

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

IN THE MATTER OF THE APPLICATION FOR APPROVAL OF 1) THE ANNUAL REVENUE REQUIREMENT 2) PERFORMANCE INCENTIVE SCHEME AND 3) PROCEDURE TO CONVERT THE MAXIMUM AVERAGE PRICE INTO RATES, ALL IN ACCORDANCE WITH THE PROVISIONS OF THE RULES FOR SETTING DISTRIBUTION WHEELING RATES,

ERC CASE NO. 2006-____RC

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

Applicant,

APPLICATION

COMES NOW, applicant CAGAYAN ELECTRIC POWER AND LIGHT CO., INC. (also referred as "CEPALCO" for brevity), through the undersigned counsel, and unto this Honorable Commission, most respectfully states:

1. That applicant is a corporation duly organized and existing under and by virtue of the laws of the Philippines, with principal office at 44 Toribio Chaves Street, Cagayan de Oro City, where it may be served with summons and other legal processes, represented in this instance by its President and Chief Operating Officer, MRS. CONSUELO G. TION, of legal age, Filipino, married and with office address also at 44 Toribio Chaves Street, Cagayan de Oro City. Herein applicant is the exclusive franchise holder issued by Congress of the Philippines 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. That applicant has selected to enter Performance-Based Regulation at the first entry point, as described in Annex B of ERC Resolution No. 12-02 Series of 2004 "Adopting a Methodology for Setting Distribution Wheeling Rates", dated December 10, 2004 and that such selection has been approved by the Energy Regulatory Commission (ERC). The

application submitted to the ERC is for the approval of the Annual Revenue Requirement and Performance Incentive Scheme required for the Second Regulatory Period described in the Guidelines on the Methodology for setting Distribution Wheeling Rates (DWRG) issued by the ERC on December 10, 2004 and as subsequently amended in the Rules for Setting Distribution Wheeling Rates (RDWR) issued by the ERC on *August 4, 2006*. This Second Regulatory Period commences on July 1, 2007 and terminates in June 30, 2011.

- 2a. That applicant proposes the Annual Revenue Requirement and Performance Incentive Scheme values thus approved to form the basis of the ERC's determination of the X-factor, P₀-factor and the Maximum Annual Prices that will apply to the applicant and on which it will base its rate setting for the Second Regulatory Period.
3. That applicant has prepared its proposal as contained in this application in accordance with the conditions described in the afore-mentioned RDWR and in the implementing guidelines issued by the ERC in its Position Paper on the Regulatory Reset for the Second Regulatory Period, dated December 9, 2005 (Position Paper). The application submitted to the ERC made use of the methodology described in the RDWR, the Position Paper and applied the financial spreadsheet model titled ERC-MODEL-FINAL-V3.3.xls (Price-Cap Model) that was provided to the applicant by the ERC.
4. That the proposed Annual Revenue Requirement is based on the Building Block calculation described in the afore-mentioned RDWR, as set out below for each Regulatory Year and for which the applicant is seeking the immediate approval of the ERC:

Table 1. Annual Revenue Requirement as per Building Block approach

Building Block	Proposed revenue requirement per Regulatory Year (PhP)			
	2008	2009	2010	2011
Operating and maintenance expenditure	311,885,289	339,327,473	358,392,237	381,061,615
Taxes, levies & duties (other than corporate tax)	37,740,761	37,363,465	44,873,908	47,215,838
Regulatory depreciation	128,919,618	151,005,051	165,860,505	177,525,945
Return on capital	460,681,451	507,114,823	546,432,958	577,735,642
Corporate income tax	93,042,274	82,622,727	77,759,407	84,579,321
TOTAL REVENUE REQUIREMENT	1,032,269,393	1,117,433,539	1,193,319,015	1,268,118,361

Note: All values are in nominal terms

The meaning and application of these parameters are as described in the aforementioned RDWR.

- That the afore-mentioned Annual Revenue Requirement is based on a proposed rolled-forward value of the applicant's Regulatory Asset Base as described below. The opening value of the Regulatory Asset Base for 2008 is based on the value of the Regulatory Asset Based on June 30, 2006, as valued by the ERC and communicated to the applicant, suitably amended to a June 30 2007 value in accordance with the method described in the RDWR.

Table 2. Summary of proposed Rolled-forward Regulatory Asset Base (RAB)

Item	PhP for Regulatory Year			
	2008	2009	2010	2011
Opening Value of RAB	2,475,465,434	2,759,614,622	3,008,676,991	3,228,351,733
plus Capital Expenditure	413,068,806	400,067,421	385,535,247	315,527,297
Minus Regulatory Depreciation on Asset Base at Start of Second Regulatory Period	116,863,723	116,863,723	114,722,503	113,114,305
Minus Regulatory Depreciation on Capital Expenditure incurred during the Second Regulatory Period	12,055,895	34,141,328	51,138,002	64,411,640
Closing Value of RAB	2,759,614,622	3,008,676,992	3,228,351,733	3,366,353,085
AVERAGE VALUE OF RAB	2,617,540,028	2,884,145,807	3,118,514,362	3,297,352,409

Note: All values are in nominal terms

6. That allowance has been made in accordance with the RDWR to include assets used beyond their standard lives in the Regulatory Asset Base, at a value equal to 5% of their optimized replacement cost.
7. That for the calculation of the above-mentioned Annual Revenue Requirement and Rolled-forward Regulatory Asset Base, as instructed by the ERC, applicant has applied the preliminary values for the parameters presented below:

