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

IN THE MATTER OF THE APPLICATION FOR APPROVAL OF THE REVISED RATE SCHEDULES IN COMPLIANCE WITH SECTION 36 OF REPUBLIC ACT NO. 9136 AND ERC ORDER DATED OCTOBER 30, 2001, WITH PRAYER FOR PROVISIONAL AUTHORITY

- and -

FOR APPROVAL OF REVISION OF RATES AND APPRAISAL OF PROPERTIES WITH PRAYER FOR PROVISIONAL AUTHORITY

ILIGAN LIGHT AND POWER, INC. (ILPI),

Applicant.

x - x

ERC CASE NO. 2001-893

D E C I S I O N

Before the Commission for resolution are the consolidated applications filed by Iligan Light and Power, Inc. (ILPI) for: (a) approval of revision of rates and appraisal of properties with prayer for provisional authority filed on June 5, 2001 and docketed as ERB Case No. 2001-841 (ERB Case No. 2001-57); and (b) approval of the revised rate schedules in compliance with Section 36 of Republic Act No. 9136 and ERC Order dated October 30, 2001, with prayer for provisional authority filed on December 26, 2001 and docketed as ERC Case No. 2001-893.

ERC CASE NO. 2001-841 (ERB Case No. 2001-57)

On March 23, 2001, ILPI filed an application for approval of revision of rates and appraisal of properties with prayer for provisional authority. Subsequently, on June 5, 2001, ILPI filed a “Motion to Admit Supplemental Application” attaching therewith its “Supplemental Application” docketed as ERB Case No. 2001-841 (ERB Case No. 2001-57).

Having found the said application sufficient in form and substance with the required fees having been paid, an Order and a Notice of Public Hearing, both dated June 14, 2001, were issued setting the application for hearing on July 9 and 10, 2001.

In the same Order, ILPI was directed to cause the publication of the Notice of Public Hearing at its own expense, twice (2x) in two (2) newspapers of general circulation in the Philippines, which should include one (1) newspaper of local circulation within ILPI’s franchise area, the last day of publication to be made not later than two (2) weeks before the date of the initial hearing.

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

Likewise, the Mayor of Iligan City was furnished with a copy of the Order and the Notice of Public Hearing for the appropriate posting thereof on its bulletin board.

On June 26, 2001, ILPI filed a “Motion to Reset Hearing” praying that the initial hearing of the case set on July 9 and 10, 2001 be reset to a later date. Accordingly, in the Order dated June 28, 2001, the said hearing was reset to July 23 and 24, 2001. ILPI was directed to cause the publication of the Notice of Public Hearing indicating therein the new dates of hearing.

On July 23, 2001, Lanao Power Consumers Group (LAPOCOF) filed a "Motion for Intervention" praying that it be admitted as intervenor in the case. On even date, the Consumer's Organization in Iligan Light and Power (COILPOWER) filed its "Opposition" alleging, among others, that ILPI is not losing and therefore not entitled to any increase; that any increase would be contrary to the spirit of R.A. 9136 and would deprive the residents of the city of affordable electricity; and that the application is premature.

In the meantime, at the July 23, 2001 initial hearing, the following entered their appearances: Atty, Manuel L. M. Torres for ILPI; Attys. Thomas Dean Quijano and Cipriano Benedicto Ratunil for oppositor City of Iligan, Atty. Leonor Quiñones for intervenor LAPOCOF; and Atty, Elmer Maglinao for oppositor COILPOWER. Intervenor and oppositors questioned the jurisdiction of the then Energy Regulatory Board (ERB) to conduct hearings in view of the passage of R.A. No. 9136, particularly Section 36 thereof. ILPI argued that the provision invoked by the intervenor and oppositors did not limit the ERB's authority to continue to hold office to merely administrative matters but pertains to all powers and functions vested with it before the passage of the aforesaid Act, including its rate-fixing power. Relative thereto, said intervenor and oppositor were directed to submit their respective memoranda on the issue within fifteen (15) days from said date of hearing. However, ILPI was allowed to present its proofs of compliance with the publication and posting of notice requirements which were duly marked as Exhibits "A" to "E-1", inclusive. Thereafter, the hearing of the case was adjourned and held in abeyance pending the resolution of the aforementioned issue.

On August 7, 2001, ILPI filed its "Memorandum on Opposition to Motion to Suspend Proceedings", alleging that the ERB, on a hold-over capacity, was authorized to continue performing its rate fixing function; that the instant application is separate and distinct from the unbundling application mandated to be filed under R.A. 9136; and that the financial standing of ILPI warrants immediate relief.

On August 20, 2001, COILPOWER filed its “Memorandum” reiterating its stand that the ERB no longer has the power to hear the application. On even date, City of Iligan filed its “Memorandum” alleging that R.A. 9136 has abolished ERB; that the members of the Board can only act on administrative matters not on rate fixing; and that absent any implementing rules of R.A. 9136, ERB cannot act on the instant application. Still on the same date, LAPOCOF filed its “Position Paper” stating its stand similar to the oppositors.

On October 3, 2001, the Honorable Congressman Alipio Cirilo Badelles filed his opposition to the instant application.

On January 30, 2002, LAPOCOF filed a “Motion to Suspend Proceedings and to Declare Previous Proceedings Null and Void” and “Omnibus Motion to Suspend Proceedings and for the Production and Inspection of Applicant’s Business Records and Accounts”. On even date, a similar motion was filed by COILPOWER. LAPOCOF likewise moved that it be given a copy of ILPI’s unbundling application. Said motion was granted.

In the Order dated February 11, 2002, the Commission has resolved to consolidate the instant application with the unbundling application of ILPI which was docketed as ERC Case No. 2001-893.

On March 7, 2002, LAPOCOF filed a “Motion for Reconsideration” praying that the Order dated February 11, 2002, which declared the consolidation of the two (2) cases be set aside alleging that the two are entirely different proceedings that cannot be validly consolidated without confusing the issues. Relative thereto, in the Order dated March 22, 2002, the Commission denied said “Motion for Reconsideration.

ERC CASE NO. 2001-893

On December 21, 2001, ILPI filed an application for approval of the revised rate schedules in compliance with Section 36 of Republic Act No. 9136 and ERC

Order dated October 30, 2001, and for approval of appraisal of properties with prayer for provisional authority.

Having found the said application sufficient in form and substance with the required fees having been paid, an Order and a Notice of Public Hearing, both dated January 30, 2002, were issued setting the application for hearing on March 7 and 8, 2002.

In the same Order, ILPI was directed to cause the publication of the Notice of Public Hearing at its own expense, twice (2x) for two (2) successive weeks in two (2) newspapers of nationwide circulation in the country, the last day of publication to be made not later than two (2) weeks before the scheduled date of initial hearing.

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

Likewise, the Mayor of Iligan City was furnished with copies of the Order and the Notice of Public Hearing for the appropriate posting thereof on its bulletin board.

On March 6, 2002, the City of Iligan filed a “Motion for Reconsideration” praying that the order of denial of the motion to suspend proceedings be reconsidered and set aside. On the same date, LAPOCOF filed its “Motion for Intervention” and “Opposition”.

During the March 7, 2002 initial hearing, ILPI presented its proofs of compliance with the Commission’s publication and posting of notice requirements and had these marked as Exhibits “A” to “C”, inclusive. Thereafter, it presented its witnesses, Mr. Frederick Regala, ILPI’s Head for Rates and Regulatory Matters; Ms. Maria Veronica Andrea Pore, Sycip, Gorres and Velayo’s (SGV) Branch

Manager for Cagayan de Oro; and Engr. Salvador D. Ocianas, Cuervo Appraisers, Inc. Division Manager, for direct examinations. Mr. Regala testified on the procedures followed in the preparation of the unbundling application. Ms. Pore testified on the audit conducted on the books of ILPI. Engr. Ocianas testified on the conduct of the appraisal of ILPI's properties and equipment. In the course thereof, documents were presented and marked as Exhibits “D” to “V”, inclusive. At the termination of the direct examinations, intervenor Engr. Robert Mallillin and LAPOCOF reserved their rights to cross-examine the said witnesses while the Commission propounded clarificatory questions. In the course thereof, ILPI was directed to submit a copy of the authority of the Internal Audit Manager to represent it and file the instant application.

