

GUIDELINES FOR THE FINANCIAL STANDARDS OF GENERATION COMPANIES

ARTICLE I

Section 1. Background

A. Philosophy / Rationale

Pursuant to Section 6 of Republic Act No. 9136 and its Implementing Rules and Regulations, generation of electric power, a business affected with public interest, shall be competitive and open. In prescribing and implementing financial standards required by the law for the generation sector, therefore, the Commission is primarily guided by its mandate to ensure quality and reliable delivery of power service to the public and protect electricity consumers.

B. Objectives

1. Financial capability standards are required by the Philippine Grid Code to be complied with by Generation Companies (GENCOs) in order to:
 - a. Promote the overall financial viability of the generation sector;
 - b. Ensure the affordability of electric power supply while maintaining the required quality and reliability; and
 - c. Protect the public interest.
2. This set of Guidelines is promulgated to:
 - a. Identify the minimum financial capability standards for GENCOs;
 - b. Prescribe the frequency and form of GENCO submissions; and
 - c. Prescribe the actions/consequences/penalties for non-compliance with the minimum financial standards for GENCOs.

C. General Principles

1. These Guidelines will set the minimum financial capability standards for GENCOs as required by Chapter 4 of the Philippine Grid Code. However, ERC may require other/additional standards for compliance in connection with other applications filed/to be filed before it by the GENCO.

2. To promote continuous improvement in efficiency and financial performance in the sector, ERC may revise/update the financial capability standards as deemed necessary by the Commission.

Section 2. Definition of Terms

- a. Debt - any indebtedness of the Borrower maturing by its terms more than one year after the date on which it is originally incurred (including that portion of any such debt payable within one year from the date of any debt-service ratio calculation), provided that debt shall be counted only to the extent that it is drawn down and outstanding
- b. Debt Service – aggregate amount of debt repayments (including lease obligations under power purchase agreements and sinking fund payments, if any) and interest and other charges on debt, including capitalized interest during construction on loans for capital expenditures
- c. Debt Service Capability Ratio (DSCR) or Interest Cover Ratio – the measure of the Genco’s ability to fulfil its debt obligations; computed in 2 ways: (1) ratio of Cash Flow From Operations after Taxes to Debt Service, and (2) ratio of Earnings before Interest and Taxes (EBIT) plus depreciation to debt service For purposes of computing this ratio, Cash Flow from Operations After Taxes shall exclude interest received and interest paid. Amortization expenses shall also be treated similarly to depreciation.
- d. Earnings Before Interest and Taxes – revenues less expenses from the Genco’s principal business activities; is identical to income from operations as determined under Philippine Generally Accepted Accounting Principles
- e. Generation Company or GENCO - refers to any person or entity authorized by ERC to operate facilities used in the generation of electricity;
- f. Generation Facility - refers to a facility for the production of electricity;
- g. Lease – an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time²
 - g.1 Capital or Financial Lease – a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not be transferred.

² from International Accounting Standard No. 17 (Leases)

g.2 Operating Lease – a lease other than a capital lease

h. National Power Corporation or “NPC” refers to the government corporation created under Republic Act No. 6395, as amended;

Section 3. Scope of Application

These Guidelines shall apply to all generation companies, including but not limited to:

- a. Entities which own and operate a generation facility;
- b. Entities which own a generation facility that is operated by another entity under any management contract;
- c. Entities which hold a Capital Lease on generating assets; and
- d. Entities which hold an Operating Lease on generating assets.

In cases where the owner and operator of the generation facility are not the same entity, both owner and operator shall be covered by the financial standards, unless it can be established to the satisfaction of the Commission that only one of the two has control over the prices and/or quantities of the output of the generation facility and as such should be the only one covered by the financial standards prescribed herein.

An entity which owns only generation facilities used exclusively for its own consumption shall be exempted from compliance with the standards required under these Guidelines.

Section 4. Financial Benchmark

A generation company is required to meet a minimum annual Interest Cover Ratio or DSCR of 1.5x throughout the period covered by its COC.

The use of the other financial standards prescribed in Section 4.2 of the Philippine Grid Code to evaluate the financial capability of a Genco shall be optional on the part of the Commission.

Section 5. Submission Requirements

1. For COC applicants and renewals:
 - a. Audited financial statements for the 2 most recent 12-month periods, if available;
 - b. Schedule of liabilities, to include the following information: name of creditor, type of credit, credit terms;
 - c. 5-year financial plan(i.e., forecast financial statements, including assumptions/bases used for revenue and cost projections); and

- d. Documentation on financial track record of the GENCO and of its principal stockholder, if available.