Table 3. Input values provided by the ERC

Parameter	Date instructed by ERC	Preliminary value adopted
Construction work in progress factor (CWIP factor)		For substation projects : 4.5% For other projects : 3.2%
P ₀ -factor		0 PhP/kWh
X-factor		0
Valuation of the applicant's regulatory asset base as at June 30, 2006		PhP 1,945,938,961
Working-capital proportion		For Distribution : 1/6 of Total Distribution O&M Expenses For Purchased Power : 8/360 of Total Estimated Purchased Power Expenses

The meaning and application of these parameters are as described in the aforementioned RDWR. Further, CEPALCO proposes to include an additional Working Capital to cover the cost of power purchased from its suppliers. The said additional Working Capital is equivalent to the estimated cost of purchased power for 8 days based on a lead-lag study presented in Schedule P.

8. That in calculating the afore-mentioned Annual Revenue Requirement for the Second Regulatory Period, the applicant made use of the estimated Philippine Consumer Price Index, United States of America Consumer Price Index and Philippine Peso/United States dollar exchange rate figures below:

Table 3a. Forecast Consumer Price Index for the Philippines

Quarter Ending	2006	2007	2008	2009	2010	2011
31-Mar	136.70	144.55	151.20	157.10	163.85	170.90
30-Jun	138.10	146.88	153.63	159.63	166.49	173.65
30-Sep	142.15	148.85	155.70	161.77	168.72	
31-Dec	143.65	150.57	157.49	163.63	170.67	
Base index : 100				Base index year :		2000
Data source	Derived from ERC's Final Determination for Transco (Please see Schedule B.1.1 for details)					

Table 3b. Forecast Consumer Price Index for the United States of America

Quarter ending	2006	2007	2008	2009	2010	2011
31-Mar	199.80	207.01	212.59	218.33	224.23	230.28
30-Jun	202.90	208.14	213.76	219.53	225.45	231.54
30-Sep	206.79	210.08	215.75	221.58	227.56	
31-Dec	204.71	209.37	215.03	220.83	226.79	
Base index : 100				Base index year :		1982-84
Data source	Derived from ERC's Final Determination for Transco (Please see Schedule B.2.1 for details)					

Table 3c. Forecast PhP/US\$ Exchange Rate

Quarter ending	2006	2007	2008	2009	2010	2011
31-Mar	51.219	52.451	52.153	52.153	52.650	52.650
30-Jun	53.157	52.715	52.416	52.416	52.915	52.915
30-Sep	52.135	53.378	53.075	53.075	53.581	
31-Dec	51.747	52.982	52.681	52.681	53.182	
Data source	Derived from ERC's Final Determination for Transco (Please see Schedule B.3.1 for details)					

- 8a. That for the purposes of the initial and subsequent annual price resets during the Second Regulatory Period as required in terms of the RDWR, the applicant will update the aforementioned Consumer Price Indices and foreign exchange rates with actual values in accordance with the RDWR and that such updated values will be used for the price resets.
9. That the afore-mentioned Annual Revenue Requirement is in part based on a proposed rate of return of 16.85% per annum. This rate of return corresponds with the Regulatory Weighted Average Cost of Capital which the applicant calculated in accordance with the

RDWR. The applicant recognizes that the ERC will determine the actual Weighted Average Cost of Capital that will apply for its setting of the Maximum Annual Prices for the Second Regulatory Period and that this may differ from that proposed.

10. That the proposed Capital Expenditure included in the afore-mentioned calculation of the Rolled-forward Regulatory Asset Base is as demonstrated below:

Table 4. Summary of Proposed Capital Expenditure (per regulatory year)

ITEM	NOMINAL PESO				
	2007	2008	2009	2010	2011
A. Distribution Plant					
Land and Land Rights (Distribution Purpose)	2,403,675	-	2,626,425	-	-
Structures and Improvements (Distribution Purpose)	4,109,750	4,079,067	4,724,063	-	-
Station Equipment					
- Power transformers	105,936,737	2,415,023	26,755,080	-	-
- Switchgear	24,977,341	23,427,848	11,987,795	-	656,632
- Protective equipment	8,647,208	10,865,102	6,906,788	-	-
- Metering & control equipment	983,922	1,677,226	1,028,674	-	-
- Communications equipment	31,199,500	62,213,348	10,197,138	4,835,780	-
- Other station equipment	7,343,961	3,079,903	2,008,339	42,835	-
Poles, Towers and Fixtures – Distribution	89,908,377	65,710,592	58,793,077	50,386,786	52,626,546
Poles, Towers and Fixtures – Customer	-	-	-	-	-
Overhead Conductors and Devices – Distribution	59,304,758	50,649,814	45,401,161	43,543,235	40,931,734
Overhead Conductors and Devices – Customer	-	-	-	-	-
Underground Conduits – Distribution	-	-	-	-	-
Underground Conduits – Customer	-	-	-	-	-
Underground Conductors and Devices – Distribution	-	-	-	-	-
Underground Conductors and Devices – Customer	-	-	-	-	-
Line Transformers - Distribution	13,604,698	20,058,143	20,910,842	21,768,916	22,705,811
Line Transformers – Customer	-	-	-	-	-
Power Conditioning Equipment	2,889,554	29,976,392	23,754,401	8,626,067	-
Services	4,896,787	5,627,934	6,129,099	6,677,638	7,273,560
Meters, Instruments & Metering Transformers-distribution	26,659,685	52,162,315	35,469,309	37,217,620	39,641,881
Meters, Instruments & Metering Transformers – customer	-	-	-	-	-
Information technology equipment (distribution)	-	-	-	-	-
Regulated Entity Property on Consumers' Premises	-	-	-	-	-
Street Lights and Signal Systems	136,850	286,870	299,065	311,337	324,736
Submarine Cables	-	-	-	-	-
B. General Plant					
Land and Land Rights (non-network)	-	-	-	-	-

