

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

IN THE MATTER OF THE
APPLICATION FOR APPROVAL
OF THE UNBUNDLED RATES
PURSUANT TO THE PROVISIONS OF
REPUBLIC ACT NO. 9136

ERC CASE NO. 2001-970

**ZAMBOANGA DEL SUR I ELECTRIC
COOPERATIVE, INC. (ZAMSURECO I),**

Applicant.

x ----- x

DECISION

Before this Commission for resolution is the application filed by applicant Zamboanga del Sur I Electric Cooperative, Inc. (ZAMSURECO I) on December 26, 2001 for approval of its unbundled rates pursuant to the provisions of Republic Act No. 9136.

Relative thereto, on August 20, 2002 and September 6, 2002, additional data/documents were filed by ZAMSURECO I in support of its application.

Having found said application sufficient in form and in substance with the required fees having been paid, and Order and a Notice of Public Hearing, both dated October 1, 2002, were issued setting the case for initial hearing on November 18, 2002.

ZAMSURECO I was directed to cause publication of the Notice of Public Hearing, at its own expense, twice (2) for two (2) successive weeks in two (2) newspapers of general circulation in the country, the last date of publication to be made not later than two (2) weeks before the scheduled date of initial hearing. In compliance with the said directive, ZAMSURECO I published the Notice of Public Hearing in "*Kabayan*" and "*The Manila Times*" both on October 21 and 28, 2002.

The Office of the Solicitor General (OSG), the Commission on Audit (COA) and the Committees on Energy both Houses Congress were furnished copies of the Order and the Notice of Public Hearing and were requested to have their respective duly authorized representatives present at the aforesaid initial hearing.

Likewise, the City/Municipal Mayors of Pagadian City, Aurora, Dimataling, Dinas, Dumalinao, Dumingag, Don Mariano Marcos (Sominot), Guipos, Josefina, Labangan, Lapuyan, Mahayag, Margosatubig, Midsalip, Molave, Pitogo, Ramon Magsaysay, Vincenzo Sagun, San Miguel, San Pablo, Tabina, Tambulig, Tigbao, and Tukuran, all in the Province of Zamboanga del Sur, were furnished copies of the Order and the Notice of Public Hearing for the appropriate posting thereof on their respective bulletin boards.

At the initial hearing on November 18, 2002, only ZAMSURECO I appeared. No oppositor appeared nor was there an opposition registered.

During said hearing, ZAMSURECO I submitted proofs of its compliance with the Commission's publication and posting of notice requirements which were duly marked as Exhibits "A" to "C-24", inclusive. Thereafter, ZAMSURECO I presented its two (2) witnesses. The first witness, Ms. Corcini M. Saltiga, ZAMSURECO I's Finance Manager, testified on certain relevant schedules and other documents submitted in support of the application. In the course thereof, additional documents were presented, identified by reference and marked as Exhibits "D" to "X", inclusive. Thereafter, the Commission propounded clarificatory questions on the said witness.

The second witness, Mr. Anastacio D. Autor, ZAMSURECO I's Division Chief for Special Equipment, testified on the various technical aspects of the application. At the termination of the direct examination, the Commission again propounded clarificatory questions on the said witness.

On March 18, 2003, ZAMSURECO I submitted additional data/documents required by the Commission.

On August 25, 2003, ZAMSURECO I filed its "Formal Offer of Evidence".

I. SUMMARY OF ZAMSURECO I's APPLICATION

I.A. REVENUE REQUIREMENT

ZAMSURECO I's revenue requirement per unbundled application based on historical year 2000 was as follows:

| ACCOUNT NAME | TEST YEAR |
|--|--------------------|
| KWh Sales | 77,971,648 |
| Purchased Power | PhP 181,972,238 |
| Payroll | 38,934,447 |
| Operation & Maintenance (less Purchased Power & Payroll) | 52,125,996 |
| Debt Service | 13,000,199 |
| Other Revenue Items | (275,570) |
| Reinvestment Fund (4%) ¹ | 10,933,357 |
| TOTAL REVENUE REQUIREMENT | 296,690,667 |

ZAMSURECO I's proposed revenue requirement was PhP 296,690,667 based on historical test year 2000. The Overall Average Tariff Adjustment (OATA) proposed and published was PhP 0.0625/kWh (Transcript of Stenographic Notes [TSN], November 18, 2002, page 20).

ZAMSURECO I also submitted Audited Financial Statements for the year 2000.

¹ In the UFR, this item is reflected as "Plus Percentage for Cooperative Investment".

I.B. RATE STRUCTURE/DESIGN

The unbundled rates proposed by ZAMSURECO I were as follows:

Residential

| | | |
|------------------------|-----|----------------------|
| Retail Customer Charge | PhP | 23.91/customer/month |
| Metering Charge | | 26.09/customer/month |
| Energy Charge | | 2.3338/kWh |
| Distribution Charge | | 1.0036/kWh |

Commercial

| | | |
|------------------------|--|----------------------|
| Retail Customer Charge | | 47.83/customer/month |
| Metering Charge | | 52.17/customer/month |
| Energy Charge | | 2.3338/kWh |
| Distribution Charge | | 1.5323/kWh |

Industrial

| | | |
|----------------------------|--|----------------------|
| Retail Customer Charge | | 47.71/customer/month |
| Metering Charge | | 52.29/customer/month |
| Energy Charge | | 2.8177/kWh |
| Distribution Demand Charge | | 32.42/ kW NCP |

Public Building

| | | |
|------------------------|--|----------------------|
| Retail Customer Charge | | 23.85/customer/month |
| Metering Charge | | 26.15/customer/month |
| Energy Charge | | 2.3338/kWh |
| Distribution Charge | | 0.7922/kWh |

Irrigation/Water System

| | | |
|----------------------------|--|----------------------|
| Retail Customer Charge | | 23.85/customer/month |
| Metering Charge | | 26.15/customer/month |
| Energy Charge | | 2.8107/kWh |
| Distribution Demand Charge | | 32.46/KW NCP |

Street Lights

| | | |
|--------------------------------|--|----------------------|
| Retail Customer Charge | | 11.93/customer/month |
| Metering Charge | | 13.07/customer/month |
| Energy Charge | | 2.3338/kWh |
| Distribution Facilities Charge | | 1.9353/kWh |

I.B.1. FUNCTIONALIZATION, CLASSIFICATION and ALLOCATION

All the functionalization and the allocation factors used by ZAMSURECO I were default factors provided in the Uniform Rate Filing Requirements (UFR) prescribed by the Commission. These were adopted by ZAMSURECO I as applicable to its operations.