2. Annual submissions for the duration of the COC:

- a. Within 30 days from the filing of its Annual Income Tax Return with the Bureau of Internal Revenue, the Generation Company shall submit a complete set of its audited financial statements (i.e., balance sheet, income statement, statement of cash flows, notes), including the audit opinion and the statement of management's responsibility on the financial statements. The income statement should include a detailed schedule of operating expenses for the period. The submitted financial statements should clearly show the financial position, results of operations, and cash flows pertaining to the generation business.
- b. Together with its audited financial statements, a GENCO shall also submit forecast financial statements for the following two (2) fiscal years. The submission shall clearly identify the major forecast assumptions used by the GENCO including, but not limited to, the assumptions and bases for its volume, price, fuel, and other operating cost projections.
- c. Within 3 days from the happening of an event which results in a material change concerning or potentially affecting the company's ownership, management, operations, financial condition and performance, the Generation Company shall submit a written disclosure to the ERC of such fact or event and its impact on the company. If the event results in a GENCO not meeting or potentially not meeting the financial standards prescribed by the ERC, the GENCO is required to submit a Program to Comply within 60 days of the happening of said event.

3. Program to Comply

- a. A GENCO performing below the benchmark is required to submit, within 60 days of receipt of an ERC directive, a Program to Comply. The Program to Comply shall identify the specific activities to be undertaken by the GENCO in order to meet the benchmark.
- b. Information on the Program to Comply shall include the following:

- (i) Concrete activities/measures to be undertaken to upgrade performance and their estimated financial effects;
 - (ii) Expected semi-annual targets/milestone achievements; and
 - (iii) Clear and definite timetable for the activities and the targets.
- c. The ERC shall inform the GENCO of its action on the GENCO's Program to Comply within 60 days of receipt thereof.
- d. The GENCO shall be given one (1) year, or the remaining life of the COC in the case of a new owner of a GENCO previously issued a COC, whichever is shorter, within which to comply with the ERC-prescribed benchmark.

4. Notice of Events Affecting Program to Comply

At any time after its submission of a Program to Comply, it shall be the responsibility of the GENCO to inform the ERC in writing of any event or condition which shall prevent it from meeting the ERC-prescribed financial standard. The notice shall be given to the ERC within 7 days of the happening of such event or condition. The ERC may require the GENCO to submit a revised Program to Comply to consider the new information brought to its attention by the GENCO.

Unless the GENCO formally advises the ERC of any condition affecting the meeting of targets in its Program to Comply, the ERC shall expect the GENCO to comply with the financial standard within the prescribed period.

Section 6. Administrative Sanctions

Failure to submit to ERC the requirements as prescribed in these Guidelines may be grounds for the suspension or cancellation of the COC and/or payment of fines and penalties as may be imposed by ERC under Article III of the "Guidelines to Govern the Imposition of Administrative Sanctions in the Form of Fines and Penalties Pursuant to Section 46 of R.A. No. 9136."

Section 7. Disclosure of Non-Compliance with Financial Standards

1. Non-compliance with the financial standards by a GENCO may result in a disclosure by the ERC of such fact, together with any mitigating or aggravating circumstances related thereto, via periodic public bulletins. The public bulletin may also include the GENCO's program to comply

and other disclosures made by the GENCO to the ERC regarding its financial condition and performance.

2. In the determination of whether or not a public bulletin is necessary to be made, the GENCO's operating performance and other factors that may mitigate its poor debt service ability as measured by the DSCR shall be taken into consideration.

Section 8. Transitory Provisions

1. The NPC shall be required to meet a minimum annual DSCR of 1.0x or the minimum DSCR required by its major lenders until such time as it has completed the privatization of its generation assets. Non-compliance with this benchmark requires NPC to comply with the provisions of Section 5 (3) and (4) of these Guidelines.
2. Transferees/new owners of NPC generation assets are required to meet a DSCR of 1.5x, as set forth in Section 4 of these Guidelines.
3. Transferees/new owners of NPC generation assets in missionary electrification areas and other entities authorized to operate generation facilities in missionary electrification areas shall be exempt from compliance with the financial standards prescribed herein insofar as generation activity in the missionary electrification area is concerned. The exemption is enjoyed only for the duration of the period in which they are provided a subsidy for undertaking the missionary electrification function. Beyond this period, the financial standard prescribed in Section 4 applies.

Section 8. Effectivity

These Guidelines shall take effect on the fifteenth (15th) day following its publication in two (2) newspapers of general circulation.