ITEM	NOMINAL PESO				
	2007	2008	2009	2010	2011
Structures and Improvements (non-network)	4,109,750	1,777,244	58,787,563	182,960,512	101,894,769
Office Furniture and Equipment	18,561,435	16,569,657	16,156,541	6,770,007	23,262,142
Transportation Equipment	19,088,919	27,039,299	34,998,164	4,858,613	6,513,429
Stores Equipment	-	-	-	-	-
Tools, Shop and Garage Equipment	10,777,008	5,613,006	6,883,308	1,483,789	865,823
Laboratory Equipment	-	1,349,239	-	334,180	-
Information systems equipment (non-network)	12,080,833	16,250,634	20,609,702	9,221,899	10,463,885
Power-operated Equipment	-	-	-	-	-
Communication Plant and Equipment	3,673,884	2,286,987	479,760	132,457	869,505
Miscellaneous Equipment	1,443,365	6,601,564	476,725	337,978	6,845
C. Materials and Supplies (including spares)	-	3,351,600	4,684,400	6,025,600	7,490,000
D. Transferred subtransmission assets	-	-	-	-	-
E. Allocated Overheads Capitalized	-	-	-	-	-
TOTAL	452,737,997	413,068,806	400,067,421	385,535,247	315,527,297

10. That the above-mentioned proposed Capital Expenditure for the years 2007 – 2011 post an annual average nominal values of P393 million or 78% higher than the capital expenditures for 2005. Of which, P54 million or equivalent to 24% increment over 2005 capital expenditure level is due to inflation which is projected to hit an average of 4.5% per annum.

Capital expenditures for Distribution Plant facilities post an annual average real values of P232 million. These investments are necessary to upgrade system capacity to serve load growth that shall propel the socio-economic development within the franchise area; renew or refurbish the existing distribution system in order to maintain and improve system reliability and service quality, meet performance targets; and implement programs and projects to ensure compliance with the Philippine Grid and Distribution Codes and other regulatory requirements.

Investment for non-network facilities hits an annual average real values of P107 million. This is needed to provide the basic support facilities, systems, and personnel in order to carry the company's obligations to provide better service and satisfy the requirements of existing and future customers.

11. That the proposed Operating & Maintenance Expenditure included in the aforementioned calculation of the Annual Revenue Requirement is as demonstrated below:

Table 5. Summary of proposed Operating & Maintenance Expenditure (per regulatory year)

OPEX Category & Sub-Category	Nominal, PhP				
	2007	2008	2009	2010	2011
Distribution: Operation					
Operation supervision & engineering	4,896,929	5,612,897	5,947,993	6,283,550	6,553,474
Load dispatching	1,547,790	2,102,762	2,158,209	2,124,428	2,232,124
Substation	1,638,836	2,226,454	2,285,163	2,249,395	2,363,426
Overhead line - demand	-	-	-	-	-
Overhead line - customer	2,317,829	3,183,704	3,333,507	3,343,385	3,467,686
Streetlighting (non-roadway)	182,093	247,384	253,907	249,933	262,603
Streetlighting (roadway)	10,616	14,145	15,307	16,222	17,007
Metering	3,941,719	4,141,975	4,481,562	4,789,896	5,155,638
Consumer installation expenses	7,418,416	8,793,714	9,417,142	9,873,574	10,585,301
Rents	-	-	-	-	-
Information technology	1,251,822	1,930,437	2,397,385	2,688,567	2,987,695
Miscellaneous	1,310,507	1,782,806	1,845,302	1,834,144	1,919,304
Distribution: Maintenance					
Maintenance supervision & engineering	4,654,982	5,824,684	6,155,566	6,439,989	6,696,957
Structures	2,777,687	3,839,438	4,096,088	4,181,895	4,292,256
Substations	441,680	598,715	626,475	630,086	656,435
Overhead line - demand	-	-	-	-	-
Overhead line - customer	5,006,394	6,886,436	7,416,133	7,629,585	7,803,858
Streetlighting (non-roadway)	-	-	-	-	-
Streetlighting (roadway)	729,176	829,190	903,216	954,710	1,025,797
Line transformers	2,942,420	4,017,716	4,267,473	4,434,434	4,631,082
Information technology	674,058	1,039,466	1,290,900	1,447,690	1,608,759
Metering	1,675,159	5,115,040	5,671,550	6,196,305	6,740,695
Miscellaneous	-	-	-	-	-
Sub-total Distribution	43,418,113	58,186,963	62,562,878	65,367,788	69,000,097
Consumer Accounts					
Supervision	4,293,802	5,133,352	5,453,461	5,758,157	6,095,140
Meter reading	3,968,441	4,308,453	4,706,627	5,029,051	5,339,096
Information technology	2,303,080	3,963,973	3,679,638	3,942,313	3,252,609
Consumer records & collection	20,721,758	24,402,557	26,559,204	28,636,216	30,789,667
Uncollectible accounts	7,180,958	7,526,461	7,846,421	8,168,398	8,519,951
Informational and instructional advertising	4,768,598	6,087,494	6,834,202	7,513,228	8,592,014
Miscellaneous	-	-	-	-	-
Consumer prompt payment discount	-	-	-	-	-
Sub-total Consumer accounts expenses	43,236,637	51,422,290	55,079,553	59,047,363	62,588,477
Admin and General					
Admin & general salaries	35,115,045	44,858,447	48,857,618	52,798,461	57,396,360
Office supplies & expenses	18,630,088	19,584,529	20,194,861	19,514,003	17,318,682
Information technology	1,809,562	3,114,550	2,891,144	3,097,532	2,555,621
Outside services employed	11,235,707	15,897,225	17,046,436	20,040,424	20,765,026
Property insurance	1,896,900	2,556,032	2,934,766	3,398,996	3,681,750
Injuries & damages	801	-	-	-	-
Employee pension & benefits	57,241,462	80,255,456	90,107,640	91,883,363	101,192,894

