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

IN THE MATTER OF THE PETITION FOR THE AMENDMENT OF THE GUIDELINES FOR THE FINANCIAL STANDARDS OF GENERATION COMPANIES

ERC CASE NO. 2019-001 RM

PHILIPPINE INDEPENDENT POWER PRODUCERS ASSOCIATION, INC. (PIPPA),
Petitioner.

Promulgated:
MAY 20 2019

x-------------------------------------x

ORDER

On 07 March 2019, Petitioner Philippine Independent Power Producers Association, Inc. (PIPPA) filed a *Petition* dated 07 March 2019, seeking the amendment of ERC Resolution No. 06, Series of 2005, which refers to the Guidelines for the Financial Standards of Generation Companies.

The pertinent provisions of the said *Petition* are hereunder quoted as follows:

1. PIPPA is a domestic corporation existing under and by virtue of the laws of the Republic of the Philippines, with its principal office at the Ground Floor, Benpres Building, PIPPA Avenue corner Exchange Road, Ortigas Centre, Pasig City. It is an association composed of 28 companies engaged in power generation, presently supplying more than 82.8% (13,549.40MW) of the national grid-installed generating capacity. PIPPA serves as the forum and principal institutional advocate of common interests and concerns of private generating companies in the country.

2. On 14 April 2005, the Honorable Commission adopted ERC Resolution No. 06, series of 2005, which refers to the Guidelines for the Financial Standards of Generation Companies (hereinafter referred to as "Guidelines").

3. Considering that the Guidelines were promulgated in 2005, or fourteen years ago, there have since been a number of

significant changes in the economic conditions in the Philippines.

4. Member-companies of PIPPA understand that the Honorable Commission is mandated to ensure quality and reliable delivery of power services to the public and to protect electricity consumers. However, these economic changes should be considered when exercising this mandate. As such, PIPPA proposes the following amendments to update the Guidelines imposed on generation companies:

A. PROPOSED AMENDMENTS TO SECTION 1.2 – DEFINITION OF TERMS

5. Section 1.2 of the Guidelines currently provides the definition of terms, including the following:

1.2 Definition of Terms

x x x x

b. Debt Service – aggregate annual 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 be derived from the audited financial statements and shall exclude interest received and interest paid. Amortization expenses shall also be treated similarly to depreciation.

d. Earnings Before Interest and Taxes – equal to revenues less expenses from the GENCO's principal business activities; is identical to income from operations as determined under Philippine Generally Accepted Accounting Principles.

x x x x

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 time[2] 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.

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.

6. PIPPA proposes to include the definitions of an "INDEPENDENT POWER PRODUCER (IPP)" and an "IPP ADMINISTRATOR (IPPA)" in recognition of such entities' participation in the industry, and to provide appropriate provisions on the Petition of the rules to these entities.

7. To clarify, IPPAs enter into Administration Agreements with the Power Sector Assets and Liabilities Management Corporation (PSALM). Part of the IPPA's obligations is to make monthly payments to PSALM (often referred to as "Generation Payments"). These monthly payments are booked as a financial lease, and are not in the same nature of a debt. The monthly payments are a long-term obligation to PSALM, and are different from a long-term loan. A loan, under the Civil Code of the Philippines, is defined as:

> Art. 1933. By the contract of loan, one of the parties delivers to another, x x x money or other consumable thing, upon the condition that the same amount of the same kind and quality shall be paid, in which case the contract is simply called a loan or *mutuum*.

8. By this definition, a financial lease of an IPPA is not a loan because PSALM does not deliver money or a consumable thing to the IPPA with the condition that the same amount of the same kind and quality shall be paid. The monthly payments to PSALM are unchangeable and cannot be subject to refinancing like typical debt obligations.