I.B.2. SYSTEM LOSS

The actual System Loss for the year 2000 was 12%. ZAMSURECO I adopted the actual purchased power cost net of Primary Voltage and Power Factor Discounts (TSN, November 18, 2002, page 29).

I.B.3. INTER-CLASS CROSS SUBSIDY

ZAMSURECO I provided the amounts of cross subsidies for each customer type but did not include a program for the removal thereof.

| CUSTOMER TYPE | ADJUSTED EXISTING (PhP) | PROPOSED (PhP) | INTER-CLASS CROSS SUBSIDIES (PhP) |
|-------------------------|--------------------------------|-----------------------|--|
| Residential | 128,294,380 | 141,030,729 | (12,736,349) |
| Commercial | 77,743,040 | 82,834,956 | (5,091,916) |
| Industrial | 47,276,413 | 35,211,864 | 12,064,549 |
| Public Buildings | 27,044,316 | 23,108,807 | 3,935,509 |
| Irrigation/Water System | 12,573,018 | 10,084,672 | 2,488,346 |
| Street Lights | 3,759,500 | 4,419,639 | (660,139) |
| TOTAL | 296,690,667 | 296,690,667 | 0 |

Based on the submitted Supplemental Application, marked as Schedule H-1

I.B.4. LIFELINE RATE and LEVEL

ZAMSURECO I proposed the following level and rate for marginalized end-users:

| | Option 1 (At Existing Rates) |
|--------------|---|
| Level | 15 kWh |
| Rate | PhP 3.3374/kWh |

Based on the submitted Supplemental Application, marked as Sub-schedule H-3.

I.C. OTHER CHARGES

ZAMSURECO I, in its subsequent submission, provided this Commission with information on its existing Other Charges as shown below. ZAMSURECO I did not propose any adjustment to these charges.

| PARTICULARS | RATES/Unit |
|-------------------------------------|-------------------|
| 1. Transfer Fee | PhP 25.00 |
| 2. Meter Calibration | |
| Single Phase | 50.00 |
| 3 Phase | 150.00 |
| 3. Reconnection Fee | |
| a. Disconnection due to delinquency | 50.00 |
| b. Disconnection due to owners | 50.00 |
| 4. Transformer:* | |
| a. Testing Fee | |
| b. Banking/Hooking up Fees | |
| c. Debanking Fee | |

**No amount provided.*

II. COMMISSION DISCUSSIONS AND CONCLUSIONS

II.A. DETERMINATION OF TOTAL REVENUE REQUIREMENT

II.A.1. TEST YEAR

The Commission finds ZAMSURECO I's proposal to use the test year 2000 in its unbundled rate application acceptable, since it is consistent with Rule 15, Section 6 (c) of the Implementing Rules and Regulations (IRR) of R.A. 9136. Therefore, the discussions and conclusions that follow are based on Schedule A, drawn from audited financial statement figures for the historical test year 2000.

II.A.2 GENERATION and TRANSMISSION COSTS

At present, ZAMSURECO I is buying power only from the National Power Corporation (NPC).

The Generation and Transmission charges shall reflect the generation charges and transmission charges of the NPC as approved in the Commission's Orders dated February 24, 2003 and May 15, 2003, Case Nos. 2003-44 [In the Matter of the Adoption of the Generation Rate Adjustment Mechanism (GRAM) and Incremental Currency Exchange Recovery Adjustment (ICERA)] and 2003-156 [In the Matter of the Application for the Recovery of Fuel and Independent Power Producer Costs under the Generation Rate Adjustment Mechanism

(GRAM)], respectively; and the transmission charges of the National Transmission Corporation (TRANSCO) as approved in ERC Orders dated September 6 and 20, 2002, Case No. 2001-901 (In the Matter of the Application for the Approval of the Revised Unbundled Power Rates, National Power Corporation (NPC) – Applicant). The FOREX component of NPC’s Generation Charge used is as of October 2003 in the amount of PhP 0.2506/kWh. A separate charge to account for the allowable system losses shall likewise be provided (please refer to Section II.B.2.d. for details). Hence, a distribution utility with a system loss that is within the allowable cap can recover from its end-users the total cost of the generation and transmission. *Annualization*² of billing determinants was not applied.

The upward adjustment of PhP 10,663,050 made by the Commission to Purchased Power consisted of the following:

| | | |
|------------------------------------|------------|-------------------|
| Adjustment to Purchased Power Cost | PhP | 13,379,690 |
| Adjustment to System Loss | | (2,716,640) |
| Total Adjustments | PhP | 10,663,050 |

The adjustment to Purchased Power Cost of PhP 13,379,690 pertains to the difference between the proposed purchased power of ZAMSURECO I amounting to PhP 181,972,238 and the Generation and Transmission Charges based on the new rates of NPC and TRANSCO amounting to PhP 195,351,928.

² The annualization of kWh sales is calculated by multiplying the average kWh consumption of a specific customer class by their respective year-end number of customers.

Records show that ZAMSURECO I's average system loss (excluding cooperative own use) for the years 2000, 2001 and 2002 was 15.19%. The Commission allowed a system loss of 14% in the calculation of ZAMSURECO I's revenue requirement, as discussed in Section II.B.2.d. of this Decision. Thus, the Commission made an adjustment to system loss of PhP 2,716,640 to exclude the excess of actual system loss over the allowable recoverable cap of PhP 27,793,104.