OPEX Category & Sub-Category	Nominal, PHP				
	2007	2008	2009	2010	2011
Rents	1,133,996	2,589,544	2,740,920	2,886,772	3,047,085
Maintenance of office & general plant	1,487,009	1,268,326	1,564,046	2,192,655	2,800,307
Officers allowance & benefits	7,245,500	8,855,707	10,045,784	10,583,177	11,252,865
Travel	3,176,662	5,317,194	5,613,659	5,924,151	6,271,212
Training	2,678,215	2,095,100	2,162,667	2,492,963	2,825,036
Bad debt	-	-	-	-	-
Regulatory liaison & compliance	5,631,677	6,410,370	7,351,172	8,418,109	8,780,409
Foreign exchange losses or gains	-	-	-	-	-
Other	7,889,341	9,473,558	10,174,330	10,746,479	11,585,793
Sub-total Administration & general	155,171,965	202,276,038	221,685,043	233,977,085	249,473,040
WESM Compliance					
Registration fees	-	-	-	-	-
Metering fees	-	-	-	-	-
Billing & settlement fees	-	-	-	-	-
Administration fees	-	-	-	-	-
PEM board, committees & working groups	-	-	-	-	-
Market management software & upgrades	-	-	-	-	-
Provision of security	-	-	-	-	-
Other	-	-	-	-	-
Sub-total WESM compliance	-	-	-	-	-
Total Operating and Maintenance Expenditure	241,826,715	311,885,289	339,327,473	358,392,237	381,061,615

- 11a. That the above-mentioned proposed Operating and Maintenance expenditure are increased from current levels by an annual average of P37 million or at an average rate of **15%** per annum. Of which, P16 million or 5% annual increase is due to projected inflation during the period, and the P21 million or 9% annual increase is mainly needed to carry the company's obligation to serve load growth, to maintain the existing facilities/system and personnel resources in order to maintain or improve service reliability, meet system and service performance targets, and ensure compliance with the regulatory requirements
12. That the proposed expenditure on Taxes, Levies & Duties (other than corporate income tax) included in the afore-mentioned calculation of the Annual Revenue Requirement is as demonstrated below:

Table 6. Summary of proposed Taxes, Levies & Duties (other than corporate income tax) expenditure (per Regulatory Year)

	Nominal PhP				
	2007	2008	2009	2010	2011
Taxes, levies & duties (nominal PhP)	31,260,381	37,740,761	37,363,465	44,873,908	47,215,838

12a. That the above-mentioned proposed taxes, levies & duties (other than corporate income taxes) expenditure are increased from current levels by an annual average of P5 million or at an average rate of 16% per annum. Of which, P2 million or 5% annual increase is due to projected inflation during the period, and the P3 million or 11% annual increase is mainly due to Local Franchise Tax brought about by the increase in revenue due to load growth and projected increase in rates.

12b. That the taxes, levies and duties (other than corporate income tax) figure include provision for increased regulatory compliance costs associated with the Regulatory Reset for the Second Regulatory Period.

13. That the proposed Depreciation included in the afore-mentioned calculation of the Annual Revenue Requirement, including an allowance for assets intended to be disposed of during the Second Regulatory Period after allowing for any potential income from the sales of such disposed assets, is as demonstrated below. These values include depreciation on the applicant's Regulatory Asset Base as at the start of the Second Regulatory Period, as well as depreciation on those assets proposed to be acquired during the Second Regulatory Period.

Table 7. Summary of proposed Depreciation (per Regulatory Year)

ITEM	2007	2008	2009	2010	2011
A. Distribution Plant					
Land and Land Rights (Distribution Purpose)	-	-	-	-	-
Structures and Improvements	700,532	850,596	960,635	1,019,686	1,019,686
Station Equipment	-	-	-	-	-
Power Transformers	4,394,812	6,539,466	7,025,634	7,471,552	7,471,552
Switchgear	3,933,043	5,018,046	5,608,307	5,808,104	5,819,048
Protective equipment	1,541,877	1,975,742	2,271,941	2,387,054	2,387,054
Metering & control equipment	32,924	79,884	124,983	142,127	142,127
Communications equipment	1,769,684	6,595,112	10,215,637	10,967,283	11,209,072
Other station equipment	218,698	410,031	494,835	529,021	529,735

