2006 issue, as Exhibit "E"

Page 9 as Exhibit "E-1"

12. Affidavit of Publication, as Exhibit "F"

13. Copy of Manila Times Newspaper dated September 3, 2006 issue, as Exhibit "G".

Page A7 as Exhibit "G-1"

14. Affidavit of Publication, as Exhibit "H".

15. Copy of Daily Tribune, September 10, 2006 issue, as Exhibit "I".

Page 5 as Exhibit "I-1"

16. Affidavit of Publication, as Exhibit "J".

17. Copy of Manila Times – September 10, 2006 issue, as Exhibit "K".

Page A7 as Exhibit "K-1"

18. Affidavit of Publication, as Exhibit "L".

Purpose of Exhibits "D" to "L" – These are to prove compliance of jurisdictional requirements as per Order of this Honorable Commission dated September 1, 2006.

19. Application for the approval of the Annual Revenue Requirement and Performance Incentive Scheme (PIS), as Exhibit "M".

Purpose of Exhibit "M" – *to show allegations in support of the relief asked for in this application, particularly the approval of Annual Revenue Requirement, Performance Incentive Scheme and Procedures to Convert the MAP to Rates*

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| Exhibit "N" | |
| A | Regulatory Asset Base |
| A1 | Summary of the optimized depreciated replacement cost (ODRC) and the depreciated historical cost of the Regulatory Asset Base as |

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| | <p>at the initial valuation date (the Regulatory Asset Base).</p> <p>A2 Summary of the optimized depreciated replacement cost and the depreciated historical cost of the Original Regulatory Asset Base as at the start of the Second Regulatory Period, with supporting calculations for indexing applied.</p> <p>A3 Assets forecast to be acquired during the period between the initial valuation date and the start of the Second Regulatory Period.</p> <p>A3.1 - Schedule of assets to be acquired</p> <p>A3.2 - Value of the assets to be acquired</p> <p>A3.3 - Justification for assets to be acquired</p> <p>A5 Forecast asset disposal during the period between the initial valuation date and the start of the Second Regulatory Period.</p> <p>A5.1 - Schedule of assets to be disposed of</p> <p>A5.2 - Value of the assets to be disposed of</p> <p>A5.3 - Forecast income from the sale of disposed assets</p> <p>A6 ODRC depreciation schedules for the Regulatory Asset Base for the period between the initial valuation date and the start of the Second Regulatory Period.</p> <p>A6.1 - Assets included in the Original Regulatory Asset Base</p> <p>A6.2 - Assets acquired in the lead-up to the Second Regulatory Period</p> <p>A7 Historical cost depreciation schedules for the Regulatory Asset Base for the period between the initial valuation date and the start of the Second Regulatory Period.</p> <p>A7.1 - Assets included in the Original Regulatory Asset Base</p> <p>A7.2 - Assets acquired in the lead-up to the Second Regulatory Period</p> <p>A8 Period</p> <p>A9 Application of the construction work in progress (CWIP) factor to the Regulatory Asset Base as at the start of the Second Regulatory Period.</p> <p>Summary of the optimized depreciated replacement cost (ODRC) and the depreciated historical cost of the full Regulatory Asset Base as at the start of the Second Regulatory Period (the opening value of the rolled-forward Regulatory Asset Base).</p> <p>Purpose: <i>To show and prove on applicant's proposed regulatory asset base as well as historical data</i></p> |
| | <p>Exhibit "O"</p> <p>B Financial indices forecast for Second Regulatory Period</p> <p>B1 Philippine quarterly CPI</p> <p>B2 United States quarterly CPI</p> <p>B3 PhP/US\$ quarterly exchange rate</p> |

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| B4 | 180-Day Manila Reference Rate Purpose: <i>To show and prove these financial indices needed for the forecast</i> |
| | Exhibit “P” C Forecast capital expenditure for the Second Regulatory Period C1 Summary of capital expenditure forecasts for each year of the Second Regulatory Period C1.1 - Real values, divided in PhP and US\$ components C1.2 - Nominal values, divided in PhP and US\$ components C1.3 - Total nominal values, in PhP C1.4 - Justification for capital expenditure (major and minor projects) C1.5 ERC Template on Capital Asset to be acquired for RY 2007-2011 a. Network – classified according to Renewal, Refurbishment and Load Growth b. Non-network – classified according to Renewal, Refurbishment and Load Growth C2 Broken down historical capital expenditure Purpose: <i>– to show and prove the proposed capital expenditures and its justification</i> |
| | Exhibit “Q” D Forecast disposals during the Second Regulatory Period D1 Value of assets to be disposed of (based on ODRC register) D2 Forecast income from the sale of disposed assets Purpose: <i>– to show and prove the forecasted values of the assets to be disposed and forecasted income from the sale</i> |
| | Exhibit “R” E Forecast depreciation during the Second Regulatory Period E1 Depreciation of the opening asset base E1.1 - ODRC basis E1.2 - Historical cost basis E2 Depreciation of the assets forecast to be acquired during the Second Regulatory Period E2.1 - ODRC basis E2.2 - Historical cost basis Purpose <i>– to show and prove forecasted depreciation including historical basis</i> |
| | Exhibit “S” |