Based on the new NPC generation charges and transmission charges, as well as the allowable system loss, the Commission sets ZAMSURECO I's unbundled Generation, Transmission and Recoverable System Loss as follows:

| | | |
|-------------------------|------------|--------------------|
| Generation Charge | PhP | 104,096,543 |
| Transmission Charge | | 60,745,641 |
| Recoverable System Loss | | 27,793,104 |
| Total | PhP | 192,635,288 |

ZAMSURECO I's approved generation charge shall remain fixed until changes in NPC's generation rate are approved and authorized by the Commission pursuant to its Orders dated February 24, 2003 and May 15, 2003, Case Nos. 2003-44 [In the Matter of the Adoption of the Generation Rate Adjustment Mechanism (GRAM) and Incremental Currency Exchange Recovery Adjustment (ICERA)] and 2003-156 [In the Matter of the Application for the Recovery of Fuel and Independent Power Producer Costs under the Generation Rate Adjustment Mechanism (GRAM)]. In which case ZAMSURECO I shall bill its

end-users the new generation rate charged by NPC. In the meantime, ZAMSURECO I shall discontinue charging the Purchased Power Adjustment (PPA) upon effectivity of the unbundled rates.

II.A.3. PAYROLL

The Commission made an upward adjustment on the payroll account by PhP 7,992,401, bringing this to the current salary level of PhP 46,926,848. The adjustment is due to updating salary levels as a result of step increments and an understated payroll as per ZAMSURECO I's application.

The Commission reviewed the Wage Adjustment Clause (WAC) Formula authorized by the then Energy Regulatory Board through ERB Case Nos. 94-25 and 94-96. The then Board allowed the implementation of the WAC Formula based on three (3) established criteria for it to be classified under automatic adjustment clauses. These are: 1) when such costs are extremely volatile, changing rapidly over a short period of time; 2) when such volatile cost changes represent significant portions of total utility operating expenses; and 3) when such volatile cost changes are beyond the ability of the utility to control.

Analysis shows that the wage adjustments do not warrant an automatic recovery clause. The Commission therefore rules that the application of the WAC Formula be discontinued. The growth in kWh sales will be sufficient for the

electric cooperatives to absorb increases in salaries/wages mandated by wage orders.

The Commission noted that ZAMSURECO I did not avail of the WAC Formula.

**II.A.4. OPERATION and MAINTENANCE
(less Purchased Power and Payroll)**

In general, operating expenses allowed are those which are reasonably incurred in connection with business operations to yield revenue or income. These should be required or necessary in the operation of a utility, are recurring, and should redound to the service or benefit of end-users.

The Commission enjoins ZAMSURECO I to incur only “prudent and reasonable costs” for inclusion in the determination of retail rates. While a distribution utility enjoys the benefit of passing its costs of purchased power and other reasonable costs to end-users, it is obligated as a public utility to ensure that its costs of operations, including payroll, are kept at a minimum. The distribution utility must bear in mind that its very nature is that of a service company for its end-users, with a mandate to advocate and transact judiciously for and in their behalf.

“Reasonable costs” may be defined as the cost of those goods and services which, while may not be the lowest in price, need to be incurred with

consideration of quality, efficiency, reliability and security, which are characteristics of the service that should be delivered by the distribution utility. “Prudent costs” demand that the utility ensures that its purchases of goods and services are at their minimum, without sacrificing the foregoing characteristics. When making a purchase or executing a contract, it cannot simply rely on its right to pass on its costs to its end-users.

As such, the Commission, in fulfillment of the policy of R.A. 9136 to establish a regime of free and fair competition and full public accountability to achieve greater operational and economic efficiency, enjoins ZAMSURECO I to institute and report to the Commission its respective policies and procedures for cost-cutting and for the transparent and competitive procurement of goods and services.

ZAMSURECO I’s end-users have a right to receive safe, reliable, and adequate service at a reasonable rate. On the other hand, these end-users should pay their power bills on time to ensure ZAMSURECO I’s viability. To this end, ZAMSURECO I should view a petition for an increase in rates to be the last recourse. In future filings, ZAMSURECO I should be reminded that it has the burden of proving that all reasonable and appropriate cost cutting measures have been taken, before resorting to a petition to increase rates.

The Commission made a net downward adjustment of PhP 11,992,803 on ZAMSURECO I’s Operation and Maintenance (O&M) Expenses, as follows:

Excluded Expenses:

| | |
|--|-------------------------------------|
| Amount in the UFR that exceeds the employees' benefits that are provided under NEA Guidelines on Benefits, Allowances and Other Incentives to EC Officers and Employees. | PhP (5,669,458) |
| Coop Power Consumption that is already provided for in the computation of allowable System Loss - duplication. | (1,483,454) |
| BAPA Incentives – these costs will be recovered through the Supply and Metering Charges the BAPA can charge its end-users. | (1,625,044) |
| Total Excluded Expenses | <hr/> PhP (8,777,956) |
| Other Adjustments: | |
| Consumer Prompt Payment Reclassified to Other Revenue Items | (3,214,847) |
| Net O&M Adjustment | <hr/> PhP (11,992,803) <hr/> |

The Commission rules that these excluded expenses with a total amount of PhP 8,777,956 do not fall under the qualification here-to-fore cited. These expenses translate to PhP 0.1100/kWh, which the Commission considers material.

For future rate cases, ZAMSURECO I will continually be required to make full disclosure of all its O&M expenses for the Commission to determine the prudence of all its expenditures. ZAMSURECO I should ensure that procedures are put in place so that all expenditures that are included in the determination of revenue requirement are adequately documented and that such documentation is reasonably accessible to ERC.

II.A.5. OTHER REVENUE ITEMS

The Commission defines Other Revenue Items (ORI) as revenues earned (net of other expenses) by the electric utilities from activities other than sale of electricity.

The Commission encourages ZAMSURECO I to improve its financial operation through the development of other related sources of revenue. In order to balance the interest of ZAMSURECO I and its end-users and in recognition of the fact that some of the costs incurred in rendering services under ORI have already been included in the determination of revenue requirements, the Commission has adopted this policy. The ORI that arises from activities not related to the business of the cooperative nor involves the use of its assets will not be deducted from the revenue requirement of the cooperative. The ORI that arises out of related business activities or is asset based will be shared by the cooperative and the end-user by including 50% in revenue requirement.

The total non-asset based ORI which were not deducted from the total revenue requirement amounts to PhP 3,825,271.