On March 15, 2003, the Sangguniang Panlunsod of Iligan City submitted Resolution No. 02-148 seeking that the hearings of this case be transferred to Iligan City. Relative thereto, in the Order dated March 19, 2002, the Commission denied said request due to lack of material time and citing the provision of Rule 3, Section 4(s) of the Implementing Rules and Regulations of R.A. 9146. In the same Order, ILPI was directed to submit its comment on City of Iligan's “Motion for Reconsideration”.

On April 3, 2002, LAPOCOF filed a “Motion for the Issuance of Subpoena Duces Tecum/Order Directing the Sycip Gorres & Velayo (SGV) Audit Firm to Bring/Submit to the Commission its Audit Working Papers of Financial Statements for 1999 & 2000 of Iligan Light & Power Inc., (ILPI)”. On April 24, 2002, ILPI filed its “Opposition to Motion for Issuance of Subpoena Duces Tecum” alleging that the documents being requested are irrelevant to the proceedings and partake of confidential matters, which are proprietary in nature. In connection therewith, in the Order dated April 26, 2002, LAPOCOF's motion was denied for being unreasonable as the same can be verified during the course of the cross-examination of ILPI's witness.

During the May 20, 2002 hearing, ILPI submitted a copy of the Board Resolution authorizing its Internal Audit Manager to file the instant case. Thereafter, it continued its direct examination of its witness, Engr. Ocianas. Engr.

Mallillin and LAPOCOF conducted their respective cross-examinations on the said witness.

During the May 21, 2002 hearing, LAPOCOF cross-examined ILPI's witness, Mr. Regala. In the course thereof, the Commission directed ILPI to submit a copy of the Resolution allowing the writing-off of the uncollectible accounts. Engr. Mallillin likewise cross-examined said witness. The Commission propounded clarificatory questions.

ILPI then presented its last witness, Mr. Ronillo Catapang, Cuervo Appraisers' Manager for Machinery and Equipment Division, who testified and collaborated the testimony of Engr. Ocianas. In the course thereof, a document was presented and marked as Exhibits "V-1" and "W". LAPOCOF and Engr. Mallillin conducted their respective cross-examinations of the said witness. In the course thereof, the Commission directed ILPI to submit certain documents.

ILPI then moved that it be given fifteen (15) days from said date of hearing within which to submit its formal offer of exhibits. Said motion was granted.

On June 3, 2002, Engr. Mallillin submitted a "Position Paper" which discussed the following issues:

a) Rate Design

The Distribution Charges, which are attributable to fixed costs, should be in "P/kW" if metering installations permit, with the exception of those without demand meters; that meter charge should be in terms of "Peso per Customer"; that the supply charge should also be in "Peso per customer"; that the Distribution System Charge should be determined based on the delivery voltage level of the customer; that the Distribution System Loss Recovery should be a separate and distinct charge segregated by voltage level in each customer class in order to reflect rate levels that are closer to the true cost of service; and that the

Lifeline Rate threshold level should consider also the connected load aside from the historical energy consumption of the customer.

b) Rate Base should be reduced by 20% since it is bloated.

c) Costs and Financial Issues

If the Weighted Average Cost of Capital (WACC) is used, it should be related to their long term sources of funds so that short term securities, loans or other obligations are not included; that cross subsidies should be phased out starting with the proposed charges/ rates under the rate unbundling case; that poles, line hardware, line transformers, conductors and wires should be allocated under "Demand" only; and that the System Loss Cap under Republic Act No. 7832 should be maintained.

On June 18, 2002, ILPI filed its formal offer of exhibits.

During the July 11, 2002 hearing, LAPOCOF manifested that it would submit its comment on ILPI's formal offer within fifteen (15) days from said date of hearing. Thereafter, it presented its only witness, Engr. Norberto V. Oller, LAPOCOF's Vice President, who testified on the inaccuracy of the figures for the rate base, working capital and revenue submitted by ILPI based on his study and on the real financial position of ILPI. ILPI conducted its cross-examination of said witness. LAPOCOF then conducted redirect examination of the same witness while ILPI conducted its re-cross examination. Engr. Mallillin made some manifestations on LAPOCOF's presentation. LAPOCOF also made some manifestations.

In the same hearing, ILPI submitted several documents as requested by LAPOCOF. Relative thereto, LAPOCOF moved that the lifeline rate be restudied.

On August 23, 2002, LAPOCOF submitted its "Comments or Opposition to the Formal Offer of Exhibits".

At the August 30, 2002 hearing, ILPI recalled two (2) of its witnesses, Mr. Regala and Mr. Catapang, for rebuttal. Thereafter, LAPOCOF conducted its cross-examination of the said witnesses. The Commission then propounded clarificatory questions. ILPI conducted a re-direct examination of the witnesses.

During the October 10, 2003 hearing, LAPOCOF conducted a re-cross-examination of Mr. Regala while the Commission propounded clarificatory questions. Thereafter, LAPOCOF moved that it be given fifteen (15) days from said date of hearing within which to submit its formal offer of exhibits. ILPI moved that it be given the same number of days from receipt of said formal offer within which to file its comment thereon and to submit the computation of its franchise tax as well as the Statement of its Procedure of Aging its Accounts Receivables. Both motions were granted.

In the Commission's Order dated October 21, 2002, ILPI was directed to submit several documents. On December 19, 2002, ILPI submitted said documents.

In its letter dated December 10, 2002, LAPOCOF submitted its proposal on ILPI's lifeline rate.

On February 26, 2003, LAPOCOF submitted its formal offer of exhibits.

On April 8, 2003, ILPI was directed to submit various documents.

On May 26, 2003, ILPI submitted the various documents required in its letter dated May 22, 2003.

1. ILPI's PROPOSAL

ILPI's proposed rate structure reflects the unbundling of rates in accordance with the sectors or functions identified in Section 5, R.A. 9136. These rates were developed on the basis of the data and calculations contained in the schedules prescribed in the Uniform Rate Filing Requirements (UFR) as per ERC Order dated October 30, 2001, as follows:

TABLE 1

Rate Schedule	Reference
Flat Rate Service – Retail	Schedule No. 11
Flat Rate Service – Wheeling	Schedule No. 12
Residential – Retail	Schedule No. 21
Residential – Wheeling	Schedule No. 22
Commercial – Retail	Schedule No. 31
Commercial – Wheeling	Schedule No. 32
Industrial – Retail	Schedule No. 41
Industrial – Wheeling	Schedule No. 42
Bulk KV Power – Retail	Schedule No. 51
Bulk KV Power – Wheeling	Schedule No. 52

I.A. Revenue Requirement

ILPI in its application calculated its Total Revenue Requirement based on test year 2000 using the Return on Rate Base (RORB) methodology. The application contains asset value both at historical cost and appraised value. ILPI's calculation used the appraised or sound value of assets, as underlying basis for the formulation and design of the Revised Rate Schedules. The submitted historical cost of assets, as required by RA 9136-UFR, was solely for informational purposes, and not as basis for ratemaking.

On the basis of the submitted schedule (Schedule B), the proposed total revenue amounted to PhP 443,816,741, has been calculated by adding the total cost of service and the total return on rate base (computed at 12.11% of the rate base) or an average increase of PhP 0.3181 per kilowatt-hour.