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| <p>F</p> <p>F1</p> <p>F2</p> | <p>Forecast assets used beyond standard lives</p> <p>Forecast addition to assets used beyond standard lives</p> <p>Forecast removal from assets used beyond standard lives</p> <p>Purpose: – to show and prove forecast addition to assets beyond standard lives and forecast removal from assets used beyond standard lives</p> |
| <p>G</p> <p>G1</p> <p>G1.1</p> <p>G1.2</p> <p>G1.3</p> <p>G1.4</p> <p>G2</p> <p>G3</p> <p>G3.1</p> <p>G3.2</p> <p>G3.3</p> <p>G3.4</p> | <p>Exhibit “T”</p> <p>Forecast operating & maintenance expenditure</p> <p>Summary of forecast operating & maintenance expenditure</p> <ul style="list-style-type: none"> - Annual expenditure, divided in real PhP and US\$ components - Annual expenditure, divided in nominal PhP and US\$ components - Total annual expenditure, in nominal PhP - Justification for operating & maintenance expenditure forecasts <p>Historical operating & maintenance expenditure</p> <p>Summary of expenditure on taxes (other than corporate income tax), duties and levies</p> <ul style="list-style-type: none"> - Annual expenditure, in real PhP - Annual expenditure, in nominal PhP - Justification for expenditure - Historical taxes, levies & duties <p>Purpose – to show and prove the proposed Operating and Maintenance Expenditures, its necessity and that it is of reasonable magnitude</p> <ul style="list-style-type: none"> - to show historical data - to show and prove the proposed expenditures for taxes (other than income taxes), levies and duties, its justification and historical data |
| <p>H</p> <p>H1</p> <p>H1.1</p> <p>H1.2</p> <p>H2</p> <p>H2.1</p> <p>H2.2</p> | <p>Exhibit “U”</p> <p>Forecast energy consumption and demand</p> <p>Forecast energy consumption figures (kWh)</p> <ul style="list-style-type: none"> - Breakdown of consumption figures - Supporting evidence <p>Forecast energy demand figures (kW)</p> <ul style="list-style-type: none"> - Breakdown of demand figures - Supporting evidence - <p>Purpose – to show and prove forecasted energy consumption and demand</p> |

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| I | <p>Exhibit “V”</p> <p>Regulatory financial statements</p> <p>Purpose: – to show the projected financial statements such as balance sheet, income statement and cash flow statement based on general inputs and, assumptions</p> |
| <p>J</p> <p>J1</p> <p>J1.1</p> <p>J1.2</p> <p>J1.3</p> <p>J2</p> <p>J2.1</p> <p>J2.2</p> <p>J2.3</p> <p>J2.4</p> | <p>Exhibit ‘W’</p> <p>Performance incentive scheme details</p> <p>Price-linked incentive scheme</p> <ul style="list-style-type: none"> - Details of scheme proposed - Proposed target levels - Supporting information & calculations <p>Guaranteed service level scheme</p> <ul style="list-style-type: none"> - Details of scheme proposed - Proposed target levels - Proposed penalty levels - Supporting information & calculations <p>Purpose: – to show and prove the proposed Performance Incentive, the proposed target levels, penalty levels and calculations</p> |
| K | <p>Exhibit “X”</p> <p>Calculation of Weighted Average Cost of Capital</p> <p>Purpose: – to show the financial indices, other data and formula needed for the calculation of the proposed WACC</p> |
| <p>L</p> <p>L1</p> <p>L2</p> <p>L3</p> <p>L4</p> <p>L5</p> | <p>Exhibit “Y”</p> <p>Additional information for price-cap model</p> <p>Contact details for input sheets</p> <p>2006 Billing & consumption data</p> <p>Related business revenue for 2006</p> <p>Maximum annual price for 2006 and 2007 (initial entrants)</p> <p>Tax losses carried forward from 2007 regulatory year</p> <p>Purpose: – to show and prove additional information for the price-cap model</p> |
| M | <p>Exhibit “Z”</p> <p>Detailed calculations for Second Regulatory Period</p> <p>Rolled forward regulatory asset base</p> |