9. Given the foregoing considerations, PIPPA proposes the inclusion of the following definitions:

> ***Independent Power Producer or 'IPP' – refers to an existing power generating entity which is not owned by NPC.***
>
> ***IPP Administrator or 'IPPA' – refers to qualified independent entities appointed by PSALM who shall administer, conserve and manage the contracted energy output of NPC IPP contracts.***

> ***Power Sector Assets Liabilities Management Corporation or PSALM - refers to the government corporation created under Republic Act No. 9136 to take over the ownership of all existing generation assets of the NPC, IPP contracts, real estate and all other disposable assets including the transmission business of the National Transmission Corporation. It is mandated to manage the orderly sale and privatization of such assets with the objective of liquidating all of NPS's financial obligations in an optimal manner.***

10. Similarly, PIPPA also proposes to restate the definition of "Debt Service", and to expand the definition of Earnings Before Interest and Taxes, as follows:

> Debt Service – aggregate annual amount of debt service repayments and interest and other charges on debt, including capitalized interest during construction on loans for capital expenditures ***but excluding IPPA financial lease obligations to PSALM.***

> Earnings Before Interest, Taxes, ***Depreciation and Amortization*** – equal to revenues less expenses from the GENCO's principal business activities, ***plus taxes, depreciation and amortization expense.***

11. PIPPA likewise proposes the deletion of the definition for Debt Service Capability Ratio (DSCR) in relation to PIPPA's proposal to amend the two methods of computing for the financial benchmarks. PIPPA's proposed amendments to the financial benchmarks are provided under a new Section 2.1.1. Thus, the definition of the DSCR in Section 1.2 will be redundant if not deleted.

12. Finally, PIPPA proposes the deletion of the definition of Lease, since any lease capital, financial or operating lease should not be treated as debt.

B. PROPOSED AMENDMENTS TO SECTION 1.3 – SCOPE OF PETITION

13. Section 1.3 of the Guidelines provides the applicability of the Guidelines, which states:

1.3 Scope of Petition

1.3.1 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.

14. PIPPA proposes the removal of "Entities which hold a Capital Lease on generating assets" and "Entities which hold an Operating Lease on generating assets". These entities are already included in (a) and (b) of the definition. Moreover, as previously mentioned, capital lease and operating lease is not a debt. If an entity just has a capital or operating lease, it does not necessarily provide information on the financial capability of the entity.

15. Thus, the proposed amended Scope of Petition of the Guidelines reads:

1.3 Scope of Petition

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

a. Entities which own and operate a Generation Facility; ***and***

b. Entities which own a Generation Facility that is operated by another entity under any management contract.

C. PROPOSED AMENDMENTS TO SECTION 2.1 – FINANCIAL BENCHMARK

16. The Guidelines on the Financial Benchmark reads as follows:

2.1 Financial Benchmark

2.1.1 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.

2.1.2 The use of the other financial standards prescribed in Chapter 4.2 of the Philippine Grid Code to evaluate the financial capability of a GENCO shall be optional on the part of the ERC.

17. PIPPA proposes that the financial benchmark should be revised, primarily because the DSCR of 1.5x imposes a hefty burden to generating companies, especially in a highly competitive environment and when the rates at which generators sell to regulated entities are restricted.

18. Moreover, it is now experienced that major financial institutions require a lower DSCR in obtaining loans, and these institutions have a great interest in ensuring the financial health of its borrower-entities. If the lenders do not require as much DSCR, then it is submitted that the Commission adopt a similar lower DSCR.

19. Further, since DSCR is defined to be computed in either of two ways: (1) from the ratio of Cash Flow From Operations after Taxes to Debt Service, and (2) ratio of Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) plus Cash Beginning to Debt Service, then the Financial Standards should likewise reflect this.

20. In addition, the Cash Beginning should be included in either cash flow method or EBITDA method. Including the Cash Beginning will accurately capture the Generation Companies ability to fulfil its financial obligations. Further, including Cash Beginning, and even Ending Cash or Near Cash Equivalents in determining the DSCR is an accepted practice by major financial institutions.

21. Finally, the financial standard for NPC and PSALM is lower than that of the other generation companies. NPC owns and PSALM manages generation assets, and generate electricity for the public, like other generation companies. If the financial standard for NPC is a DSCR of 1.0x because it is the minimum DSCR imposed by NPC's major lenders, this reasoning should also be followed for all other generation companies.

22. In view of this, PIPPA proposes that the financial standards should be amended as follows:

2.1 Financial Benchmark

2.1.1 A ***GENCO, NPC, and/or PSALM, shall be*** required to meet ***any one of the following financial requirement:***

a. Ratio of Cash Flow from Operations after Taxes plus Cash Beginning to Debt Service of 1.0x throughout the period covered by its COC; or

b. Ratio of Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) plus Cash Beginning to debt service of 1.0x throughout the period covered by its COC. For purposes of

computing this ratio, Cash Flow from Operations After Taxes shall be derived from the audited financial statements and shall exclude interest received and interest paid.