The ORI subjected to the 50% rule and the net adjustment to other revenue items was computed as follows:

| Particulars | Amount |
|--|----------------------|
| NPC Prompt Payment Discount , net of Consumer Prompt Payment Discount of PhP 3,214,847 | PhP 2,127,356 |
| Rental Income –Transformers | 333,180 |
| Rental Income – Poles | 275,570 |
| Staff House Rental | 50,250 |
| Other Income Rehab | 571,835 |
| Total | 3,358,191 |
| 50% of the above | 1,679,095 |
| Less: | |
| ZAMSURECO I's Proposed Other Rev. Items | 275,570 |
| NET ADJUSTMENT TO OTHER REVENUE ITEMS | PhP 1,403,525 |

The Commission also rules that any interest/dividend income earned will be retained 100% by ZAMSURECO I. However, such income should form part of the reinvestment fund and will be used solely for rehabilitation/expansion programs of ZAMSURECO I.

II.A.6. DEBT SERVICE

The Commission made a downward adjustment of PhP 1,404,224 to assure that the debt service included in ZAMSURECO I's revenue requirement is consisted with NEA's records. The details of the adjustment are shown below.

| LOANS | PhP |
|------------------------------------|-------------------|
| PER NEA: | |
| Rural Electrification: | |
| A | 278,338 |
| B | 269,656 |
| C | 122,134 |
| D | 203,892 |
| E (FR) | 83,568 |
| F | 689,492 |
| WB – RERP (RE) | 872,247 |
| Compact #1 USA | 379,666 |
| EQA | 2,898,993 |
| ANNUAL AMORTIZATION | 11,595,975 |
| PER ZAMSURECO I: | |
| ANNUAL AMORTIZATION | 13,000,199 |
| DIFFERENCE – FOR ADJUSTMENT | 1,404,224 |

Pursuant to Section 60 of R.A. 9136 and E.O. 119, savings realized by electric cooperatives (ECs) due to the assumption of certain loans by the Power Sector Assets and Liabilities Management Corporation (PSALM Corp.) shall be passed on to the ECs' end-users. ZAMSURECO I applied for a rate reduction under the Guidelines for the Implementation of the Reduction in Rates of the Electric Cooperatives Due to Condonation of Debts issued by the Commission on October 21, 2002, as amended on November 15, 2002. The Commission, in its Order on this matter dated June 19, 2003, granted ZAMSURECO I a provisional authority to reduce its rates by PhP 0.1000/kWh effective on the next billing cycle after receipt of the said Order. The said reduction in rates is likewise shown on the rate schedule provided in the Disposition of this Decision.

II.A.7. REINVESTMENT FUND

ZAMSURECO I made a proposal for the provision for reinvestment fund in its unbundling of rates application in the amount of PhP 10,933,357.

The Commission permits a reinvestment fund equivalent to 5% of a cooperatives' Gross Revenue to finance expansion and rehabilitation/upgrading of its existing electric power system in accordance with the submitted System Rehabilitation/Upgrading and/or System Loss Reduction Plan. This resulted in an upward adjustment of PhP 4,309,391 in the reinvestment fund account to bring it to the 5% allowed by the Commission.

One of the main purposes of providing the 5% Reinvestment is for the end-users of ZAMSURECO I to shoulder part of the increasing capitalization requirements, as outside sources of funding are getting scarce.

The Reinvestment Fund is authorized subject to the following conditions:

- (a) This reinvestment fund shall not be used, even temporarily, for any purpose other than for those projects specified in the submitted plan;
- (b) The amounts collected for the reinvestment fund, including interest income (as discussed in Section II.A.5.), shall be placed in a

separate account and shall be disbursed in accordance with the plan submitted by ZAMSURECO I;

- (c) ZAMSURECO I is further required to submit a progress report not later than one (1) year after the date of this Decision and every year thereafter using the format prescribed by the Commission. The progress report shall include detailed accounting itemizing total collections, the actual use of all disbursements, and actual current system losses.

Upon review of the progress report, the Commission may issue an order for ZAMSURECO I to appear and show cause why it should continue collection for the reinvestment fund; and

- (d) ZAMSURECO I shall submit a new System Rehabilitation/Upgrading and/or System Loss Reduction Plan covering the period 2004-2008, no later than one (1) year after the date of this Decision using the format to be prescribed by the Commission.

II.A.9. REVENUE REQUIREMENT SUMMARY

The table provided below is the comparison of approved revenue requirement with that proposed by ZAMSURECO I:

| ACCOUNT NAME | | ZAMSURECO I PROPOSAL | ADJUSTMENTS | ERC APPROVAL |
|----------------------------------|------------|----------------------|------------------|--------------------|
| Purchased Power | PhP | 181,972,238 | 10,663,050 | 192,635,288 |
| Payroll | | 38,934,447 | 7,992,401 | 46,926,848 |
| O & M (less PP & Payroll) | | 52,125,996 | (11,992,803) | 40,133,193 |
| Other Revenue Items | | (275,570) | (1,403,525) | (1,679,095) |
| Debt Service | | 13,000,199 | (1,404,224) | 11,595,975 |
| Reinvestment Fund ³ | | 10,933,357 | 4,309,391 | 15,242,748 |
| TOTAL REVENUE REQUIREMENT | PhP | 296,690,667 | 8,164,290 | 304,854,957 |

ZAMSURECO I proposed and published an OATA of PhP 0.0625/kWh using rates of year 2000 (as discussed in Section I.A. of this Decision). The OATA is a measurement tool based on the formula: [(Total Revenue Requirement less Existing Revenue) divided by kWh sales]. This measurement is not meant to refer to any specific customer class.

The Commission, after considering adjustments of PhP 8,164,290, approves a total revenue requirement of PhP 304,854,957, based on the year 2000, equivalent to an OATA⁴ of PhP 0.0625/kWh. The actual impact to end-users will depend on the level of rates currently being charged. This impact is illustrated in Sec. II.B.6. of this Decision.

³ In the UFR, this item is reflected as "Plus Percentage for Cooperative Investment".

⁴ The OATA was computed using existing approved distribution rates (inclusive of current WAC, if any) and unbundled power cost as of October 2003.