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| | <p>Annual revenue requirement</p> <p>Corporate income tax forecasts</p> <p>Forecast price-caps for the opening and subsequent years of the Second Regulatory Period</p> <p>Purpose: – to show and prove detailed calculations on rolled-forward RAB, ARR, income tax forecast and forecast price-caps of the Second Regulatory Period</p> |
| N | <p>Exhibit “AA”</p> <p>Calculation of demonstrative unbundled rates</p> <p>Purpose: – to show and prove the calculation of demonstrative unbundled rates</p> |
| | <p style="text-align: center;">Exhibit “BB”</p> <p>O Proposed Procedure and Design to Convert MAP into rates of Individual customers</p> <p>Purpose: to show, prove and justify these proposed procedures</p> <p style="text-align: center;">Exhibit “CC”</p> <p>P Computation of the Proposed Working Capital for Purchased Power</p> <p>Purpose: to show the computation of the proposed working Capital for purchase power</p> |

20. Affidavit of Chiquita N. Capili – as Exhibit “DD”..
21. Affidavit of David A. Tauli – as Exhibit “EE”.
22. Affidavit of Richard S. Ratunil – as Exhibit “FF”
23. Affidavit of Pacita Ch. D. Gabriel – as Exhibit “GG”
24. Affidavit of Atty. Jose Edgardo Y. Uy – as Exhibit “HH”
25. Affidavit of Wilma C. Cagas – as Exhibit “II”
26. Affidavit of Carlito L. Hembrador – Exhibit “JJ”
27. Affidavit of ERC personnel to testify on the valuation – as Exhibit “KK”

Since the documents from Exhibit “M” up to Exhibit “KK” contain several pages each, it is proposed that from the second page up to last page, each page will just be submarked, thus the second page of Exh. “M” which is the Application will be Exh. “M-1”, the third as “Exh. “M-2” and so on, up to Exh. “KK”.

WITNESSES

Applicant will present the following witnesses:

1. CHIQUITA C. CAPILI, Vice President and Controller

- a) *To testify on the allegations contained in the Application, and that she headed the preparation of the application and the supporting documents;*
- b) *To testify on proposed Annual Revenue Requirement and the five building blocks, the resulting Maximum Annual Price;*
- c) *to testify on the proposed Performance Incentive Scheme ;*
- d) *to testify that the Annual Revenue Requirement, the proposed Performance Incentive Scheme are in accordance with the RDWR*

2. DAVID A. TAULI, Senior Vice President and Head, Engineering Services

Division of CEPALCO, who is a responsible and authorized person:

- a) *To testify on the proposed Capital Expenditures, and on the justification why the projects included in the Capital Expenditure have to be implemented to enable CEPALCO to fulfill its obligations as an electric utility under the PBR regime in an efficient, reliable and economical manner;*
- b). *to testify on proposed Operating and Maintenance Expenditures and on the justification that the proposed Operating and Maintenance Expenditures are necessary to enable CEPALCO to fulfill its obligations as an electric utility under the PBR regime in an efficient, reliable and economical manner;*
- c). *to testify and justify the proposed Performance Incentive Scheme, particularly on the details on how it will carried out.*

3. JOSE EDGARDO Y. UY, Vice President and Head, Administrative Services Division

- a).*To testify on the proposed new and bigger main headquarters for CEPALCO and its justification.*
- b).*to testify that the cost of this project as estimated and based on CEPALCO’s office space requirements is reasonable.*

4. PACITA CH. D. GABRIEL, Manager and Head, Accounting Department

- a).*To testify on forecasted Taxes , Levies and Duties, the amount of Regulatory Depreciation, Corporate Income Tax, which are three of the five building blocks of the ARR, and the Regulatory Asset Base*

b). To testify that the proposed ARR and the resulting MAP will result to rates that would still enable CEPALCO to provide reasonable return for its investors

5. RICHARD S. RATUNIL, Supervisor

a). To testify on the proposed Procedures to Convert the Maximum Average Price and its justification and that these procedures are in accordance with the RDWR

6. MA. WILMA C. CAGAS, Supervisor

a). To testify on how the threshold levels for proposed GSL 3 are derived.

7. CARLITO L. HEMBRADOR, JR., Supervisor

a) To testify on how the threshold levels for proposed GSL 4 are derived.)

Applicant reserves to present other witnesses as may be necessary.

Respectfully submitted.

Pasig City, Philippines, September 21, 2006.


JOSE EDGARDO Y. UY

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