ITEM	2007	2008	2009	2010	2011
Poles, Towers and Fixtures - Distribution	22,531,439	26,806,146	28,881,208	30,700,872	32,417,761
Poles, Towers and Fixtures - Customer	-	-	-	-	-
Overhead Conductors and Devices - Distribution	18,562,432	21,762,605	23,363,454	24,845,861	26,253,777
Overhead Conductors and Devices - Customer	-	-	-	-	-
Underground Conduits - Distribution	-	-	-	-	-
Underground Conduits - Customer	-	-	-	-	-
Underground Circuits - Distribution	-	-	-	-	-
Underground Circuits - Customer	-	-	-	-	-
Line Transformers - Distribution	8,642,223	9,823,314	10,506,130	11,217,460	11,958,705
Line Transformers - Customer	-	-	-	-	-
Power Conditioning Equipment	136,446	693,338	1,588,852	2,128,526	2,272,294
Services	2,257,502	2,591,816	2,787,767	3,001,213	3,233,733
Meters, Instruments & Metering Transformers-distribution	15,184,949	17,927,454	19,680,087	21,133,825	22,671,015
Meters, Instruments & Metering Transformers - customer	-	-	-	-	-
Information technology equipment (distribution)	-	-	-	-	-
Regulated Entity Property on Consumers' Premises	-	-	-	-	-
Street Lights and Signal Systems	202,591	223,555	233,320	243,494	254,095
Submarine Cables	-	-	-	-	-
B. General Plant	-	-	-	-	-
Land and Land Rights (non-network)	-	-	-	-	-
Structures and Improvements (non-network)	1,084,703	1,235,159	1,992,219	5,014,070	8,574,761
Office Furniture and Equipment	3,758,320	4,884,646	5,702,800	6,275,964	7,026,768
Transportation Equipment	3,209,292	7,090,941	10,808,010	13,104,711	13,871,227
Stores Equipment	-	-	-	-	-
Tools, Shop and Garage Equipment	1,821,438	2,490,171	2,802,579	3,011,757	3,070,497
Laboratory Equipment	1,128,285	1,243,019	1,276,750	1,285,104	1,293,459
Information systems equipment (non-network)	4,659,062	7,732,989	11,419,022	12,260,962	12,679,002
Power-operated Equipment	-	-	-	-	-

ITEM	2007	2008	2009	2010	2011
Communication Plant and Equipment	1,922,993	2,349,776	2,488,114	2,518,725	2,568,823
Miscellaneous Equipment	362,287	595,811	772,768	793,136	801,757
C. Materials and Supplies (including spares)	-	-	-	-	-
D. Transferred subtransmission assets	-	-	-	-	-
E. Capitalized Overheads	-	-	-	-	-
TOTAL	98,055,534	128,919,618	151,005,051	165,860,505	177,525,945

13a. That the afore-mentioned depreciation is calculated on a straight-line basis, based on the standard asset lives approved by the ERC.

14. That the proposed Corporate Income Tax included in the afore-mentioned calculation of the Annual Revenue Requirement is based on a Philippines corporate tax rate of 35% and is calculated as demonstrated below:

Table 8. Summary of proposed Corporate Income Tax (per Regulatory Year)

	2008	2009	2010	2011
Corporate Tax (nominal PhP)	93,042,274	82,622,727	77,759,407	84,579,321

15. That the calculation of the afore-going proposed Corporate Income Tax is based on the forecast sales of energy as demonstrated below:

Table 9. Summary of forecast energy consumption (per Regulatory Year)

	2007	2008	2009	2010	2011
Energy Consumption (MWh), including company use	710,961	730,858	750,726	782,355	804,348

16. That the calculation of the afore-mentioned Corporate Income Tax is based on an estimated price-path for the Second Regulatory Period that was determined using the afore-mentioned proposed Allowed Annual Revenue and an assumed zero X-factor and P₀-factor. The estimated Maximum Annual Prices thus calculated for the Second Regulatory Period is as demonstrated below:

Table 10. Assumed Maximum Annual Prices for the Second Regulatory Period

	2008 Regulatory Year	2009 Regulatory Year	2010 Regulatory Year	2011 Regulatory Year
Maximum Annual Price (PhP/kWh)	1.1398	1.1979	1.2509	1.3010

16a. That the applicant recognizes that the ERC will determine the actual X-factor and P₀-factor after its consideration of this application for Allowed Annual Revenue and will determine the actual price-path for the Second Regulatory Period after incorporating such amendments to these proposals as the ERC deems necessary. As part of its consideration the ERC may also amend one or more of the parameters on which the calculations of the Allowed Annual Revenue are based. The actual approved price path is therefore likely to differ from that estimated above.

17. That, since the Maximum Average Prices calculated under Performance-Based Regulation are not directly comparable with unbundled rates, for illustrative purposes the applicant has prepared a comparison of its current rates for providing distribution wheeling services with those that would result from the implementation of the aforementioned estimated Maximum Annual Prices. This is presented below:

Table 11. Comparison of estimated rates with current rates (illustrative only)