II.B. RATE STRUCTURE/DESIGN DETERMINATION

II.B.1. FUNCTIONALIZATION, CLASSIFICATION and ALLOCATION

The functionalization and allocation factors used by ZAMSURECO I were the default factors provided for in the UFR issued by the Commission on October 30, 2001. In the case of ZAMSURECO I, the default factors were found not to represent the best alternative among possible factors. Thus, the following three (3) default factors used by ZAMSURECO I for functionalization and allocation were modified, to wit:

First, the use of Net Plant in Service (PLTSVC-N) as a factor to functionalize and allocate Maintenance for Office and General Plant will cause skewed results by allocating these maintenance costs toward assets not part of such activity. The Commission, therefore, adopted a factor based on Net General Plant (GP-N) as a more reasonable method to allocate maintenance expense associated with general plant.

Second, the factor "Total Operation and Maintenance, Net of Fuel and Purchased Power" (TOMXFP), which was used as a default factor to functionalize costs under outside services, was replaced with the factor "Total Payroll Excluding Administrative and General Payroll" (PAYXAG) in order to remove the possibility of allocating a portion of outside services costs to the transmission function.

Third, since the Commission is now including ORI not included by ZAMSURECO I in the calculation of its revenue requirement, it was necessary to functionalize and allocate these amounts. The functionalization factors for the ORI, which were determined based on direct assignment, were as follows:

| Factor Name | Functionalization Factor Description | Total Check | Generation | Transmission | Distribution | Supply | Metering |
|-------------|--------------------------------------|-------------|------------|--------------|--------------|--------|----------|
| ORI | Other Revenue Items | 1.0000 | 0.0000 | 0.0000 | 0.3333 | 0.3333 | 0.3333 |

ZAMSURECO I submitted a classification of distribution cost into demand- and customer-related cost using the Minimum-Plant Method. This method resulted in an 80%-20% allocation on the average.

II.B.2. DESIGN AND CALCULATION OF CHARGES

II.B.2.a. BAPA

The Commission, in the design and calculation of charges takes note of the existence of the Barangay Power Associations (BAPAs) that were conceptualized by the National Electrification Administration (NEA) for the purpose of strengthening member awareness and involvement in efforts towards the reduction of system loss, improvement of collection efficiency and fortification of the institutional consciousness in the grassroots level. The creation of BAPAs was also necessitated by the growing number of cooperatives' membership, which made it impossible for the cooperatives to physically reach out to all end-users.

The cooperatives are responsible for the energization of the BAPAs while the latter are responsible for the maintenance of the electric lines and other installed equipment, the reading of meters and billing of respective member end-users. The cooperatives in this regard are mandated to grant various incentives to BAPAs such as three percent (3%) prompt payment discount, rebates on kWh sold, system loss allowance, honorarium for working BAPA officers, annual cash rewards for outstanding BAPAs and livelihood projects.

The Commission further acknowledges that cooperatives which have instituted BAPAs in their respective franchise areas incur costs with respect to the generation and distribution of power. With reference to the supply and metering functions, the cooperatives generally sustain minimal costs because they only read and bill the BAPAs' mother meters.

In the design and calculation of charges, the Commission did not consider the BAPA as a separate customer class.

II.B.2.b. GENERATION CHARGE

Consistent with the Decision in ERC Case No. 2001-901, In the Matter of the Application for Approval of the Revised Unbundled Power Rates, National Power Corporation- Applicant, dated June 26, 2002, and the Commission's Order dated May 15, 2003, the generation charge to be billed to end-users shall be the approved rate per kilowatt-hour including Benefits to Host Communities and

Franchise Charge and Foreign Exchange Rate Adjustment (FOREX). The FOREX component of NPC's Generation Rate used pertains to the supply month of October 2003 amounting to PhP 0.2506 per kWh. The NPC's approved rate will remain fixed until changes are authorized by the Commission pursuant to its Order dated May 15, 2003, as discussed in Section II.A.2. of this Decision. This allows ZAMSURECO I's Generation Charge to remain fixed until such time that NPC's approved rate is adjusted. This eliminates the need for future Purchased Power Adjustment (PPA).

II.B.2.c. TRANSMISSION CHARGE

The Commission's Decision in ERC Case No. 2001-901 dated June 26, 2002 and Order dated September 20, 2002 set the transmission charges for the National Transmission Corporation (TRANSCO) without automatic adjustments. Since the transmission rates to be paid by ZAMSURECO I are fixed, it is the decision of the Commission to likewise fix the unbundled transmission rates billed to end-users. The transmission charges approved for billing by ZAMSURECO I have been calculated based on the approved TRANSCO rates, which include cross subsidy elements to be phased out over a three-year period. The following transmission charges will apply to all end-users consistent with the gradual phase-out of the intra-grid cross-subsidies:

| Transmission Charges | Residential | Commercial | Industrial | Public Buildings | Street Lights | Irrigation |
|---------------------------------------|--------------------|-------------------|-------------------|-------------------------|----------------------|-------------------|
| October 2003 – September 2004 | | | | | | |
| Demand Charge PhP/kW | | | 19.80 | | | 19.80 |
| Transmission System Charge PhP/kWh | 0.7701 | 0.7648 | 0.6797 | 0.7511 | 0.7640 | 0.7168 |
| October 2004 – September 2005 | | | | | | |
| Demand Charge PhP/kW | | | 19.80 | | | 19.80 |
| Transmission System Charge PhP/kWh | 0.7901 | 0.7846 | 0.6988 | 0.7706 | 0.7838 | 0.7367 |
| October 2005 – September 2006 | | | | | | |
| Demand Charge PhP/kW | | | 19.80 | | | 19.80 |
| Transmission System Charge PhP/kWh | 0.8101 | 0.8046 | 0.7179 | 0.7902 | 0.8037 | 0.7567 |

The Commission utilized the Average & Excess Demand Allocation Method on the transmission costs considering that it yielded the most reasonable result for ZAMSURECO I's end-users.

II.B.2.d. SYSTEM LOSS CHARGE

The Commission defines system loss for utilities to include technical loss, non-technical loss and administrative loss or the utility's use of power for its own operations.

The Commission approves the recovery of allowed system loss through the establishment of a separate System Loss Charge in the bill to end-users. The System Loss Charge shall vary from one customer class to another depending on their respective contribution to the system loss. However, due to limited

information, the Commission is constrained to adopt a uniform System Loss Charge for all end-users of ZAMSURECO I.