TABLE 2

Account Name	Electric Only	Electric Adjust.	Adjusted Electric
Fuel	PhP 0		PhP 0
Purchased Power	310,423,465		310,423,465
Payroll	24,883,793		24,883,793
Operation & Maintenance	49,972,802		49,972,802
Depreciation & Amortization	26,727,452		26,727,452
Income Taxes	963,469		963,469
Other Expenses	0		0
Return on Rate Base	22,100,686		22,100,686
Revenue Requirement	443,816,741		443,816,741
Other Revenue Items	0		0
Total Revenue Requirement	**PhP 443,816,741**		**PhP 443,816,741**

I.A.1. Operating Revenue

ILPI's actual total operating revenue amounted to PhP 397,658,797 for the year 2000 computed as follows:

TABLE 3

Customer Type	Operating Revenue
69kV Schedule 51 – Bulk Power	PhP 73,176,689
13.8kV Schedule 41 – Industrial Schedule 43 – Industrial	25,516,822
220V Schedule 11 – Flat Rate Schedule 21 – Residential Schedule 31 – Commercial	1,527,528 148,707,540 148,730,219
Total	**PhP 397,658,797**

I.B. Rate Base

ILPI proposed that Schedule B (Restated Value of assets) be used as basis in the determination of its Rate Base. Thus, ILPI utilized the appraised value of assets as of December 31, 1997 which was further adjusted to reflect additions, retirements and depreciation for the period January 1, 1998 to December 31, 2000. The proposed rate base is as follows:

TABLE 4

	Total Company	Non Electric	Electric Only
Distribution Plant	PhP 349,413,049		PhP 349,413,049
General Plant	70,181,824		70,181,824
Total Plant in Service	PhP 419,594,873		PhP 419,594,873
Unbundled CWIP	582,589		582,589
Total	PhP 420,177,462		PhP 420,177,462
Accumulated Depreciation			
Distribution Plant	PhP 208,447,152		PhP 208,447,152
General Plant	30,144,553		30,144,553
Total Accum. Depr.	PhP 238,591,705		PhP 238,591,705
Net Plant in Service	PhP 181,585,757		PhP 181,585,757
Plant Held for Future Use	8,583,531		8,583,531
Materials & Supplies	5,404,714		5,404,714
Cash Working Capital	62,668,949		62,668,949
Other Rate Base Item	(3,502,200)		(3,502,200)
Total Rate Base	**PhP 254,740,751**		**PhP 254,740,751**

I.B.1. Plant in Service

I.B.1.a. Asset Valuation

ILPI, in support of its unbundled rates application, submitted for approval to the Commission a report of Cuervo Appraisers, Inc. with respect to the sound value of ILPI's properties existing as of December 31, 1997. Based on the Appraisal Report dated March 24, 1998, ILPI's existing assets as of December 31, 1997 were appraised based on cost level as of December 1997 at the prevailing Peso-to-Dollar exchange rate of PhP 40.116 to US$1.00. Based on its report, ILPI's assets had a total cost of reproduction new of PhP 343,310,900 and sound value of PhP 209,346,400, to wit;

TABLE 5

	Cost of Reproduction, New	Sound Value
Land	PhP 46,064,200	PhP 46,064,200
Building	9,559,000	5,115,000
Other Land Improvement	755,000	469,000
Electrical Equipment	271,187,000	147,572,000
Communication Equipment	832,000	501,000
Transportation Equipment	10,200,000	6,740,000
Computer Equipment	2,574,800	1,695,000
Furniture & Office Equipment	2,138,900	1,190,200
Grand Total	**PhP 343,310,900**	**PhP 209,346,400**

I.C. Weighted Average Cost of Capital

ILPI proposed for a Weighted Average Cost of Capital of 12.11% or equivalent to a return of PhP 30,845,759, computed as follows:

TABLE 6

Component	Amount as of Dec. 31, 2000	Component As % of Total	Component Cost of Capital	Weighted Cost of Capital
Long-Term Debt	4,781,434	2.87	13.70%	0.39%
Notes Payable	2,000,000	1.20	17.00%	0.20%
Total Debt	6,781,434	4.07		0.60%
Common Equity	160,014,482	95.93	12.00%	11.51%
Total	166,795,916	100.00		12.11%
Rate Base				254,740,751
Return On Rate Base				30,845,759

I.D. Functionalization Factors

ILPI applied the formulated functionalization factors to the individual identified accounts by simply multiplying the factors to the whole value of each account. In addition, ILPI proposed a Supply function which represent the 12.11%

return on cash working capital in the cost of power.

As alleged by ILPI, the Supply function deserves a return on rate base because it provides retail service to its customers, it pays NPC the cost of power in advance before it is able to charge and collect the same from its customers. Effectively, the Supply function requires working capital to finance the said trading or buy-and-sell activity. The rate base for this function is the cash working capital that entitles it to a corresponding return.

I.E. Rate Structure/Design

ILPI's proposed rate structure consisted of charges for the following specific functions: a) Generation/Transmission, b) Supply, c) Distribution (Sub-Transmission, Primary & Secondary), and d) Customer and Metering.

I.E.1. Generation Charge

In calculating the Generation Charge, ILPI submitted for approval the following formula:

$$\textbf{GENERATION CHARGE} = \frac{\text{Total Cost of NPC Generation Charge}}{\text{Total kWh sales for the month}}$$

I.E.2. Supply Charge

ILPI proposed Supply Charge to represent return on rate base for generation and transmission. This was determined by dividing the computed revenue requirement for the Supply Related Revenue function against kiloWatthour sold for customer class resulting to P0.0432 per kWh applicable to all customer classes.

I.E.3. Transmission Charge

ILPI likewise proposed a formula designed to calculate the Transmission Charge:

$$\textbf{TRANSMISSION CHARGE} = \frac{\text{Total Cost of NPC Transmission Charge}}{\text{Total kWh Sales for the Month}}$$

I.E.4. Distribution Charge

ILPI functionalized its Distribution function into three categories: Sub-Transmission, Primary and Secondary. ILPI determined its Distribution Charge for Residential, Commercial & Flat Rate for each categories with kilowatt-hour sold as their billing determinant resulting in a peso per kilowatt-hour charge, while customer for Bulk Power & Industrial customer were determined by using the non-coincident peak as billing determinant deriving a peso per kilowatt-hour.

I.E.5. Customer and Metering Charges

ILPI used year end number of customer and total number of meters in determining the customer and metering charges, respectively, resulting to a peso per customer per month.

I.E.6. System Loss

ILPI proposed a 12% system loss cap to be the recoverable rate for its system loss through the proposed Line Loss Charge formula. The proposed 12% loss cap is based on five (5) year historical systems loss. ILPI's percent loss allocation is based on purchased energy. The 69 KV sub-transmission, transformer loss and 13.8 KV distribution line loss are all technical loss. ILPI alleged that the 220V loss contribution is both technical and non-technical losses, which cannot be segregated. The line losses are categorized as follows:

TABLE 7

Per Voltage Level	Purchased Energy (in kWh)	69KV Sub-Trans. Contr. (in kWh)	Transfor-Mer Loss Contr. (in kWh)	13.8KV Distr. Line Loss Contr. (in kWh)	220V Loss Contr. (in kWh)	Loss (in kWh)	% Loss Alloc.	Proposed System Loss Cap (%)
Totals	162,229,945	695,639	8,884,031	1,883,132	5,665,495	17,118,298	10.55%	
69KV		177,388				177,388	0.11%	0.12%
13.8KV		41,042	703,567	149,133		893,744	0.55%	0.63%
220KV		477,208	8,180,463	1,733,998	5,655,495	16,047,165	9.89%	11.25%
						Total Proposed System Loss Cap		12.00%

I.E.7. Other Charges

ILPI proposed to bill separately the line loss and franchise tax for generation and transmission through the following proposed formula:

Line Loss Charge (P/Month) = [(TTC + TGC) x (1 + LLR)]

Franchise Tax Charge (P/Month) = [(TTC + TGC + LLC) x (1/(1-FT)]

Where:

TTC = Total transmission charge by the Company to the customer for the month
TGC = Total generation charge by the Company to the customer for the month
LLR = Line loss rate for the month which is the actual line loss rate for the Company's secondary (220V) distribution system or the line loss cap as stated below.
LLC = Total line loss charge by the Company to the customer for the month as computed herein.
FT = Franchise tax rate of 2.75% (2%=National plus 75% of 1% = Local).

System Loss percentage vary depend on customer classification

a. Residential Retail Service	-	11.25%
b. Flat Rate Retail Service	-	11.25%
c. Commercial Customer	-	11.25%
d. Industrial Retail Service	-	0.63%
e. Bulk kV Power Retail Service	-	0.12%

Flat Rate Service (Schedule No. 11 & 12)

In line with ILPI's efforts to reduce systems loss, ILPI proposed to change the duration of Flat Rate Service under Schedule Nos. 11 & 12 from 12 hours to 24 hours a day for the following basic reasons:

1. Photocells installed at streetlights do not last for over one year and are often not replaced. Most flat rate service is provided to streetlights. This would result to street lights consuming electricity for 24 hours instead of only 12 hours, presumably during night time, as the photocells no longer work and that street lights are often left switched on; and
2. Billing of streetlights is based on the count of working streetlights. Those that are busted although with ballast are excluded in the count. It is settled that ballasts consume electricity when switched on even if the bulb is busted. Consequently, the electricity consumed thereon will not be billed in the flat rate service but would go to systems loss.