	Current Rates	Illustrative Rates (2008)	Illustrative Rates (2009)	Illustrative Rates (2010)	Illustrative Rates (2011)
Customer Class					
Residential					
Distribution (PhP/kWh)	0.9167	1.1436	1.1778	1.2228	1.2474
Supply (PhP/kWh)	0.5771	0.7199	0.7415	0.7698	0.7853
Metering (PhP/kWh)	0.2670	0.3331	0.3431	0.3561	0.3633
Metering (PhP/customer/month)	5.00	6.24	6.43	6.68	6.81
Inter-class cross-subsidy (PhP/kWh)	(0.2650)	-	-	-	-
Total PhP/kWh	1.7608	2.1966	2.2624	2.3487	2.3960
Total PhP/customer/month	5.00	6.24	6.43	6.68	6.81
Average PhP/kWh distribution wheeling rate	1.5284	2.2373	2.3043	2.3922	2.4403
Small Commercial					
Distribution (PhP/kWh)	0.6991	0.8823	0.9119	0.9498	0.9721
Supply (PhP/kWh)	0.2954	0.3728	0.3853	0.4013	0.4107
Metering (PhP/customer/month)	210.21	262.32	270.19	280.52	286.18
Inter-class cross-subsidy (PhP/kWh)	(0.1960)	-	-	-	-
Total PhP/kWh	0.9945	1.2551	1.2971	1.3512	1.3828
Total PhP/customer/month	210.21	262.32	270.19	280.52	286.18
Average PhP/kWh distribution wheeling rate	1.3568	1.9596	2.0253	2.1097	2.1591

	Current Rates	Illustrative Rates (2008)	Illustrative Rates (2009)	Illustrative Rates (2010)	Illustrative Rates (2011)
Customer Class					
Big Commercial					
Distribution (PhP/kWh)	0.6069	0.6969	0.6979	0.7041	0.6980
Supply (PhP/kWh)	0.0451	0.0518	0.0519	0.0523	0.0519
Metering (PhP/customer/month)	210.21	238.78	238.36	239.82	237.09
Inter-class cross-subsidy (PhP/kWh)	0.0808	-	-	-	-
Total PhP/kWh	0.6520	0.7487	0.7497	0.7565	0.7499
Total PhP/customer/month	210.21	238.78	238.36	239.82	237.09
Average PhP/kWh distribution wheeling rate	0.8242	0.8537	0.8548	0.8625	0.8550
Small Industrial					
Distribution (PhP/kWh)					
Distribution demand charge (PhP/kW)	206.01	415.87	445.23	480.48	509.56
Supply (PhP/customer/month)	126.40	176.80	189.20	204.09	216.35
Metering (PhP/customer/month)	619.39	866.37	927.10	1,000.10	1,060.17
Inter-class cross-subsidy (PhP/kWh)	0.1623	-	-	-	-
Total PhP/kWh					
Total PhP/kW	206.01	415.87	445.23	480.48	509.56
Total PhP/customer/month	745.79	1,043.17	1,116.30	1,204.19	1,276.52
Average PhP/kWh distribution wheeling rate	1.0208	1.2025	1.2873	1.3892	1.4733
Big Industrial					
Distribution (PhP/kWh)					
Distribution demand charge (PhP/kW)	206.01	255.74	260.44	267.34	269.64
Supply (PhP/customer/month)	126.40	181.57	195.99	213.26	228.01
Metering (PhP/customer/month)	619.39	889.72	960.41	1,045.01	1,117.30
Inter-class cross-subsidy (PhP/kWh)	0.1623	-	-	-	-
Total PhP/kWh					
Total PhP/kW	206.01	255.74	260.45	267.34	269.64
Total PhP/customer/month	745.79	1,071.28	1,156.41	1,258.27	1,345.31
Average PhP/kWh distribution wheeling rate	0.7463	0.7249	0.7383	0.7578	0.7644
Bulk 69-kV Power					
Distribution (PhP/kWh)					
Distribution demand charge (PhP/kW)	127.55	189.74	204.81	210.57	225.14
Supply (PhP/customer/month)	126.40	181.57	195.99	195.49	209.01
Metering (PhP/customer/month)	619.39	889.72	960.41	957.93	1,024.20
Inter-class cross-subsidy (PhP/kWh)	0.1144	-	-	-	-
Total PhP/kWh					
Total PhP/kW	127.55	189.74	204.81	210.57	225.14
Total PhP/customer/month	745.79	1,071.28	1,156.41	1,153.41	1,233.20
Average PhP/kWh distribution wheeling rate	0.4064	0.3312	0.3575	0.3675	0.3930

	Current Rates	Illustrative Rates (2008)	Illustrative Rates (2009)	Illustrative Rates (2010)	Illustrative Rates (2011)
Customer Class					
Bulk 138-kV Power					
Distribution (PhP/kWh)					
Distribution demand charge (PhP/kW)	127.55	81.65	87.19	93.86	99.30
Supply (PhP/customer/month)	126.40	181.57	195.99	213.26	228.01
Metering (PhP/customer/month)	619.39	889.72	960.41	1,045.01	1,117.30
Inter-class cross-subsidy (PhP/kWh)	-	-	-	-	-
Total PhP/kWh					
Total PhP/kW	127.55	81.65	87.19	93.86	99.30
Total PhP/customer/month	745.79	1,071.28	1,156.41	1,258.27	1,345.31
Average PhP/kWh distribution wheeling rate	0.1823	0.1167	0.1246	0.1341	0.1419
Streetlights					
Distribution (PhP/kWh)	0.7765	1.0029	1.0473	1.1037	1.1440
Supply (PhP/customer/month)	0.0055	0.0071	0.0074	0.0078	0.0081
Metering (PhP/customer/month)	-	-	-	-	-
Inter-class cross-subsidy (PhP/kWh)	0.0504	-	-	-	-
Total PhP/kWh	0.7820	1.0100	1.0548	1.1115	1.1521
Total PhP/customer/month	-	-	-	-	-
Average PhP/kWh distribution wheeling rate	0.8324	1.0100	1.0548	1.1115	1.1521

18. That the applicant proposes to adopt a Price-Linked Performance Incentive Scheme as required in terms of the RDWR. According to this Performance Incentive Scheme the applicant will be rewarded if the service performance levels of its electricity distribution business exceed the target levels proposed below, and will be penalized if the service performance level of its electricity distribution business falls below the proposed targets. This reward or penalty will be directly incorporated into the Maximum Annual Prices from the second year of the Second Regulatory Period onward. The proposed Price-linked Performance Incentive Scheme is based on the performance measures and performance targets demonstrated below. Stepped performance target levels are proposed, which will influence the size of the reward or penalty.