The allowed system loss is equal to the average system loss for the years 2000, 2001 and 2002 or the system loss cap, whichever is lower. In arriving at this decision, the Commission recognizes that the distribution utility faces some risks of over- or under-recovery in the event its load characteristics change through time. The system loss not only results in additional unbundled generation costs but also additional unbundled transmission costs to be paid by end-users. When system loss is within the allowable cap, the distribution utility shall recover from the end-users all generation and transmission costs. Thus, system loss in excess of the allowable cap shall not be recovered from the end-users, as discussed in Section II.A.2. of this Decision.

On December 8, 1994, Republic Act No. 7832, otherwise known as the Anti-Pilferage Law, was enacted. In July 1995, the ERB promulgated the Implementing Rules and Regulations (IRR) under ERB Case No. 95-05, to implement said law. Section 10 of R.A. 7832 and Rule IX, Section 1 of its IRR provide that the recoverable Technical and Non-Technical System Loss should not exceed the fourteen percent (14%) ceiling allowed for year 2000.

The Commission found that ZAMSURECO I's 2000 to 2002 average system loss (excluding cooperative own use) was 15.19% which is higher than the aforementioned cap of 14%. The Commission believes that the present cap on

Technical and Non-Technical System Loss of 14% should be used in the calculation of revenue requirements at this time. This would, however, be subject to change upon the approval of a new policy by the Commission. The average Technical and Non-Technical System Loss or cap of 14% plus 1% cooperative own use (which should not include personal consumption of ZAMSURECO I's Board of Directors, officers and staff), whichever is lower shall be deducted from total power cost and to be billed separately as System Loss Charge.

II.B.2.e. DISTRIBUTION CHARGE

The distribution charge shall be billed on a fixed rate per kilowatt-hour for all end-users. For end-users with demand meters, the distribution charge shall be billed using a combination of a fixed rate per kilowatt (kW) and a fixed rate per kilowatt-hour (kWh).

ZAMSURECO I did not proposed for distribution wheeling rates. The Commission believes that wheeling rates are parallel to the cost of service functionalized under Distribution. Thus, the Commission orders that the Distribution Charge provided on Rate Schedules be likewise utilized as Distribution Wheeling Charges available to the future contestable market. However, other distribution utilities requesting to wheel power across ZAMSURECO I's facilities shall pay wheeling charges equivalent to Distribution Wheeling Charges for Industrial customers.

The Commission's decision to allow a distribution utility to avail of the Distribution Wheeling Charges of another distribution utility is based on the general intent of R.A. 9136 to promote a competitive generation market. Distribution utilities that currently or in the future shall rely in full or in part on the distribution facilities of another distribution utility should not be held captive by the other distribution utility in the purchase of unbundled generation. Therefore, distribution utilities are prohibited from bundling or tying the sale of generated or purchased power with the sale of unbundled distribution wheeling service.

II.B.2.f. METERING and SUPPLY CHARGES

The Commission acknowledges that cost-causation rate design principle suggests the recovery of customer-related costs associated with the metering and supply functions through fixed monthly charges. Along with this cost of service principle, however, the Commission also considers rate design impacts across the spectrum of end-users within each rate class. Although R.A. 9136 requires the removal of inter-class cross subsidies, the law does not require the removal of revenue flows that may be characterized as intra-class cross subsidies. The Commission has the flexibility to consider other factors in determining rate design for a particular class of end-users. Therefore, to mitigate the impact on below-average consumption of residential end-users, the Commission orders ZAMSURECO I to use a PhP 5.00 per meter per month and a PhP 0.4631/kWh rate for the metering function and orders ZAMSURECO I to use a PhP per kWh

rate for the supply function. All other end-users shall be billed fixed monthly meter and customer charges for the metering and supply functions, respectively.

All BAPA residential end-users will be charged with rates used for the Residential Class. The revenue that will be generated from the Supply and Metering Charges for BAPA end-users will comprise the fund from which ZAMSURECO I will draw various incentives it provides the same.

II.B.3 INTER-CLASS CROSS SUBSIDY

II.B.3.a. CROSS SUBSIDY RATE CALCULATION

The inter-class cross subsidies in existing rates are as follows:

| | Total | Residential | Commercial | Industrial | Public Buildings | Street Light | Irrigation |
|--|-------------|--------------|-------------|-------------|------------------|--------------|-------------|
| New Cost-Based Rev. Reqs. PhP | 304,854,957 | 155,398,301 | 68,813,475 | 39,364,461 | 25,567,599 | 4,424,066 | 11,287,055 |
| Existing Rates Revenue PhP | 299,868,897 | 133,137,666 | 76,844,873 | 45,209,007 | 27,929,807 | 3,841,200 | 12,906,344 |
| Total Change in Revenue PhP | 4,986,060 | 22,260,635 | (8,031,398) | (5,844,546) | (2,362,208) | 582,866 | (1,619,289) |
| %Change in Rev. | 1.66% | | | | | | |
| Normalized Existing Revenue PhP | 304,854,957 | 135,351,408 | 78,122,608 | 45,960,718 | 28,394,209 | 3,905,070 | 13,120,944 |
| Inter-Class Cross Subsidy PhP | 0 | (20,046,893) | 9,309,133 | 6,596,257 | 2,826,610 | (518,997) | 1,833,889 |
| Class Billing Determinants kWh | 79,767,466 | 35,564,448 | 20,256,661 | 11,917,281 | 7,460,760 | 1,026,082 | 3,542,234 |
| Inter-Class Cross Subsidy Charge PhP/kWh | | (0.5637) | 0.4596 | 0.5535 | 0.3789 | (0.5058) | 0.5177 |

II.B.3.b. CROSS SUBSIDY REMOVAL

Section 74 of R.A. 9136 and Rule 16, Section 5 of its Implementing Rules and Regulations provide that the ERC shall issue a scheme for phasing out all cross subsidies including subsidies within Grids, between Grids, and between classes of end-users. The phasing-out period shall not exceed three (3) years from the establishment of the Universal Charge, which may be extended for a maximum period of one (1) year subject to certain conditions.