With this change, ILPI gives an option to those who would like to avail of the electricity by having their connections metered. Thus, only their actual consumption are registered and billed. This way, the consumer is billed for what he actually consumes and the utility is able to bill what it actually provides.

Wheeling Rate

In consonance with the filing requirement, ILPI also proposed Wheeling Rate for each customer class as follows:

1. Distribution Charge
   a) Wire Charge – based on computed distribution charge/customer class
   b) Customer-Related Charge – based on computed distribution charge/customer class
   c) Metering Charge
2. Universal Charge – to be determined by ERC
3. Cross Subsidy – to be determined by ERC

I.F. Cross-Subsidies

ILPI adjusted its actual revenue as presented in Schedule H and Sub-Schedule H-2 (Proof of revenue using the existing rates). The total revenue requirement for each customer class was compared to normalized existing rates, which resulted to the following inter-class cross subsidy calculation:

TABLE 8

		Revenue Requirements			
		Existing Rates			
Rate Schedules	KWh Sales	Actual	Normalized	Proposed Rates	Cross-Subsidy
69 Kv					
Sched. 51-Bulk Power	36,922,620	73,176,689	82,291141	84,921,255	(2,630,114)
13.8 kV					
Sched. 41-Industrial	8,548,744	25,516,822	25,063,679	28,236,057	(3,172,378)
220 V					
Sched.11-Flat Rate	520,558	1,527,528	1,509,542	1,693,111	(183,569)
Sched.21-Residential	49,525,574	148,707,540	181,073,161	164,460,929	16,612,232
Sched.31-Commercial	49,594,051	148,730,219	153,879,218	164,505,389	(10,626,171)
Total	145,111,547	397,658,797	443,816,740	443,816,741	(1)

ILPI proposed to gradually remove these inter-class cross subsidies within a 3-year period where actual removal will start on the second year after implementation of the unbundled rates under the following scheme: In the first year, no removal of subsidies will be effected on the unbundled rates. This is to avoid rate shock to the customers in the initial implementation of the unbundled rates because the effective rates will be the normalized existing rates of ILPI. On the second year, one-third of subsidy will be removed to gradually reflect the true cost of service of the different customer classes. On the third year, another one-third of the subsidy will be removed. Thus, on the fourth year, the remaining one-third of the subsidy will be finally removed. As for the detailed manner of the gradual removal of subsidies, ILPI proposed the following:

- Cross Subsidy debits of the Flat Rate, Commercial, Industrial and Bulk Power customers under rate Schedule Nos. 11,12,31,32,41,42,51 & 52 shall be implemented immediately at the start of the unbundled rates implementation in accordance with the proposed rate schedules.
- Cross Subsidy (credits) of the Residential customers under rate Schedule Nos. 21 & 22 shall be implemented on the second month upon implementation of the unbundled rates. This cross subsidy credit is made a month delayed due to its nature and the manner it is computed as stated in the proposed rate schedule.
- ILPI further proposed to delay by a month the implementation of the unbundled (proposed/new) rates of the Residential customers under Schedule No.21 to avoid rate shock to the customers since the first month of implementation does not include any cross subsidy (credit). Thus, the Residential customers shall be billed the latest ERB approved rates (ILPI existing rates before normalization) only on the first month of implementation of the unbundled (proposed/new) rates. The second and succeeding months will be billed under the proposed /new unbundled rates.

Under this scheme, the Subsidizing customers (Flat Rate, Commercial, Industrial and Bulk Power) will first be charged the cross subsidy debit. The total of the said cross subsidy debits will be the basis for determining the cross subsidy (credit) of the Subsidized customer (Residential). Hence, ILPI will not be burdened of financing any portion of the cross subsidy removal process. The customers would also be mutually benefited by this scheme since it would be cost-neutral for them. More importantly, rate shock would be avoided.

I.G. Lifeline Rate

ILPI proposed a lifeline rate of PhP 0.6646/kWh (existing distribution rate) for its lifeline customers with a recommended 10.8 level of consumption (kWh/month) to be qualified for the lifeline rate within the franchise area of ILPI. ILPI assumes that a marginalized end-user has only the most essential and necessary electric appliances and household fixtures, to wit:

TABLE 9

	Power	Usage (Hrs)	Energy (kWh)
2 x 25 watts Incandescent Bulb	0.05	6	9
1 x 5 watts AM/FM Radio	0.005	12	1.8
Total			**10.8**

The deficit in revenue requirement as a result of billing these groups of marginalized end-users shall be the lifeline cross-subsidy that will be billed only to other residential customers.

I.H. Transmission and Distribution Utility Customer Services

ILPI proposed other charges applicable to all its customer classes, to wit:

TABLE 10

Description of Services	Ave. Annual Cost
Relocation of Pole	3,440.00
Transformer testing	
On-site	1,720.00/transformer
On-compound	860.00/transformer
Transformer servicing	5,160.00/transformer
Testing of Potential Transformer or Current	250.00/transformer
Installation of Streamer	
3 meters and below	395.00 -for 1st streamer 180.00 –succeeding streamers
4 meters and above	645.00 – for 1st streamer 430.00 – succeeding streamers
With removal	Plus 50% of total cost

I.I. Affiliate Data

ILPI claimed that the affiliate submitted in this instant application refer to First Iligan Services and Trading Corp. (FISTCOR), an affiliate which provides contractual services for ILPI. This affiliate is treated like any other non-affiliate contractual services provider and all contracts awarded thereto were subjected to established bidding procedures. Contract rates are likewise subjected to evaluation based on prevailing market rates. None of the assets of ILPI is being used by the said affiliate without corresponding costs, and vice-versa.

The following are the services provided by FISTCOR as stated in Schedule G-4 (UFR filing):

1. Clearing the road right-of-way
2. Secondary line improvement
3. Streetlights metering
4. Transformer Load Monitoring
5. Removal and/or replacement of primary and secondary poles
6. Tellering services

I.J. Non-Recurring Rates

ILPI proposed the following non-recurring charges as charges for other services:

TABLE 11

Description of Other Services	Rate
Rental	
Service Vehicle	250/hour
Utility Vehicle 5 tonner	550/hour
Utility Vehicle 25 tonner	1,250/hour
Transformer rental	50/kVA/month
Pole Rental	100/pole/year
Line Rental	5% of actual materials usage
Services	
Transformer installation	1,290/transformer
Transformer removal	1,290/transformer
Private Secondary Line Extension	1,720/span
Relocation of pole	3,440/pole
Transformer testing	
On-site	1,720/transformer
On-compound	860/transformer
Transformer servicing	5,160/transformer
Testing of potential or current transformer	250/PT or CT
Installation of Streamer	395 – for 1st streamer
3 meters and below	180 – succeeding streamers
4 meters and above	645 – for 1st streamer
	430 – succeeding streamers
With removal	Plus 50% of total cost
Tools Usage	
Testing Equipment	350/day

II. COMMISSION DISCUSSIONS AND CONCLUSIONS:

In reaching the conclusion herein, the Commission took into consideration the documents as well as the comments and issues submitted by the applicant, intervenor, oppositor and other interested parties who manifested their respective position on the instant application.

II.A. Determination of the Total Revenue Requirement

II.A.1. Test Year

The Commission finds ILPI'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 B, "Revalued Cost by Function" (Cost of Service by Function-Historical Test Year).

II.A.2. Generation and Transmission Costs

Generation Cost

The Commission updated the generation cost based on the most recent approved NPC rate, i.e. ERC Case No. 2003-44, (In the Matter of the application for the recovery of Fuel and Independent Power Producer Costs under the Generation Rate Adjustment Mechanism [GRAM], NPC – Applicant) Order dated May 15, 2003 and ERC Case No. 2003-498, (In the Matter of the Adoption of the Incremental Currency Exchange Rate Adjustment (ICERA), NPC and PSALM – Applicants) Order dated December 4, 2003. The Commission authorized NPC and PSALM to implement effective December 2003 billing ICERA Rate of PhP0.2206 per kWh for Mindanao.

The total purchased power cost, as presented in the application, amounting to PhP 310,423,465 was adjusted to reflect the following:

a) The Commission decided to retain the system loss cap prescribed under Rule IX Section 1 of the Implementing Rules of Republic Act No. 7832 pending the conduct of a comprehensive study, which is

9.5% and 1%. Hence, the Commission used the maximum allowable cap for system loss at 9.5% instead of the 12% proposed herein by ILPI and actual company use of 0.32% for the year 2000. (See further discussion on Section II.H.3)

b) The Commission also used annualization in calculating the kilowatt-hour purchased power cost. This is calculated as the sum of the products of the average kilowatt-hour consumption for each rate class and the year-end number of customers for each rate class; and

c) Since power rates are to be applied prospectively, the Commission also updated the purchased power costs to the most recent levels available.