Table 12. Summary of proposed Price-linked Performance Incentive Scheme

Performance index	Units	Weight	Reward		Target	Penalty	
			Level 5	Level 4	Level 3	Level 2	Level 1
System average interruption frequency index (SAIFI)	Number	0.20	19.62	22.20	27.38	32.56	35.14
Customer average interruption duration index (CAIDI)	Minutes	0.20	72.14	76.41	84.95	93.49	97.76
Planned system average interruption duration index (SAIDI)	Minutes	0.15	1,066.70	1,211.96	1,502.47	1,792.98	1,938.24
Probability of voltage levels falling within prescribed limits	%	0.10	15%	18%	20%	22%	25%
System losses	%	0.05	7.0%	8.5%	9.5%		
Average time to process applications for Regulated Distribution Services	Days	0.15	3.20	4.00	5.50	7.00	7.70
Average time to connect premises to the Regulated Distribution System	Days	0.15	2.50	3.40	5.00	6.60	7.50
Ave. time to answer calls at call centre	Seconds	0.00					

19. That the applicant proposes to adopt a Guaranteed Service Level Performance Incentive Scheme as required in terms of the RDWR. According to this Guaranteed Service Level scheme, customers will be directly compensated, in the form of reductions in their monthly electricity bills, if service performance falls below certain minimum thresholds. The thresholds and the penalties that will apply are as demonstrated below:

Table 13. Summary of proposed Guaranteed Service Level Incentive Scheme

Performance Measure	Threshold	Penalty level (PhP)
GSL 1. Customer experiencing a total duration of sustained service interruptions in a Regulatory Year that exceeds the threshold GSL 1.A. Unplanned Interruption GSL 1.B. Planned Interruption	22 hours 34 hours	53.00 53.00
GSL 2. Customer experiencing a number of sustained service interruptions in a Regulatory Year that exceeds the threshold GSL 2.A. Unplanned Interruption GSL 2.B. Planned Interruption	46 hours 23 hours	53.00 53.00
GSL 3. Restoration of supply to a customer after a fault on the secondary distribution network taking longer than the threshold time GSL 3.A. Fault in the Secondary Line GSL 3.B. Fault in the Distribution Transformer GSL 3.C. Fault in the Service Drop	11 hours 12 hours Within 12 hours	53.00 53.00 53.00
GSL 4. Customer connection not provided on the day agreed with the customer	within 5 working days	53.00

- 19a. That the applicant will be entitled to an additional revenue amount equal to 0.5% of its Annual Revenue Requirement, which is intended to be applied to the Guaranteed Service Level Scheme and can be used to either provide for penalties under the scheme, or for network or operational improvements to avoid such penalties.
20. That applicant proposed to convert the Maximum Average Price that will be approved by the Honorable Commission to individual rates of the Applicant's customer classes using the procedure and the proposed rate design set forth in Schedule O.
21. That applicant will comply with the requirements in Section 4(e), Rule 3 of the Rules and Regulations of Republic Act No. 9136, in relation to Rule 6 of the ERC Rules of Practice and Procedure, prior to the filing of this application with the ERC.
22. That in support of this application for the approval of its Allowed Annual Revenue and Performance Incentive Scheme, the applicant has attached the following required documents as described in the RDWR and the Position Paper:

Table 14. Supporting Information attached

Schedule	Information provided
A	Regulatory Asset Base
A1	Summary of the optimized depreciated replacement cost (ODRC) and the depreciated historical cost of the Regulatory Asset Base as at the initial valuation date (the Regulatory Asset Base).
A2	Summary of the optimized depreciated replacement cost (Schedule A2.1) and the depreciated historical cost (Schedule A2.2) of the Original Regulatory Asset Base as at the start of the Second Regulatory Period, with supporting calculations for indexing applied.
A3	Assets forecast to be acquired during the period between the initial valuation date and the start of the Second Regulatory Period.
A3.2	- Value of the assets to be acquired
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.
A6.1	- Assets included in the Original Regulatory Asset Base
A6.2	- Assets acquired in the lead-up to the Second Regulatory Period
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.
A7.1	- Assets included in the Original Regulatory Asset Base
A7.2	- Assets acquired in the lead-up to the Second Regulatory Period
A8	Application of the construction work in progress (CWIP) factor to the