The Commission approved the cross subsidy removal scheme for TRANSCO in its Decision dated June 26, 2002, Case No. 2001-901, which impacts the unbundled transmission rates for ZAMSURECO I's end-users. This impact is reflected in the three-year schedule for unbundled transmission charges provided in Section II.B.2.c. above.

In the instant case, the Commission will order the cross subsidy removal process at a later date following the establishment of the Universal Charge. Until such time, ZAMSURECO I will continue to charge the inter-class cross subsidy rates set forth in Section II.B.3.a. above.

II.B.4. LIFELINE RATE and LEVEL

Section 4 (hh) of R.A. 9136 defines Lifeline Rate as the subsidized rate given to low-income captive market end-users who cannot afford to pay at full

cost. Pursuant to Section 73 of R.A. 9136, the Commission hereby sets the level of lifeline consumption and its corresponding discount rates.

In determining the minimum lifeline level of consumption to be provided to the marginalized end-users, the Commission calculated the probable load requirement of a typical low-income end-user by considering two (2) lighting facilities at 20 watts each and a 50-watt radio that are being used for a reasonable number of hours. In setting the maximum level of lifeline consumption, the Commission may adjust the minimum level of consumption and/or level of the lifeline discount so as to maximize the benefit to low-income end-users while keeping the costs associated with such subsidy between PhP 0.05 and PhP 0.10 per kWh. Thus, the Commission sets the lifeline consumption maximum level of 25 kWh for ZAMSURECO I. The Commission considers the impact that the subsidized Lifeline Rates will have on other end-users who must carry the costs associated with such subsidy. This fact, combined with the desire to maximize the benefit to as many marginalized end-users as possible, has led the Commission to adopt the following graduated scale for lifeline discount for ZAMSURECO I. The graduated scale is also based on the recognition that individual end-user consumption may likely vary from month to month.

| | | |
|------------------|---|-----|
| 20 kWh and below | - | 50% |
| 21 kWh | - | 40% |
| 22 kWh | - | 30% |
| 23 kWh | - | 20% |
| 24 kWh | - | 10% |
| 25 kWh | - | 5% |

ZAMSURECO I shall apply these discounts to the following residential charges: Generation, Transmission, Distribution, Supply, Metering, and System Loss. In a given billing period, an end-user at any of the above consumption levels shall be given the specified corresponding discount on each of these rate components. An end-user with a level of consumption exceeding 25 kWh in a particular billing period shall not be entitled to any discounted lifeline rate for said period.

The cost of subsidy to lifeline end-users shall be passed on to all non-lifeline end-users. For ZAMSURECO I, the lifeline discounts result in a Lifeline Rate Subsidy to other end-users equals to PhP 0.0654/kWh.

The Commission believes that BAPAs' marginalized residential end-users should likewise enjoy the benefit of lifeline rates.

ZAMSURECO I shall coordinate with its Barangay Power Associations to gather information on the number of kWh falling under the different lifeline levels and corresponding discount rates for proper billing and implementation of lifeline benefits on the same. Each association will accordingly implement/provide lifeline benefits to its deserving BAPA end-users.

II.B.5. OTHER CHARGES

ZAMSURECO I's additional submissions to this Commission of its existing Other Charges as previously presented were considered in the determination of its revenue requirement. The revenues derived from these charges were appropriately deducted from the determination of the revenue requirement allowed to ZAMSURECO I. In future cases filed after Other Charges have been established based on cost, the appropriate level of deduction of the revenue derived from these charges may be revisited.

The Other Charges of ZAMSURECO I are hereby pegged at their existing levels until such time that the Commission sets new rates on the same. Further, ZAMSURECO I is ordered to make a compliance filing on its Other Charges one (1) year from the date of this Decision using a format to be prescribed by the Commission.

The compliance filing for the approval of Other Charges shall include rates that are cost-based, as well as all supporting cost justifications for the rates, including but shall not be limited to the amount of actual time and wages of employees performing each task encompassed by each type of Other Charges.

II.B.6. ESTIMATED IMPACT ON AVERAGE RESIDENTIAL END-USER

A comparison of the estimated impact of all adjustments to the revenue requirement on the monthly bill of an average residential end-user consuming 69 kWh a month using rates based on ZAMSURECO I's actual existing rates as of October 2003 against the unbundled rates approved by the Commission, is shown below.

| Based on Actual Existing Rate | | | Based on ERC Approved Unbundled Rates | | |
|---|----------|----------------------|---------------------------------------|----------|----------------------|
| | PhP/kWh | Amount PhP | | PhP/kWh | Amount PhP |
| Basic Rate | 2.8446 | 196.28 | Generation Charges | | |
| PPA | 0.7826 | 54.00 | Generation System Charge | 1.0262 | 70.81 |
| Power Act Reduction | (0.3000) | (20.70) | Franchise & Benefits to HC | 0.0282 | 1.95 |
| Universal Charges: | | | FOREX | 0.2506 | 17.29 |
| Missionary Elect. Charge | 0.0373 | 2.57 | Transmission System Charge | 0.7701 | 53.14 |
| Environmental Charge | 0.0025 | 0.17 | System Loss Charge | 0.3484 | 24.04 |
| Loan Condonation | (0.1000) | (6.90) | Distribution Charge | 1.0196 | 70.35 |
| | | | Supply Charge | 0.3899 | 26.91 |
| | | | Metering Charges: | | |
| | | | Retail Customer Charge/Month | | 5.00 |
| | | | Metering System Charge | 0.4631 | 31.95 |
| | | | Inter-class Cross Subsidy Charge | (0.5637) | (38.89) |
| | | | Universal Charges: | | |
| | | | Missionary Electrification Charge | 0.0373 | 2.57 |
| | | | Environmental Charge | 0.0025 | 0.17 |
| | | | Lifeline Rate(Discount)/Subsidy | 0.0654 | 4.51 |
| | | | Power Act Rate Reduction | (0.3000) | (20.70) |
| | | | Loan Condonation | (0.1000) | (6.90) |
| TOTAL BILL | | <u>225.42</u> | TOTAL BILL | | <u>242.20</u> |
| PhP/kWh | | <u>3.2670</u> | PhP/kWh | | <u>3.5101</u> |
| Rate Reduction due to Loan Condonation per ERC Order dated June 19, 2003 in Case No. 2003-307. | | | | | |