Based on November 2003 data submitted by ILPI to the Commission, ILPI buys 100% of its power requirements from NPC. As such, the generation cost as computed by the Commission reflects the cost of electric power bought from NPC as of supply month November 2003. The resulting total adjusted purchased power cost amounting to PhP 335,299,564 for the test year 2000 was computed as follows:

TABLE 12

Purchase Power Cost submitted by ILPI (inclusive Of Transmission Component)	PhP 310,423,465
Adjustment due to Update of Purchased Power Costs	26,363,712
Total	PhP 336,787,177
Excess System Loss	(1,487,613)
Total Purchased Power Cost included in Revenue Requirement	**PhP335,299,564**

Transmission Cost

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 TRANSCO without any provision for an automatic adjustment thereof. Since the transmission rates to be paid by ILPI are fixed, it is the decision of the Commission to likewise fix the unbundled transmission rates to be billed to end-users. The transmission charges approved for billing by ILPI have been calculated based on the approved TRANSCO rates, which include cross subsidy elements to be phased out over a three-year period.

System Loss

A separate charge to account for allowable system loss shall likewise be provided. The Commission decided to retain the system loss cap prescribed under Rule IX Section 1 of the Implementing Rules of Republic Act No. 7832 pending the conduct of a comprehensive study on the matter. Hence, the Commission sets the maximum allowable cap for system loss at 9.5% or actual, whichever is lower.

Based on the new generation and transmission charges, as well as the allowable system loss, the Commission has determined ILPI's unbundled generation, transmission and recoverable system loss as follows:

TABLE 13

Generation Charge	PhP185,714,425
Transmission Charge	116,629,488
Recoverable System Loss	32,955,651
Total	**PhP 335,299,564**

ILPI's approved generation charge shall remain fixed until changes in NPC's generation rate are approved and authorized by the Commission pursuant to its Order dated February 24, 2003, ERC Case No. 2003-44 (GRAM) and ERC Case No. 2003-498 (ICERA), Order dated December 4, 2003. In view thereof, the Commission does not foresee the need for ILPI to continue to implement its Purchased Power Adjustment (PPA) clause. Towards this end, the Commission hereby directs ILPI to discontinue the implementation of its Purchased Power Adjustment (PPA) upon the effectivity of the herein approved unbundled rates.

II.A.3. Operation and Maintenance (Less Power Cost & Payroll)

The general criteria in the evaluation of expenses to be allowed for recovery are: (1) that the expense is a requisite of, or necessary in the operation of the utility; (2) it is recurring; and (3) it redounds to the benefit of the utility's customers (Public Service Commission [PSC] Decision in Cases Nos. 85889, 85890 and 89893). The Commission enjoins ILPI 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 the consumer, 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 as a service-oriented company, its mandate is to advocate and transact judiciously for and in behalf of its consumers.

"Reasonable costs" refers to 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 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, a utility cannot simply rely on its right to pass on its costs to its consumers. As such, the Commission, in fulfillment of the policy of the EPIRA to establish a regime of free and fair competition and full public accountability to achieve greater operational and economic efficiency, enjoins ILPI to institute and report to the Commission their respective policies and procedures for cost-cutting and the transparent and competitive procurement of goods and services.

ILPI's customers have a right to receive safe, reliable, and adequate service at a reasonable rate. To this end, ILPI should view a petition for an increase in rates to be the last recourse. In future filings, ILPI 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.

Operations and Maintenance account was adjusted to PhP 37,151,517 after considering the above adjustments amounting to PhP 12,821,285.

TABLE 14

Total O & M per ILPI	PhP 49,972,285
Adjustments:	
Expenses Excluded for Ratemaking Purposes	(12,821,285)
Franchise Tax (separate item)	(9,151,587)
Adjusted O & M	**PhP37,151,517**

Adjustments

The Commission finds some expenses to be unnecessary in the provision of ILPI's electric service and therefore excluded the same for ratemaking purposes, as follows:

TABLE 15

Particulars	Amount
Pensions and Benefits	PhP 1,861,482
Donations	187,745
Total	**PhP 2,049,227**

The Commission adjusted the uncollectible accounts downward by PhP1,620,471 (PhP 2,852,422 – PhP 1,231,951) to the equivalent five year average of uncollectible accounts, as follows:

TABLE 16

Year	Amount
1996	PhP 1,910,639
1997	1,396,694
1998	0
1999	0
2000	2,852,422
Total	PhP 6,159,755
5-year average	PhP 1,231,951
Actual Uncollectible Accounts	(2,852,422)
Disallowed Amount	PhP 1,620,471

Franchise taxes shall appear as a separate line item on the customers' bills as a percentage of the total monthly electricity charges. Given this rate design, it is appropriate to remove the amount of PhP 9,151,587 associated with franchise taxes from the revenue requirement as this is just a pass through item.

For future rate cases, ILPI will continue to be required to make full disclosures of all it's O & M expenses in order for the Commission to determine the prudence of its expenditures. Unless otherwise justified by ILPI, expenses found to be unreasonably incurred shall not be allowed by the Commission as part of its recoverable costs to be passed on to ILPI's end-users.

II.A.4. Depreciation and Amortization

Based on the submitted data, ILPI already excluded the depreciation expense on ERC disallowed assets (II.C.3.). Thus, the Commission accepted the depreciation expense proposed by ILPI in its application.

ILPI is required to set up a depreciation fund each year corresponding to the whole amount of depreciation that it has recorded on its books. The setting up of this fund should be done on a monthly basis corresponding to the monthly depreciation. ILPI will be required to strictly account for the expenditures out of this fund which should be used strictly for investment in electric plant. The utility is free to withdraw funds from this account at any time but all withdrawals should be reported to the Commission within thirty (30) days specifying the use of the funds. This report should be consolidated with the monthly reportorial requirement (M-001 & M-002).

II.A.5. Income Taxes

The finality of the Supreme Court Decision in G.R. Nos. 141314 and 141369 dated April 9, 2003 affirms that for ratemaking purposes under RORB methodology, income tax payment should not be recovered from customers as operating cost.

In view of the above, income tax payments in the amount of PhP 963,469 was excluded from ILPI's revenue requirement.

II.B. Other Revenue

The Commission considered Other Revenue as items to be deducted from the revenue requirement used to calculate the rates for the end-users. Since all the expenses associated with the provision of the services that gave rise to these items of revenue are included in the revenue requirement, the income generated must also be considered, to wit:

TABLE 17

PARTICULARS	AMOUNT
Pole Rental	PhP 1,697,711
Transformer Rental	274,692
Service Fee	242,863
Utility Equipment Rental	133,290
Prompt Payment Discounts (50%)	3,526,331
Total Adjusted Other Revenues	**PhP 5,874,887**

The Commission believes that the utility and end-users should share the benefits of the prompt payment discount received by ILPI from NPC amounting to PhP 9,312,704. However, ILPI also gives prompt payment discount to its Bulk Power customers amounting to PhP 2,260,042. Thus, the fifty percent (50%) of the discount equivalent to PhP 3,526,331 should be deducted from the revenue requirement used to calculate the rates for the end-users and fifty percent (50%) retained by the utility to serve as incentive to improve efficiency in the payments of its purchased power costs.

