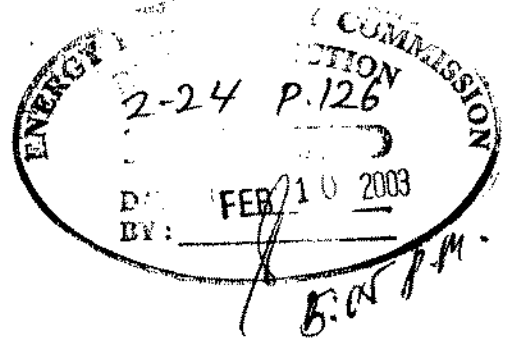


10 February 2003

The Energy Regulatory Commission
Pacific Center Building
San Miguel Avenue, Ortigas Center
Pasig City
Facsimile No. 631-8641, 631-7287, 631-5879
And through regulatory@erc.gov.ph



Attention: Atty. Marina C. Bugayong
Ms. Maurisa Moncada
Regulatory Operations Service

Re: **Comments on Draft**
Transmission Wheeling Rate Guidelines

Gentlemen:

We thank you for giving us the opportunity to comment on the draft "Guidelines on the Methodology for Setting Transmission Wheeling Rates for 2003 to 2027" (the "Guidelines") and appreciate the opportunity to participate in the public consultations thereon.

Set forth below are the general comments and proposals of First Gas Holdings Corporation ("FGHC").

General Comments

In general, FGHC finds the draft Guidelines to be sound and its strictures to be similar to rate of return (RORB) regulation. The proposed rate regulatory system (as with the RORB system), however, can be successful only where the ERC demonstrates a strong will to strictly and consistently implement its rules and procedures. These rules and procedures include proper and timely determination of the composition and prudence of assets forming the rate base (using the "used and useful" test and the 60-day working capital rule), the composition and prudence of operating expense components (which should include corporate income tax), the integrity of the asset appraisal, and the normalization of significant cost items (such as fuel and/or purchased power) which exhibit price volatility. The ERC is likewise urged to impose the RORB cap (post-tax) which is deemed fair and reasonable in this

jurisdiction. Finally, in implementing the Guidelines, FGHC urges the ERC to keep in mind that as regulator, it is duty-bound not only to protect consumers, but also to secure the continuing viability of utilities.

Specific Comments

1. **Base Rate.** In the particular case of TRANSCO, the ERC should heed the Consultants' recommendation to examine the base rate or the maximum transmission wheeling rates as set by the ERC Order of September 20, 2002 in ERC Case No. 2001-90, considering that the RORB (set at 12.38%) is beyond the maximum allowable return considered fair and reasonable in this jurisdiction.

There was also a cursory examination of the composition and valuation of the assets as well as the operating and maintenance expenses. This will result in relatively high transmission wheeling rates as well as Ancillary Charges which might encourage the bypass of transmission system.

2. **WACC.** The determination of the weighted average cost of capital ("WACC") is critical and must be verified by financial experts, specifically on the issue of the proper cost of debt and equity. Setting the WACC at an unreasonably low level may result in the system's failure to attract adequate funds to upgrade and extend our transmission facilities.

3. **Pricing.** While FGHC finds the method for setting overall rates to be reasonable, more extensive discussions must be conducted as to whether a postage stamp or other model (*i.e.*, nodal) is to be applied. This matter cannot be left simply to the workings of the wholesale electricity spot market or "WESM" which should be limited only to generation cost. This is to discourage cross-subsidization in the transmission costs.

4. **Use of CPI.** The use of the Consumer Price Index ("CPI") in the rate methodology may not be responsive to the actual movements in the market due to the lag time inherent in the said index. FGHC would seek clarification on the application of the CPI on the overall methodology.

5. **Consistency in Application to other Participants.** FGHC hopes that the ERC would be consistent in applying the approaches / principles used under the Guidelines, such as adequate return on source of capital (WACC), forecasted Operations and Maintenance Expenses and Capital Expenditures, inclusion of all taxes including corporate income tax, and a predictable timetable for review, in deciding on the unbundling cases of the Distribution Utilities.



FGHC commends the ERC for the development of the Guidelines and looks forward to participating in the scheduled public consultations thereon on February 19, 20 and 21, 2003 and to continuing its involvement as the process moves forward.

Very truly yours,

FIRST GAS HOLDINGS CORPORATION

By:



VICTOR B. SANTOS, JR.
Vice President