DISPOSITION

WHEREFORE, the foregoing premises considered, it is hereby decided as

follows:

1. To approve the unbundled schedule of rates of ZAMSURECO I to be effective on the first billing cycle thirty (30) days after receipt of this

Decision:

| | | Residential | Commercial | Industrial | Public Buildings | Street Lights | Irrigation |
|--|---------------|-------------|------------|------------|------------------|---------------|------------|
| Generation Charges: | | | | | | | |
| Generation System Charge | PhP/kWh | 1.0262 | 1.0262 | 1.0262 | 1.0262 | 1.0262 | 1.0262 |
| Franchise & Benefits to Host Communities Charge | PhP/kWh | 0.0282 | 0.0282 | 0.0282 | 0.0282 | 0.0282 | 0.0282 |
| FOREX Adjustment Charge | PhP/kWh | 0.2506 | 0.2506 | 0.2506 | 0.2506 | 0.2506 | 0.2506 |
| Transmission Charges | | | | | | | |
| Demand Charge | PhP/kWh | | | 19.80 | | | 19.80 |
| Transmission System | PhP/kWh | 0.7701 | 0.7648 | 0.6797 | 0.7511 | 0.7640 | 0.7168 |
| System Loss Charge | PhP/kWh | 0.3484 | 0.3484 | 0.3484 | 0.3484 | 0.3484 | 0.3484 |
| Distribution Charge | | | | | | | |
| Demand Charge | PhP/kWh | | | 19.80 | | | 19.80 |
| Distribution System Charge | PhP/kWh | 1.0196 | 0.7906 | 0.8156 | 0.8487 | 1.7786 | 0.6654 |
| Supply Charges: | | | | | | | |
| Retail Customer Charge | PhP/Cust./Mo. | | 27.95 | 47.63 | 28.08 | 27.81 | 45.90 |
| Supply System Charge | PhP/kWh | 0.3899 | | | | | |
| Metering Charges:* | | | | | | | |
| Retail Customer Charge | PhP/Meter/Mo. | 5.00 | 36.78 | 165.36 | 36.78 | 55.97 | 165.36 |
| Metering System Charge | PhP/kWh | 0.4631 | | | | | |
| Inter-Class Cross Subsidy | PhP/kWh | (0.5637) | 0.4596 | 0.5535 | 0.3789 | (0.5058) | 0.5177 |
| Universal Charges: | | | | | | | |
| Missionary Electrification | PhP/kWh | 0.0373 | 0.0373 | 0.0373 | 0.0373 | 0.0373 | 0.0373 |
| Environmental Charge | PhP/kWh | 0.0025 | 0.0025 | 0.0025 | 0.0025 | 0.0025 | 0.0025 |
| Lifeline Rate | PhP/kWh | 0.0654 | 0.0654 | 0.0654 | 0.0654 | 0.0654 | 0.0654 |
| Power Act Rate Reduction | PhP/kWh | (0.3000) | | | | | |
| Loan Condonation | PhP/kWh | (0.1000) | (0.1000) | (0.1000) | (0.1000) | (0.1000) | (0.1000) |
| Lifeline Rate (Discount)/Subsidy To be based on Residential Rate in a Graduated Scale as provided in Sec. II.B.4. of this Decision. | | | | | | | |
| Rate Reduction due to Loan Condonation per ERC Order dated June 19, 2003 in Case No. 2003-307. | | | | | | | |
| * Metering Charges to Street Lights consumers class shall apply only to those with installed meters. | | | | | | | |

2. To direct ZAMSURECO I to comply with the following:
 - a.) Discontinue charging the PPA upon effectivity of the approved unbundled rates; ZAMSURECO I automatically bill its end-users the new Generation Rate charged by NPC as approved and authorized by the Commission;
 - b.) Bill PhP 0.0373/kWh representing the missionary electrification portion of the Universal Charge in accordance with the Decision of the Commission in ERC Case No. 2001-165 (In the Matter of the Petition for the Availment from the Universal Charge the Share for Missionary Electrification, NPC-SPUG, Applicant);
 - c.) Bill PhP 0.0025/kWh representing the environmental portion of the Universal Charge in accordance with the Decision of the Commission in ERC Case No. 2002-194 (In the Matter of the Petition for the Availment from the Universal Charge the Environmental Share/Charge for the Rehabilitation and Management of Watershed Areas, NPC, Applicant);
 - d.) Bill its respective end-users using a billing format which contains at least the rate elements provided in Annex A of this Decision upon the effectivity of the approved unbundled rates. The rate elements provided in Annex A should appear on the

end-user's bill even if the rate elements currently have a value of zero or have not yet been determined by the Commission;

- e.) Inform the end-users within its franchise area of the said approved unbundled rates not later than thirty (30) days after receipt of this Decision;
- f.) Submit for verification and confirmation purposes on or before the twentieth (20th) day of the month following the effectivity of the approved unbundled rates and every month thereafter: a) five (5) sample bills for each end-user class; b) copy of the bills from the generation and transmission companies; and c) Monthly Financial and Statistical Reports (MFSRs), complete with all related schedules;
- g.) Make a formal application with the Commission for the approval of existing or future contracts with any entity for the wholesale purchases of power not yet approved by the Commission;
- h.) Make a formal application to continue the use of Other Charges within one (1) year from date of this Decision using a format to be prescribed by the Commission;
- i.) File a progress report on the reinvestment fund no later than one (1) year after the date of this Decision and every year thereafter using the prescribed formats provided in Annexes B

and C of this Decision. The report shall include detailed accounting of actual collections and deposits (including interest/dividend income), specific transactions and withdrawals for all disbursements, and actual current system losses;

- j.) Submit a new System Rehabilitation/Upgrading and/or System Loss Reduction Plan covering the period 2004 to 2008, no later than one (1) year after the date of this Decision using a format to be prescribed by the Commission; and
- k.) Institute policies and procedures for cost-cutting and transparent and competitive procurement of goods and services and submit a report thereon to the Commission within six (6) months from receipt of this Decision.

SO ORDERED.

Pasig City, February 4, 2004

MANUEL R. SANCHEZ
Chairman

OLIVER B. BUTALID
Commissioner

CARLOS R. ALINDADA
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