II.C. Rate Base

II.C.1. Summary of Net Plant In Service

ILPI's net plant in service as of December 31, 2000 determined in the rate base computation in this case was computed as follows:

TABLE 18

	Net Plant In Service
Assets in service as of December 31, 1997 as appraised	PhP 209,346,400
Less: Disallowed Assets	
3 Standby Generator Sets	PhP 9,210,000
Cooling Tower	174,000
3 Daytanks	45,000
Tank	57,000
Site VI (Agricultural Land)	14,342,500
Total	PhP 23,828,500
Adjusted Value of Assets in Service as of December 31, 1997	**PhP 185,517,900**
CWIP	539,268
Total	PhP 186,057,168
Add/(Deduct)	
Addition net of Retirement (1998-2000)	72,774,974
Depreciation (1998-2000)	(77,246,385)
Plant In Service as of Dec. 31, 2000	**PhP 181,585,757**

II.C.2. Asset Valuation as of December 31, 1997

ILPI submitted for ERC's approval the appraisal conducted by Cuervo Appraisers, Inc. of its properties existing as of December 31, 1997. Based on the submitted report, ILPI's assets have a total value of PhP 343,310,900 as cost of reproduction, new and PhP 209,346,400 as sound value, to wit;

TABLE 19

	As of December 31, 1997	
	Cost of Reproduction, New	**Sound Value**
Land	PhP 46,064,200	PhP 46,064,200
Building	9,559,000	5,115,000
Other Land Improvement	755,000	469,000
Electrical Equipment	271,187,000	147,572,000
Communication Equipment	832,000	501,000
Transportation Equipment	10,200,000	6,740,000
Computer Equipment	2,574,800	1,695,000
Furniture & Office Equipment	2,138,900	1,190,200
GRAND TOTAL	**PhP 343,310,900**	**PhP 209,346,400**

II.C.3. Assets Found Not In Service

In the said Appraisal Report, assets that were disallowed in ERB Case No. 94-11 were included in the valuation of ILPI's properties as of December 31, 1997 by Cuervo Appraisers, to wit:

TABLE 20

	Cost of Reproduction New	**Sound Value**
3 Standby Generator Sets	PhP 30,672,000	PhP 9,210,000
Cooling Tower	290,000	174,000
3 Daytanks	76,000	45,000
Tank	95,000	57,000
TOTAL	PhP 31,133,000	PhP 9,486,000

Above mentioned assets were disallowed by the then ERB in its Decision dated May 29, 2001 under Case No. 94-11 (In The Matter of the Application For Revision of Rates and Appraisal of Properties with Provisional Authority). The previous Board concluded that the said generator sets and support were never used by ILPI in its electric operation, hence, were deducted from the total appraised value of its properties and equipment.

During the May 20, 2002 hearing, Engr. Norberto J. Oller, Oppositor representing Lanao Power Consumer Foundation questioned the inclusion of the three (3) standby generators amounting to PhP 9,210,000 in ILPI's appraisal. Oppositor Oller alleged that these generators were never used by ILPI in its electric operation. ILPI witness, Mr. Frederic Regala testified that these standby generating units are not part of the rate base in their unbundling application. It has PhP 12 Million value at cost, but as of ILPI's UFR filing, these were already fully depreciated. The appraisal portion of these standby generating sets, although appraised by Cuervo Appraiser, were not recorded in ILPI's books since these assets were not yet in service as of UFR filing. Thus, the Commission decided that the said standby generator sets and support shall be deducted from the total appraised value of ILPI's properties and equipment as these were not useful in the operation of electric service.

Likewise included in the appraisal report were lands consisting of two (2) contiguous lots, containing an aggregate area of 28,685 square meters (Site VI) appraised at PhP 500 per square meter with a total value of PhP 14,342,500. These lands are located on the southwest side of Luinab, Barangay Road within Barangay Luinab, Iligan City. ILPI included these assets in its UFR filing as Plant Held for Future Use amounting to PhP 8,583,531, representing the acquisition cost of the land.

In the same hearing, Cuervo appraiser, Mr. Ocianas testified that these lands were considered as agricultural land and there were no improvement made by ILPI during the 1997 appraisal. In this regard, the Commission opined that said assets shall be deducted from the total appraised value of ILPI's properties and equipment as they were not used/useful in the operation of the business. This is in accordance with the principle in ratemaking that only properties and equipment which are used, useful and necessary in the operation of a utility should form part of the rate base and be entitled to return.

II.C.4. Materials and Supplies

The reported materials and supplies in the amount of PhP 5,404,714 were inclusive of office supplies amounting to PhP 251,552. The Commission believes that materials and supplies included in the computation of rate base should be limited to electrical materials and supplies that are essential in providing electricity supply. Thus, the Commission excluded office supplies from the rate base.

II.C.5. Allowance for Cash Working Capital

Working capital is money a business must have available to meet payroll and expenses until customers have paid for the service or product. Utilities are usually allowed, as part of their rate base, an amount for working capital to cover expenses during the time it takes for the customers to use the service, be billed for it and collect payments.

ILPI included an amount equal to two (2) months cash operating and maintenance expenses including purchased power costs as the allowance for cash working capital. The cash working capital allowance included in the rate base should approximate the actual cash requirements of ILPI based on the estimated net lag in its cash flow. This is not an issue related to the actual timing of the recovery of a particular cost. The relevant factors to consider in a lead-lag analysis for purposes of determining cash working capital requirements are the following:

1. The time ILPI pays for the energy (kWh) sold to its customers; and
2. The time ILPI requires its customers to pay for the same energy (kWh).

In order to refine the application of the formula used in past rate proceedings, a more detailed review of the actual lag in cash flow associated with the payments for purchased power and the inflow of cash from ILPIs' customers was undertaken. With respect to the outflow of cash associated with the payments for purchased power, it was determined that the time from the provision of service to the outflow of funds can be calculated as follows:

15 days	One-half of the billing cycle
5 days	Meter reading and bill preparations
10 days	Approximate time before payment is due
30 days	Total

Therefore, ILPI has an average approximately thirty (30) days from the time service is provided until payment is due. With respect to the collection of payments from its customers, it was determined that the time lag from the provision of service to the inflow of cash can be calculated as follows:

15 days	One-half of the billing cycle
18 days	Meter reading, bill preparation and time required to collect the customer's bill without disconnection
5 days	Processing time
38 days	**Total**

Therefore, ILPI waits for an average of approximately thirty eight (38) days before it receives payment for the services provided. Based on ILPI's current billing and collection practices, it appears that the actual net lag days is approximately eight (8) days only (38 less 30) and not the sixty (60) days assumed in the application of the formula. ILPI's customers who do pay on time should not be penalized because other customers failed to comply with ILPI's payment schedule. If additional finance costs are incurred because of late payment of bills, these costs should be recovered in the form of penalties for to the late paying customers and not as additional cash working capital to be paid by all customers.

The adjusted Cash Working Capital allowed by the Commission was computed as follows:

TABLE 21

	Per ILPI	Per ERC
Total O&M (excl.of Purchased Power)	PhP 102,547,517	PhP 88,762,762
Less: Taxes & Non-Cash Items:		
Income Tax	963,469	0
Taxes Other than Income Tax	9,266,366	114,779
Depreciation	26,727,452	26,727,452
Bad Debt	0	1,231,951
O&M-net of cash & non-cash item	PhP 65,590,230	PhP 60,688,580
Cash Working Capital on O & M (2/12)	**PhP 10,931,705**	**PhP 10,114,763**
Purchased Power Cost	PhP 310,423,465	PhP 335,299,564
Cash Working Capital on Power Cost		
2 months	**PhP 51,737,244**	
8 days		**PhP 7,451,101**
Total Cash Working Capital	**PhP 62,668,949**	**PhP 17,565,865**

II.C.6. Other Rate Base Item

The Commission excluded accumulated deferred income taxes amounting to PhP 3,502,200 in the computation of rate base for the reason that income tax is a non-allowable expense as discussed in II.A.5.

II.C.7. Summary of Rate Base

The following tabulates the adjustments made by the Commission in the components of ILPI's rate base:

TABLE 22

	Per ILPI	Per ERC
Net Plant In Service	PhP 181,585,757	PhP 181,585,757
Plant Held for Future Use	8,583,531	0
Materials and Supplies	5,404,714	5,153,162
Cash Working Capital	62,668,949	17,565,865
Other Rate Base Item	(3,502,200)	0
TOTAL RATE BASE	**PhP 254,740,751**	**PhP 204,304,784**

II.D. Rate of Return

The current form of rate regulation practiced for the privately owned electric utilities is a cost based method known as the rate of return on rate base (RORB) methodology. Power rates are set to recover cost of service prudently incurred plus a reasonable rate of return on rate base. The rate of return pertains to the percentage which when multiplied by the authorized rate base, provides a return that will fairly compensate the company for the risk inherent to the investment of capital. This simply means that a regulated utility is allowed to set rates which will cover operating costs and provide an opportunity to earn a reasonable rate of return on the assets utilized in the business.

