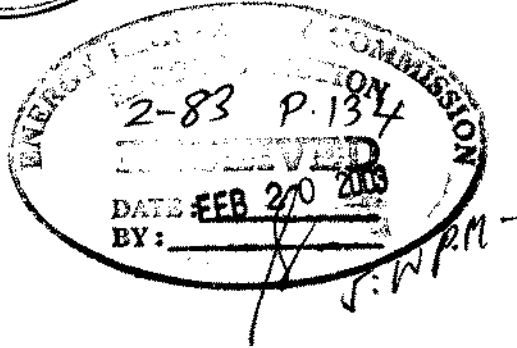




20 February, 2003

HON. LETICIA V. IBAY
Acting Chairman
Energy Regulatory Commission
Pacific Center Building
San Miguel Avenue, Pasig City

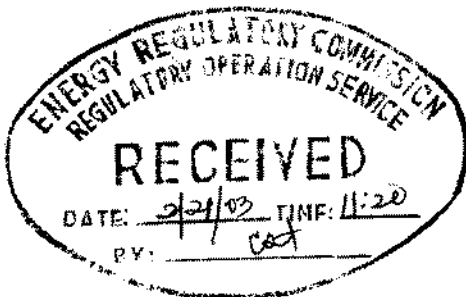


Dear Hon. Ibay:

We are hereby submitting our comments on the “Draft Business Separation and Unbundling Plan Filing Package” and the “Draft Business Separation and Unbundling Plan Guidelines.” Please see the attached sheets for details.

We look forward to our participation as we send our representatives to the upcoming public consultation.

Yours truly,



IVANNA G. Dela PEÑA
Senior Asst. Vice President
Head Utility Economics

| Section No. | Page | Topic | Comments/Recommendation |
|-------------|------|---|--|
| 1. | | General | We would like to request for clarification concerning the treatment of business overhead or "shared services" (e.g., HR, Finance), particularly, related assets, costs, and personnel. We are recommending that the Filing Package provide EPIP's guidance on the accounting and organizational separation to be required for Shared Services. |
| 2. | | Affiliate | <p>The Draft BSUP Filing Package and Guidelines do not contain a definition of an affiliate. We are recommending that the Guidelines adopt the definition from the EPIRA:</p> <p>“An “affiliate” means any person which, alone or together with any other person, directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with another person. As used herein, “control” shall mean the power to direct or cause the direction of the management policies of a person by contract, agency or otherwise. (Section 45, Paragraph 3)”</p> <p>In line with the EPIRA, we suggest that the Guidelines make it clear that the use of the term Affiliate within the BSUP Filing Package and Guidelines is limited to Affiliates within the Power Industry.</p> |
| 3. | 2.2 | 2 General Instructions: Sections of the BSUP | In line with the requirement that an EPIP submit the “number of individuals (whether employees or persons whose services are provided under a contract for service)”, we would like to request for clarification concerning outsourced activities. This is because the Outsourcing contracts between the EPIPs and the contractual service providers typically do not stipulate the number of employees that will be provided by the service provider but the specific output required by the EPIP. |
| 4. | 4.1 | 3 Description of Separation | For clarity, we are recommending that the BSUP filing package and guidelines stipulate tests or conditions to determine the minimum degree of separation and unbundling required of each EPIP. |

| Section No. | Page | Topic | Comments/Recommendation |
|--------------------|-------------|---------------------------|--|
| 5. | 5 | Milestones and Highlights | The IRR (Rule 12.1) mandates that "Retail Competition and Open Access shall be implemented no later than 3 years from the effectivity of the Act" (06/26/04). Between now and June 2004, EPIPs are left with only a few months to implement a regulator-approved plan and be allowed to participate in retail competition. |
| 6. | 6 | 5 Code of Conduct | With compliance to the Code of Conduct a requirement for EPIP-proposed BSUPs, we recommend that the effectivity of the BSUP Filing Package and Guidelines take into consideration the release date of the Code of Conduct. |

MERALCO's Comments on the *Draft Business Separation and Unbundling Plan (BSUP) Guidelines*

| | Section No. | Page | Topic | Comments/Recommendation |
|----|-------------|------|---|--|
| 1. | 1.3 | 9 | Definitions: Grid | <p>We are recommending that the definition used in the Philippine Grid Code be adopted by the Guidelines:</p> <p>“The high voltage backbone System of interconnected transmission lines, substations, and related facilities for the purpose of conveyance of bulk power. Also known as the Transmission System.” (Philippine Grid Code, p.10)</p> <p>This will align the Guidelines with definitions found in RA 9136, and the Philippine Grid and Distribution Codes.</p> |
| 2. | 2.8.5 | 15 | Cost of Auditor's Services | <p>This is only one of the various costs that an EPIP will incur to comply with and implement the BSUP. We suggest that the Guidelines establish a policy and process to allow EIPs to recover costs of this type.</p> |
| 3. | 3.6.4 | 22 | Transfer Price | <p>For clarity, we recommend that Section 3.6.4 read: “The transfer price is the cost recorded by the Business Segment acquiring the service from another Business Segment or from another business conducted by a member...” This would make it easier to determine if participants acquiring a single type of service from the particular Business Segment are paying the same price.</p> |
| 4. | 4.4.6 | 26 | Distribution Connection Services Business Segment | <p>We are suggesting that the Guidelines specify where the assets of one Distribution Business Segment (e.g. Distribution Services) ends and where that of the other Distribution Business Segment (e.g. Distribution Connection Services) begins.</p> |