For new projects, including rehabilitated power plants, the first calculation shall be done after one full year of commercial operations.

2.1.2 [DELETE]

D. PROPOSED AMENDMENTS TO SECTION 3.2 – ANNUAL SUBMISSION FOR THE DURATION OF THE COC

23. The Guidelines likewise has Article III on Requirements and Procedures, specifically, in the reportorial requirements of the Generating Company, the Guidelines state:

3.2 Annual submissions for the duration of the COC:

x x x x

3.2.2 Together with its audited financial statements, a GENCO shall also submit forecast financial statements for the subsequent two (2) fiscal years. The submission shall clearly identify the major forecast assumptions and bases for its volume, price, fuel, and other operating cost projections.

3.2.3 Within three (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 GENCO 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 sixty (60) days of the happening of said event.

24. PIPPA proposes that the provisions above be amended to limit the requirement on providing a forecast financial statement only to instances when a Certificate of Compliance is being applied for or renewed, and only when there is an event that affects the ownership, management, operations, financial condition and performance of the generating company. In view of the foregoing, the proposed amendments to 3.2.2 and 3.2.3 are as follows:

3.2.2 ***A*** GENCO shall submit forecast financial statements for the subsequent ***five (5) fiscal years in case of Certificate of Compliance Petition and Renewal.*** 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.

3.2.3 Within three (3) days from happening of an event which results in a material change concerning or potentially affecting the company's ownership, management, operations, financial conditions and performance, the GENCO 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 revised forecast financial statements for the subsequent two (2) years and a*** Program to Comply within sixty (60) days of the happening of said event.

E. PROPOSED AMENDMENTS TO SECTION 4.2 – DISCLOSURE OF NON-COMPLIANCE WITH FINANCIAL STANDARDS

25. Article IV, 4.2.2, of the Guidelines provide:

4.2 Disclosure of Non-Compliance with Financial Standards

x x x x

4.2.2 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.

26. Considering the amendments proposed by PIPPA in the Financial Standards under Article II, PIPPA now proposes 4.2.2 to read as:

4.2.2 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 ***any of the identified financial benchmark under Section 2.1.1*** shall be taken into consideration.

F. PROPOSED AMENDMENTS TO ARTICLE VI – TRANSITORY PROVISION

27. Article VI of the original Guidelines provided for a TRANSITORY PROVISION, specifically:

ARTICLE VI
TRANSITORY PROVISION

6.1 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 Article 3.3 and 3.4 of these Guidelines.

6.2 Transferees/new owners of NPC generation assets shall be required to meet a DSCR of 1.5x as set forth in Article II of these Guidelines.

6.3 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 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 Article II applies.

28. The Transitory Provision are no longer necessary because PIPPA's proposed DSCR is the DSCR of NPC under this provision. Thus, the amended Article should be read as follows:

ARTICLE VI
EXEMPTION

6.1 [DELETE]

6.2 [DELETE]

6.3 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 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 Article II applies.

29. The proposed amendment will likewise be consistent with PIPPA's proposed Financial Standards.

G. PROPOSED AMENDMENTS TO ARTICLE VII – EFFECTIVITY

30. The original Guidelines provided an article on Effectivity:

ARTICLE VII
EFFECTIVITY

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

31. In lieu of an article solely on Effectivity, PIPPA proposes instead an article on Final Provisions to read as follows:

ARTICLE VII
FINAL PROVISIONS

7.1 ***Separability Clause. If for any reason, any part or section of these Guidelines is declared unconstitutional or invalid, the other parts or sections hereof which are not affected thereby shall continue to be in full force and effect.***

7.2 Effectivity. These Guidelines shall take effect on the fifteenth (15th) day following its publication in ***one (1) newspaper*** of general circulation.

32. Petitioner likewise proposes amendments to 1.1.2.1 and 1.1.3.1 of the Guidelines to conform to the Philippine Grid Code 2016 Edition. Said provisions are proposed to read as follows:

1.1.2.1 Financial Capability standards are required by the Philippine Grid Code to be complied with by Generation Companies (GENCOs) in order to:

a. Specify the financial capability standards for the GENCOs;

b. Safeguard against the risk of financial non-performance;

c. Ensure the affordability of electric power supply while maintaining the required quality and reliability; and

d. Protect the public interest.