On the basis of current jurisprudence, the Commission has determined that the 12% rate of return will be maintained in this case but the income tax thereon will not be allowed as operating expense. Thus, the 12% rate of return is a pre-tax rate of return which is equivalent to PhP 24,516,574, computed as follows:

TABLE 23

Adjusted Rate Base	PhP 204,304,784
Rate of Return	12%
Return On Rate Base	PhP 24,516,574

The Commission intends to adopt a new internationally accepted method of rate regulation known as Performance-Based Regulation. The treatment of income tax in this new method may be different from the present RORB method.

II.E. Revenue Requirement Summary

On the basis of the foregoing discussion, the Commission after considering adjustments of PhP (835,858) approved a total revenue requirement of PhP442,704,014 equivalent to an OATA of PhP 0.2013 per kilowatt-hour for ILPI.

TABLE 24

	Per ILPI	Adjustment	Per ERC
Purchased Power	PhP 310,423,465	PhP 24,876,099	PhP 335,299,564
Payroll	24,883,793	0	24,883,793
Operation & Maintenance	49,972,802	(12,821,285)	37,151,517
Depreciation & Amortization	26,727,452	0	26,727,452
Income Taxes	963,469	(963,469)	0
Return on Rate Base	30,568,890	(6,052,316)	24,516,574
Other Revenue Item	0	(5,874,887)	(5,874,887)
Total Revenue Requirement	**PhP 443,539,872**	**PhP (835,858)**	**PhP 442,704,014**
Adjusted Revenue (2000)			**413,383,310**
Increase(Decrease)			**29,320,704**
Annualized kWh Sales			**145,646,948**
Required Increase per kWh			**P0.2013**

The overall average tariff adjustment (OATA) is a measurement tool based on the formula: (Total Revenue Requirement less Existing Revenue) divided by kilowatt-hour sales). This measurement is not meant to refer to any specific customer class. ILPI proposed an OATA of P0.3181 per kilowatt-hour.

II.F. Adjusted Operating Revenue

The Commission adjusted ILPI's actual total operating revenue to PhP413,383,310, computed as follows:

TABLE 25

ILPI's actual operating revenue	PhP 397,658,798
Add/(Deduct)	
Franchise Tax	(9,151,587)
Addtl. Revenue due to increase	24,876,099
Increase in power cost	
Total Adjusted Operating Revenue	**PhP 413,383,310**

II.G. Billing Determinants and Customer Class Allocation

The Commission believes that any energy related cost should be allocated based on the annualized sales. The Commission annualized sales by multiplying year-end number of customers by average annual kWh usage for each customer class. This was performed to project for the future kWh sales for the development of more appropriate allocation factors and billing determinants for each customer class. Based on the annualized sales per customer class, the computed adjusted kilowatt-hour sales were 145,646,948.

The Commission opines that in theory, the most appropriate way to allocate costs among customer classes is based on cost causation characteristics. Thus, the Commission intends, through future proceedings to move even further towards uniform definitions of customer classes based on cost causation characteristics. However, the Commission believes that such a change would best be accomplished through the issuance of guidelines of general applicability to all utilities. Furthermore, R.A. 9136 requires identification and removal of interclass cross-subsidies. Substantive change in customer classes at this time prevents precise calculation of cross-subsidy in existing rates. Therefore, no changes in customer class allocations are ordered for ILPI at this time.

II.H. Design and Calculation of Charges

II.H.1. Generation Charge

Consistent with the Decision in ERC Case No. 2001-901 dated June 26, 2002 and Commission's Orders dated September 6 and 20, 2002 as well as the Commission's Order in ERC Case No. 2003-44, (GRAM) dated May 15, 2003 and ERC Case No. 2003-498 (ICERA) dated December 4, 2003. The generation charge to be billed to end-users shall be the approved rate per kilowatt-hour including Franchise Charge and Foreign Exchange Rate Adjustment (FOREX). The Commission authorized NPC and PSALM to implement effective December 2003 billing ICERA Rate of PhP 0.2207 per kWh for Mindanao.

The Commission rejects the formula proposed by ILPI for generation charge. The NPC's approved rate will remain fixed until changes are authorized by the Commission. This eliminates the need for future Purchased Power Adjustment (PPA).

The Commission has developed a new recovery mechanism designed to replace the purchased power adjustment clauses being used by the power utilities. The Commission has promulgated the Implementing Guidelines on the Generation Rate Adjustment Mechanism (GRAM) effective February 24, 2003. In view thereof, the Commission does not foresee the need for the Purchased Power Adjustment (PPA) clause. Towards this end, the Commission hereby directs ILPI to discontinue implementation of its Purchased Power Adjustment Clause (PPA) upon effectivity of the herein approved unbundled rates.

II.H.2. Transmission Charge

The Commission's decision in ERC Case No. 2001-901 and Order dated September 20, 2002 fixed the transmission charges for the National Transmission Corporation (TRANSCO) without any provision for automatic adjustment thereof. Since the transmission rates to be paid by ILPI are fixed, it is the decision of the Commission to likewise fix the unbundled transmission rates billed to end-use customers.

The transmission charge shall be billed on a fixed rate per kilowatt-hour for Residential, Commercial and Streetlights end-users. In the case of Industrial and Bulk Power with demand meters, the transmission charge shall be billed using a combination of a fixed rate per kilowatt (kW) and a rate per kilowatt-hour (kWh).

In consonance with the gradual phase-out of the intra-grid subsidies being billed by TRANSCO, the Commission hereby sets the transmission charges for the succeeding years, as follows:

TABLE 26

Period	Charges	Flat Rate	Residential	Commercial	Industrial	Bulk Power
Oct.2003 to	Demand (kW)				171.43	145.22
Sept. 2004	Transmission (kWh)	0.8335	0.8335	0.8335	0.6946	0.2917
Oct.2004 to	Demand (kW)				170.11	144.10
Sept.2005	Transmission (kWh)	0.8271	0.8271	0.8271	0.6892	0.2894
Oct.2005 to	Demand (kW)				168.80	142.99
Sept. 2006	Transmission (kWh)	0.8207	0.8207	0.8207	0.6839	0.2872

II.H.3. System Loss Charge

The Commission defines System Loss for utilities to include 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. The system loss charge shall vary from one customer class to another depending on their respective contributions to the system loss. The allowed system loss is equal to the actual system loss for the test year or the existing system loss cap prescribed in R.A. 7832 whichever is lower.

The Commission believes that the present cap on System Loss of 9.5% 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 actual system loss or cap of 9.5% plus 1% of company use or actual whichever is lower shall be deducted from total power cost and to be billed separately as System Loss Charge.

II.H.4. Distribution Charge

The distribution charge shall be billed on a fixed rate per kilowatt-hour (kWh) for Residential and Commercial end-users. In the case of Bulk Power and Industrial customers, the distribution charge shall be billed using a combination of a fixed rate per kilowatt (kW) and a rate per kilowatt-hour (kWh).

Relevant to distribution charge, ILPI proposed distribution wheeling rates comprised of its proposed distribution and supply charges. 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 in the Rate Schedules be likewise utilized as Distribution Wheeling Charges available to the future contestable market.

The Commission's decision to allow a distribution utility to avail of the Distribution Wheeling Charges of another distribution utility is based on general intent of R.A. 9136 to promote a competitive generation market. Distribution utilities that currently or in the near future 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. Distribution utilities are, therefore, prohibited from bundling or tying the sale of generation or purchased power with the sale of unbundled distribution wheeling service.

II.H.5. Metering and Supply Charges

ILPI proposed a peso per month per customer for the metering and supply functions for all customer classes. The Commission acknowledges that cost-causation rate design principles suggest the recovery of customer-related costs through fixed monthly charges. In addition to this cost of service principle, however, the Commission must also consider rate design impacts across the spectrum of customers within each rate class. Although RA 9136 requires the removal of inter-class cross subsidies, the law does not require removal of intra-class cross-subsidies.

Therefore to mitigate the impact on below-average consumption of residential end-users, the Commission orders ILPI to use a combination of peso per customer per month and per kilowatt-hour for the metering function. All other end-users shall be billed a fixed monthly customer charge for both metering and supply functions.

II.H.6. Franchise Taxes

Franchise taxes shall appear as a separate line item on the customers' bills. Given this rate design, it is appropriate to remove test year amounts associated with franchise taxes from the revenue requirement used to calculate other recurring electricity rates.

Pending issuance of guidelines on this issue by the Department of Finance (DOF), ILPI is in the meantime directed to use the formula below in calculating franchise taxes.