Schedule	Information provided
A9	Regulatory Asset Base as at the start of the Second Regulatory Period. Summary of the optimized depreciated replacement cost (ODRC) (Sch. A9.1) and the depreciated historical cost (Sch. A9.2) 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).
B	Financial indices forecast for Second Regulatory Period
B1	Philippine quarterly CPI <ul style="list-style-type: none"> ▪ B.1.1 - Derivation of the Monthly Philippine CPI Forecast
B2	United States quarterly CPI <ul style="list-style-type: none"> ▪ B.2.1 - Derivation of the Monthly US CPI Forecast
B3	PhP/US\$ quarterly exchange rate <ul style="list-style-type: none"> ▪ B.3.1 - Derivation of the Monthly PhP/US\$ exchange rate forecast
B4	180-Day Manila Reference Rate
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)
C2	Broken down historical capital expenditure
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
G	Forecast operating & maintenance expenditure
G1	Summary of forecast operating & maintenance expenditure
G1.1	- Annual expenditure, divided in real PhP and US\$ components
G1.2	- Annual expenditure, divided in nominal PhP and US\$ components
G1.3	- Total annual expenditure, in nominal PhP
G1.4	- Justification for operating & maintenance expenditure forecasts
G2	Historical operating & maintenance expenditure
G3	Summary of expenditure on taxes (other than corporate income tax), duties and levies
G3.1	- Annual expenditure, in real PhP
G3.2	- Annual expenditure, in nominal PhP
G3.3	- Justification for expenditure
G3.4	- Historical taxes, levies & duties
H	Forecast energy consumption and demand
H1	Forecast energy consumption figures (kWh)

Schedule	Information provided
H1.1 H1.2	- Breakdown of consumption figures - Supporting evidence
H2	Forecast energy demand figures (kW)
H2.1	- Breakdown of demand figures
I	Regulatory financial statements
J	Performance incentive scheme details
J1	Price-linked incentive scheme
J1.1 J1.2	- Details of scheme proposed - Proposed target levels
J1.3	- Supporting information & calculations
	<ul style="list-style-type: none"> ▪ J.1.2.1 Computation of Performance Bands for each index ▪ J.1.3.1 – Calculation of the proposed targets for network performance ▪ J.1.3.2 – calculation of the proposed targets for service performance ▪ J.1.3.3 – Calculation of monthly SAIFI, CAIDI and Planned SAIDI for the Years 2002 - 2005
J2	Guaranteed service level scheme
J2.1 J2.2	- Details of scheme proposed - Proposed target levels
J2.3 J2.4	- Proposed penalty levels - Supporting information & calculations
K	Calculation of Weighted Average Cost of Capital
L	Additional information for price-cap model
L1	Contact details for input sheets
L2	2006 Billing & consumption data
L3	Related business revenue for 2006
L4	Maximum annual price for 2006 and 2007 (initial entrants)
L5	Tax losses carried forward from 2007 regulatory year
M	Detailed calculations for Second Regulatory Period
	Rolled forward regulatory asset base Annual revenue requirement Corporate income tax forecasts Forecast price-caps for the opening and subsequent years of the Second Regulatory Period
N	Calculation of demonstrative unbundled rates
	<ul style="list-style-type: none"> ▪ N.1 – derivation of Allocation Factors based on 2005 data
O	Proposed Procedure and Design to convert the MAP into rates of individual customers
P	Computation of the Proposed Working Capital for Purchased Power

23. That applicant most respectfully requests for approval of this application to allow it to fulfill its obligations under Performance Based-Regulation and in order to avoid irreparable losses which will ultimately result in the deterioration of its services, to the damage, and prejudice of the public, in general, and its consumers, in particular.

PRAYER

WHEREFORE, premises considered, CEPALCO respectfully prays of this Honorable Commission, upon the filing hereof, that this application be approved ex-parte based on the submitted documents, and that CEPALCO be authorized to adopt the afore-mentioned Annual Revenue Requirements, the Performance Incentive Scheme and the procedure to convert the Maximum Average Price into rates and its corresponding rate design.

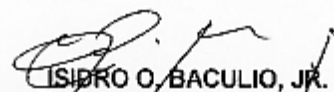
CEPALCO prays, after due notice and hearing and consideration, that the application be approved and that a final authority be issued to applicant authorizing it to adopt the above Annual Revenue Requirements, the Performance Incentive Scheme and the procedure to convert the Maximum Average Price into rates and its corresponding rate design.

Other reliefs and equitable under the premises are likewise prayed for.

Pasig City, Philippines, August 31, 2006.



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Cagayan de Oro City
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VERIFICATION CERTIFICATION

CONSUELO D. TION, of legal age, Filipino and with office address at Cagayan de Oro City, after having been duly sworn in accordance with the hereby deponee and states: That:

1. She is the President and Chief Operating Officer of Cagayan Electric Power and Light Co., Inc. (Cepalco), who had caused the preparation of the foregoing Application.

2. That the allegations set forth therein are true and correct based on her own personal knowledge and/or on the authentic records of Cepalco.

3. Cepalco has not commenced any other action or proceeding involving the same issues in the Supreme Court, the Court of Appeals, or any other tribunal or agency, to the best of their knowledge, no such action or proceeding is pending in the Supreme Court, the Court of Appeals, or different Divisions thereof, or any other tribunal or agency, which involve issues that may eventually be related to those in the Application; and that, if they should learn that a similar action or proceeding has been filed or is pending before the Supreme Court, the Court of Appeals, or different Divisions thereof, or any other tribunal or agency, they undertake to promptly inform this Honorable Commission within five (5) days thereafter.

Consuelo D. Tion
CONSUELO D. TION

SUBSCRIBED AND SWORN to before me this 22nd day of Aug 2008, at Cagayan de Oro City, affiant exhibiting to me her Community Tax Certificate No. 14484143 issued at Cagayan de Oro City on Jan. 14, 2008.

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Book No. 101 Series of 2008

LEONARDO S. BALBUENA JR.
Notary Public
My Comm. No. 10000
Exp. on 02/28/10
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Cagayan de Oro City
Cebu Prov. - 6000
2008 No. 10000