1.1.3.1 These Guidelines will set out the minimum financial capability standards for GENCOs, as required by ***Appendix 1, FS.A 1.3,*** of the Philippine Grid Code. However, ERC may require other/additional standards for compliance in connection with other Petitions filed/to be filed before it by the GENCO.

33. Finally, to remain consistent, PIPPA proposes that all references (i.e. GENCOs, PSALM, NPC, Generation Facility, Program to Comply, and other defined terms) be made uniform throughout the Guidelines.

34. For ease of reference, attached as **ANNEX "A"** hereof is the marked-up version of the original Guidelines with PIPPA's proposed amendments (marked in red font).

PRAYER

IN VIEW OF THE FOREGOING, the PHILIPPINE INDEPENDENT POWER PRODUCERS ASSOCIATION, INC. (PIPPA) respectfully prays for the Honorable Commission to **ADOPT** its proposed amendments to the Guidelines for the Financial Standards of Generation Companies and issue the corresponding Resolution adopting the said amendments.

Other relief just and equitable under the premises are likewise prayed for.

Finding the instant *Petition* to be sufficient in form and substance with the required fees having been paid, the Commission hereby sets the determination of compliance with the jurisdictional requirements, expository presentation, and public consultations on the following dates and venues:

Date	Venue	Activity
13 June 2019 (Thursday) Ten 'o clock in the morning (10:00 A.M.)	**ERC Main Office** 8th Floor, Pacific Center Building, San Miguel Avenue, Pasig City	Jurisdictional and Expository Presentation
20 June 2019 (Thursday) Ten 'o clock in the morning (10:00 A.M.)	**ERC Visayas Office** St. Mary's Drive, Banilad, Cebu City 6000	Expository Presentation and Public Consultation for Visayas Stakeholders

27 June 2019 (Thursday) Ten 'o clock in the morning (10:00 A.M.)	**ERC Mindanao Office** Mintrade Bldg., Monteverde Ave. cor Sales St., Davao City 8000	Expository Presentation and Public Consultation for Mindanao Stakeholders
19 July 2019 (Friday) Ten 'o clock in the morning (10:00 A.M.)	**ERC Main Office** 8th Floor, Pacific Center Building, San Miguel Avenue, Pasig City	Public Consultation for Luzon Stakeholders

All interested parties may submit their comments (in both hard and soft copies) on the Proposed Amendments on or before **07 June 2019**. Electronic copies may be sent to licensing@erc.gov.ph. Parties who have filed their written comments on or before the prescribed period would be given priority during the above-scheduled public consultation. The said *Petition* may be photocopied at cost, during the regular office hours at the ERC Main Office.

Accordingly, PIPPA is hereby directed to:

1) Cause the publication of the attached *Notice of Proposed Rule-Making* once (1x) in a newspaper of nationwide circulation in the Philippines at its own expense, with the date of publication to be made not later than ten (10) days before the date of the scheduled initial hearing;

2) Furnish with copies of this *Order* and the attached *Notice of Proposed Rule-Making*, all Distribution Utilities (DU's) for the appropriate posting thereof on their respective bulletin boards;

3) Furnish with copies of this *Order* and the attached *Notice of Proposed Rule-Making* the Offices of the Mayors of Pasig City, Cebu City, Davao City and their respective local legislative bodies for the appropriate posting thereof on their respective bulletin boards;

4) Inform of the filing of the *Petition,* the reason therefor, and of the scheduled public consultation thereon the consumers within the affected franchise

area of the DUs, by any other means available and appropriate;

5) Furnish with copies of this *Order* and the attached *Notice of Proposed Rule-Making* the Office of the Solicitor General (OSG), the Commission on Audit (COA), and the Committees on Energy of both Houses of Congress. They are hereby requested, if they so desire to send their duly authorized representatives at the scheduled hearing; and

6) Furnish with copies of the *Petition* and its attachments all those making requests therefor, subject to reimbursement of reasonable photocopying costs.