Franchise Tax:

Total Power Bill x FTx1,y

Where: FTx = National franchise tax of 2%
Fty = Applicable local franchise tax

II.H.7. Flat Rate Service (Schedule Nos. 11 & 12)

The Commission rejected the proposed twenty-four (24) hours per day duration of Flat Rate Service under Schedule Nos. 11 and 12 and directed ILPI to continue to bill the said schedule in its original twelve (12) hours per day duration.

II.I. Cross Subsidy Removal

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

TABLE 27

	Total	Flat Rate	Residential	Commercial	Industrial	Bulk Power
New Cost-Based Revenue	442,704,014	1,580,297	179,255,775	162,001,913	29,243,694	70,622,335
Existing Rates Revenue	413,383,310	1,583,729	154,098,581	154,152,545	26,385,480	77,162,973
Total Change in Revenue	29,320,704	(3,432)	25,157,194	7,849,368	2,858,213	(6,540,639)
Percentage Change in Rev.	7.09%					
Normalized Revenue	442,704,014	1,696,061	165,028,580	165,086,371	28,256,966	82,636,036
Inter-class Cross Subsidy	(0)	115,764	(14,227,195)	3,084,458	(986,728)	12,013,701
Class Billing Determinants (in kWh)	145,646,949	520,558	49,934,060	50,223,836	8,045,875	36,922,620
Inter-class Cross Subsidy Rates (PhP/Kwh)	0	0.2224	(0.2849)	0.0614	(0.1226)	0.3254

Section 74 of R.A. 9136 and Rule 16 Section 16, Section 5 of the Implementing Rules and Regulation thereof provide that 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 extendible for a maximum period of one (1) year subject to certain conditions.

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

II.J. Lifeline Rate

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 rate.

In determining the lifeline level of consumption to be provided to the marginalized end-users, the Commission calculated the probable load requirement of typical low-income consumers by two (2) lighting facilities at 20 watts each and a 50-watt Radio that are being used at reasonable number of hours. Thus, the Commission sets the lifeline consumption maximum level of 100 kilowatt-hours for ILPI. 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 ILPI. The graduated scale is also based on the recognition that individual end-user consumption may likely vary from month to month.

TABLE 28

KWh Consumption	% Lifeline Discount
40 kWh below	50%
41-50 kWh	45%
51-60 kWh	40%
61-70 kWh	35%
71-80 kWh	30%
81-90 kWh	20%
91-100 kWh	10%

ILPI 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 100 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 ILPI, the lifeline discounts result in a Subsidy on Lifeline by other end-users equal to PhP 0.0816/kWh.

II.K. Non-Recurring Rates

ILPI's existing charges for other services 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 ILPI.

Said charges are hereby pegged at their existing levels until such time that the Commission sets new rates on the same. Further, ILPI is ordered to make a compliance filing on its charges for other services a year from the date of this Decision using a format to be prescribed by the Commission.

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

II.L. Estimated Impact on Average Residential Consumer

A comparison of the estimated impact of all adjustments on the revenue requirement on the monthly bill of a residential end-user consuming 140 kWh a month using rates based on ILPI's actual existing rates as of November 2003 against the unbundled rates approved by the Commission is shown below:

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TABLE 29

RESIDENTIAL Consuming 140 kWh	Peso/kWh	Amount		Peso/kWh	Amount
Basic Charge:	1.4795	207.13	Generation Charge	1.2751	178.51
			Transmission Charge	0.8335	116.69
			System Loss Charge	0.3046	42.64
PPA	1.6202	226.83	Distribution Charge	0.6217	87.04
Power Act Reduction	(0.30)	(42.00)	Supply Charge	0.2705	37.86
			Metering Charge:		
			Retail Customer Charge/Mo.	5.00	5.00
			Metering System Charge	0.1183	16.57
			Inter-Class Cross Subsidy Charge	(0.2849)	(39.89)
			Subsidy on Lifeline	0.0816	11.42
			Power Act Reduction	(0.30)	(42.00)
Universal Charge	0.0398	5.57	Universal Charge	0.0398	5.57
SUB TOTAL		397.53	SUB TOTAL		419.42
			Franchise Tax 2.5%		10.35
TOTAL BILL		397.53			429.77
Ave. Rate/kWh		2.8395			3.0698
Inc./(Dec.) In Rate					0.2303
Inc./(Dec.) In Bill					32.24

DISPOSITION

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

1. To approve the unbundled schedule of rates of ILPI, to be effective on the next billing cycle after the date of this Decision, to wit;

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ILIGAN LIGHT & POWER INC. (ILPI)
ERC CASE NO. 2001-893
RATE SCHEDULE

		TYPE OF CONSUMERS				
		Flat Rate (220 V)	**Commercial** (220V)	**Residential** (220V)	**Industrial** (13.8 kV)	**Bulk Power** (60 kV)
Generation Charge	PhP/kWh		1.2751	1.2751	1.2751	1.2751
	PhP/Watt	0.4590				
Transmission Charge	PhP/kWh		0.8335	0.8335	171.43	145.22
	PhP/kW				0.6946	0.2917
	PhP/Watt	0.3001				
Distribution Charge	PhP/kWh		0.6217	0.6217	0.3531	0.0213
	PhP/kW				87.15	10.59
	PhP/Watt	0.2238				
Customer Charges						
Supply Charge	PhP/Cust./Mo.	37.43	37.43		37.43	37.43
	PhP/kWh			0.2705		
Metering Charge	PhP/Meter./Mo.	0	60.97	5.00	1,014.91	2,185.93
	PhP/kWh			0.1183		
System Loss Charge	PhP/kWh	0.1097	0.3046	0.3046	0.2375	0.0103
	PhP/Watt					
Inter-Class Cross Subsidy	PhP/kWh		0.0614	(0.2849)	(0.1226)	0.3254
	PhP/Watt	0.0801				
Lifeline Rate Subsidy	PhP/kWh	0.0294	0.0816	0.0816	0.0816	0.0816
	PhP/Watt					
Universal Charge	PhP/kWh		0.0398	0.0398	0.0398	0.0398
	PhP/Watt	0.0143				

Note: Plus National and Local Franchise Taxes

2. To approve ILPI's net utility plant in service at sound value as of December 31, 1997 amounting to PhP 185,517,900.

3. To direct ILPI to comply with the following:

   a) To discontinue charging the PPA upon effectivity of the approved unbundled rates; any change in the cost of power purchased shall be reflected as deferred charges or credits which shall be recovered through the Generation Rate Adjustment Mechanism (GRAM) approved by the Commission for implementation per ERC Order effective February 24, 2003;

   b) To bill its respective end-users using a billing format which contains at least the rate elements provided in Annex A (Rate Schedule) of this Decision upon effectivity of the approved unbundled rates;

c) To bill its respective end-users using a billing format which contains at least the rate elements provided in Annex B of this Decision upon effectivity of the approved unbundled rates. The rate elements provided in Annex B should appear on the end-users' bills even if the rate elements currently have a rate of zero (0) or have not yet been determined by the Commission;

d) To set up a depreciation fund each year corresponding to the whole amount of depreciation that it has recorded on its books. The setting up of this fund should be done on a monthly basis corresponding to the monthly depreciation. ILPI is required to strictly account for the expenditures out of this fund which should be used strictly for investment in electric plant and all withdrawals from this fund should be reported to the Commission within thirty (30) days from withdrawal;

e) To 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 Availments from the Universal Charge the Share for Missionary Electrification, NPC-SPUG, Applicant);

f) To bill PhP 0.0025/kWh representing the environmental portion of the Universal Charge in accordance with the Commission's Decision 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);

g) To adequately inform the end-users within its franchise area of the approved unbundled rates not later than thirty (30) days after receipt of this Decision;

h) To submit for verification and confirmation purposes on or before the twentieth (20th) day of the month following the effectivity of the herein approved unbundled rates and every month thereafter: (a) copy of bills from the generation and transmission companies; and (b) M-001 and M-002 with all related schedules; and

i) Make a compliance filing with respect to its Other Charges a year from date of this Decision.

SO ORDERED.

Pasig City, December 22, 2003.

MANUEL R. SANCHEZ
Chairman

OLIVER B. BUTALID
Commissioner

LETICIA V. IBAY
Commissioner

CARLOS R. ALINDADA
Commissioner

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