| | Section No. | Page | Topic | Comments/Recommendation |
|----|-------------|------|--|---|
| 5. | 4.4.10 | 27 | Metering Services Segment | The technical aspects of metering (e.g., provision, installation, commissioning, testing, repair, and maintenance) require a totally different set of competencies compared to that of meter reading. Furthermore, meter reading naturally forms part of the billing and collection processes. Hence, we recommend that the responsibility for providing the meter-reading service should be integrated with the Regulated Customer Services and Non-Regulated Retail Services Business Segments; not with the Metering Services Business Segment. |
| 6. | 4.4.14 | 27 | Related Businesses Business Segment | <p>The definition of Related Businesses Business given in the section may be interpreted to assume that if a facility does not convey electricity then its use and management immediately falls under the Related Businesses classification. This definition does not consider facilities employed in vital and essential support activities for the distribution of electricity.</p> <p>We therefore recommend that the Related Businesses Business be composed of business activities that use distribution utility assets but are not used to perform or provide support to electricity distribution or customer services.</p> |
| 7. | 4.4.23 | 29 | Non-Regulated Retail Services Business Segment | There appears to be a typographical error in the first sentence. Section 4.4.23 should read: "The assets included in this Business Segment are all assets used directly, or a relevant share of the shared assets which are used, to provide the non-regulated services referred to in Section 4.4.22." |
| 8. | 5.1 | 31 | Prohibition on discrimination | We recommend that prohibitions on discrimination by the distribution utilities be also made to apply to TransCo. |

| Section No. | Page | Topic | Comments/Recommendation |
|-------------|-------|-------|---|
| 9. | 5.2.2 | 31 | <p data-bbox="390 130 1881 157">Disclosure of Information</p> <p data-bbox="390 157 1881 267">The scope of the information and the manner by which it will be disclosed is open-ended. Since this would affect the manner of separation, we are recommending that the data for disclosure be specified in the Guidelines. Also, we recommend that all the data be submitted to the ERC on a regular basis, where all other EIPs would be allowed (by ERC) access to the information.</p> |
| 10. | 5.4.1 | 32 | <p data-bbox="390 322 1881 349">Generation of Electricity for Distribution Utilities</p> <p data-bbox="390 349 1881 391">We believe that language from the IRR (Rule 11, Section 5, b) is clear enough and could be adopted by the Guidelines.</p> |
| 11. | 5.6 | 33 | <p data-bbox="390 541 1881 569">Common directors, officers and employees</p> <p data-bbox="390 569 1881 610">These provisions may encroach upon the authority given to the Securities and Exchange Commission (SEC) by R. A. 8799 also known as the Securities Regulation Code.</p> |
| 12. | 5.7 | 33 | <p data-bbox="390 720 1881 747">Sale of electricity to the Contestable Market</p> <p data-bbox="390 747 1881 898">This provision presupposes that an Affiliate using the name or logo of its parent company has an advantage over its competitors. This has not been demonstrated even in other jurisdictions that currently allow this practice. Also, other provisions in the BSUP Guidelines, Draft Competition Rules, and the nature of Open Access already provide sufficient safeguards that will promote and ensure the competitiveness of the market.</p> |
| 13. | 5.8 | 34 | <p data-bbox="390 939 1881 967">Code of Conduct</p> <p data-bbox="390 967 1881 1008">Since it has yet to be released, the required compliance with the Code of Conduct should consider its release date.</p> |

| Topic | Issues/Questions | Recommendation |
|------------------|---|---|
| System Losses | <p>Which Distribution business segment would be responsible for electricity pilferage (i.e. subject to the system loss caps mandated by RA 7832)?</p> <p>Would system losses above the cap be treated as "unallocated costs"?</p> | <p>As a cost and as an activity, the Guidelines remain unclear as to the treatment of System Losses. Also, with RA 7832 continuing to be in effect, we believe the Guidelines should specify with whom the responsibilities of system loss reduction and pilferage apprehension reside.</p> |
| Transition Costs | <p>The business re-organization, separation, and reporting required by the Draft BSUP represent significant one-time for the EPIP.</p> | <p>We strongly believe that the EPIP has the right to recover costs it incurred to comply with the BSUP guidelines, which can be classified as transition costs.</p> |