On the date of the initial public consultation, PIPPA must submit to the Commission its written compliance with the aforementioned requirements attaching therewith, methodically arranged and duly marked the following:

1) The evidence of publication of the attached *Notice of Proposed Rule-Making* consisting of affidavits of the Editors or Business Managers of the newspapers where the said *Notice of Proposed Rule-Making* was published, and the complete issues of the said newspapers;

2) The evidence of actual posting of this *Order* and the attached *Notice of Proposed Rule-Making* consisting of certifications issued to that effect, signed by the aforementioned Mayors, LGU legislative bodies, or their duly authorized representatives, bearing the seals of their offices;

3) The evidence of other means employed by PIPPA to inform the consumers within the affected area of the filing of the *Petition*, its reasons thereof, and of the scheduled hearing thereon;

4) The evidence of receipt of copies of this *Order* and the attached *Notice of Proposed Rule-Making* by the Office of the Solicitor General (OSG), the Commission on Audit (COA), and the Committees on Energy of both Houses of Congress;

5) The evidence of receipt of copies of the *Petition* and its attachments by all those making requests therefor, if any; and

6) Such other proofs of compliance with the requirements of the Commission.

PIPPA must also be prepared to make an expository presentation of the instant *Petition* aided by whatever communication medium that it may deem appropriate for the purpose. For the benefit of the consumers and other concerned parties, PIPPA must be able to put in plain words and explain the nature of the *Petition* with relevant information and pertinent details substantiating the reasons and justifications being cited in support thereof.

Failure of PIPPA to comply with the above requirements within the prescribed period shall be a ground for cancellation of the scheduled hearing, and the resetting of which shall be six (6) months from the said date of cancellation.

SO ORDERED.

Pasig City, 06 May 2019.

FOR AND BY AUTHORITY
OF THE COMMISSION:

AGNES VST DEVANADERA
Chairperson and CEO

ERC
Office of the Chairperson
AVSTD-2019-05-510-0029

LS: RSPV/MCC/BSA/GEO

COPY FURNISHED:

1. SYMECS Law
Attys. Garth F. Castañeda, Joni R. Gomez and Aubrey Joy D. Brampio
Counsels for Petitioner PIPPA
3109 One Corporate Center, Julia Vargas corner
PIPPA Avenue, Ortigas Center, Pasig City

2. Philippine Independent Power Producers Association, Inc. (PIPPA)
Petitioner
Ground Floor, Benpres Building, PIPPA Avenue corner
Exchange Road, Ortigas Centre, Pasig City

3. Office of the Solicitor General (OSG)
134 Amorsolo Street, Legaspi Village, Makati City

4. Commission on Audit (COA)
   Commonwealth Avenue, Quezon City 1121

5. Senate Committee on Energy
   GSIS Building, Roxas Boulevard, Pasay City 1307

6. House Committee on Energy
   Batasan Hills, Quezon City 1126

7. Power Sector Assets & Liabilities Management Corporation (PSALM)
   2nd Floor SGV II Bldg., Ayala Avenue, Makati City

8. Philippine Rural Electric Cooperatives Association, Inc. (PHILRECA)
   4/F Casman Bldg., 372 Quezon Avenue, Quezon City

9. Philippine Electric Plant Owners Association (PEPOA)
   8/F STRATA 100 Building, F. Ortigas Jr. Road,
   Ortigas Center, Pasig City

10. Office of the Mayor
    Pasig City

11. Office of the Local Government (LGU) legislative body
    Pasig City

12. Office of the Mayor
    Cebu City

13. Office of the Local Government (LGU) legislative body
    Cebu City

14. Office of the Mayor
    Davao City

15. Office of the Local Government (LGU) legislative body
    Davao City

16. National Association of Electricity Consumers for Reforms (NASECORE)
    No. 10, 680 Quirino Avenue, Bayside Court Compound
    1700 Parañaque City

17. Philippine Chamber of Commerce and Industry (PCCI)
    Campus Avenue corner Park Avenue,
    McKinley Town Center, Fort Bonifacio, Taguig City

18. Department of Energy (DOE)
    Energy Center, Rizal Drive,
    Bonifacio Global City, Taguig City

19. All Private Distribution Utilities

20. All Electric Cooperatives

21. Market Operations Service (MOS)
    Energy Regulatory Commission
    12th Floor, Pacific Center, San Miguel Avenue, Pasig City