

Republic of the Philippines
ENERGY REGULATORY COMMISSION
Pasig City

**IN THE MATTER OF THE
PETITION TO INITIATE
RULE-MAKING FOR THE
SUSPENSION OF ERC
RESOLUTION NO. 07,
SERIES OF 2021 AND THE
ADOPTION OF THE
PROPOSED RULES ON THE
IMPOSITION OF
SECONDARY PRICE CAP**

ERC CASE NO. 2023-008 RM

**PHILIPPINE INDEPENDENT
POWER PRODUCERS
ASSOCIATION, INC.,**
Petitioner.

Promulgated:
December 07, 2023

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NOTICE OF PROPOSED RULE-MAKING

TO ALL INTERESTED PARTIES:

Notice is hereby given that, on 17 October 2023, Philippine Independent Power Producers Association Inc. (PIPPA) filed a *Petition*, dated 16 October 2023, to initiate rule-making for the suspension of the Commission's Resolution No. 07, Series of 2021¹ (Resolution No. 07) and the adoption of the proposed rules on the imposition of secondary price cap.

In its *Petition*, PIPPA alleged the following pertinent provisions:

PREFATORY STATEMENT

1. On 27 December 2013, the Wholesale Electricity Spot Market ("WESM") Tripartite Committee - composed of the Department of Energy ("DOE"), the Energy Regulatory Commission ("ERC"), and the Philippine Electricity Market Corporation ("PEMC") - set the offer price ceiling of

¹ Entitled, "Amendments to the Pre-Emptive Mitigating Measure in the Wholesale Electricity Spot Market (WESM)".

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Php32,000.00 per megawatt-hour (MWh), through the issuance of Joint Resolution No. 2, entitled "*Adjustments to the Wholesale Electricity Spot Market Offer Price Cap*". This is a reduction from the previous price cap of Php62,000.00/MWh imposed in WESM Tripartite Joint Resolution No. 2 issued in June 2006.

2. Pending amendment of the offer price cap, the ERC imposed a Secondary Price Cap ("SPC") in the WESM, through ERC Resolution No. 8, Series of 2014. Under said resolution, the ERC:
 - a. Imposed the SPC in the amount of Php6,245.00/MWh for the supply months of May and June 2014, upon breach of the Generator Weighted Average Price (GWAP) over a rolling seventy-two (72) hour period on the threshold of Php8,186.00/MWh;
 - b. Declared that the GWAP rolling average shall remain in effect until the succeeding GWAP rolling average is already less than the said threshold.
3. The pre-emptive mitigating measures and the SPC under ERC Resolution No. 8, Series of 2014 were initially implemented as interim mitigating measures. The ERC, however, subsequently issued several resolutions which extended, and later made permanent, the interim mitigating measures and the SPC of Php6,245/MWh.
4. Through the issuance of ERC Resolution No. 13, Series of 2014, the ERC extended the SPC's implementation until 09 August 2014. The same SPC was further extended until 08 December 2014 under ERC Resolution No. 14, Series of 2014. Eventually, the SPC was implemented as a permanent mitigating measure in the WESM through ERC Resolution No. 20, Series of 2014, which provides for a permanent pre-emptive measure with the same value as the SPC upon breach of the Cumulative Price Threshold ("CPT") of Php1,512,028.00 over a rolling seven (7) day period or an average CPT per hour of Php9,000.00/MWh.
5. On 09 May 2017, the ERC issued Resolution No. 4, Series of 2017, which recalculated the threshold level at One Million Eighty Thousand Pesos (Php1,080,000.00) equivalent to the GWAP over a rolling five (5)-day period, instead of seven (7) days. The average CPT, however, remained at Php9,000/MWh.
6. The ERC thereafter issued ERC Resolution No. 7, Series of 2021, which adopted a shorter rolling average period to three (3) days, and determined a regional/ island SPC mechanism to be applied when the grid interconnection is on outage: Luzon - Php5,249/MWh, Visayas - Php2,837/MWh, and Mindanao - Php3,074/MWh.

7. To note, ERC Resolution No. 7, Series of 2021 did not change the values of the SPC, which remains at PhP6,245/MWh, and the CPT, which stays at PhP9,000/MWh.
8. With this, Petitioner, representing its Member Generating Companies, consistently raised its position and concerns relating to the implementation of the SPC through several correspondences and conferences with the ERC.
9. Petitioner respectfully submits that there is a need to rescind and/or suspend the implementation of the SPC and to adopt a new set of rules for the imposition of the SPC.

NATURE OF THE PETITION

10. This is a Petition to Initiate Rule-Making under Rule 21 of the Revised Rules of Practice and Procedure of the ERC (the "ERC Procedural Rules") for the suspension of the Pre-Emptive Mitigation Measure in the WESM under ERC Resolution No. 07, Series of 2021.
11. Pursuant to Section 2, Rule 21 of the ERC Procedural Rules, interested persons may petition the Honorable Commission to adopt, amend, or repeal a rule, to wit:

Section 2. Petition to Initiate Rule-making. - Interested persons may petition the Commission to adopt, amend, or repeal a rule by filing a petition to initiate rule-making. The petition must contain the name, address, and e-mail address of the petitioner, the specific rule or action requested, the reasons for the rule or action requested, and facts showing that the petitioner has a substantial interest in the rule or action requested. (Underscoring supplied)

PARTY TO THE PETITION

12. Petitioner is a domestic corporation duly organized and existing under and by virtue of Philippine laws, with principal office at Unit 2408, 24th Floor, Prestige Tower, F. Ortigas Jr. Road (formerly "Emerald Avenue"), Ortigas, Pasig City. It may be served pleadings, orders, and other legal process through the undersigned counsel at SYMECS Law, 3109 One Corporate Center, Julia Vargas corner Meralco Avenue, Ortigas Center, Pasig City; or through Petitioner's e-mail address at pleading&@symecslaw.com.²
13. Petitioner is a professional organization of independent power producers. It represents its members that are engaged

² A copy of the Secretary's Certificate authorizing the undersigned to file the instant Petition on behalf of Petitioner is attached as Annex "A" of the *Petition*. A copy of Petitioner's Certificate of Filing Amended Articles of Incorporation and Amended Articles of Incorporation are attached as Annexes "A-1" and "A-2", respectively of the *Petition*.

in power generation and are covered by the Pre-Emptive Mitigating Measure in the WESM. Thus, Petitioner has substantial interest in initiating this Petition, pursuant to Rule 21 of the ERC Procedure Rules.

ARGUMENTS

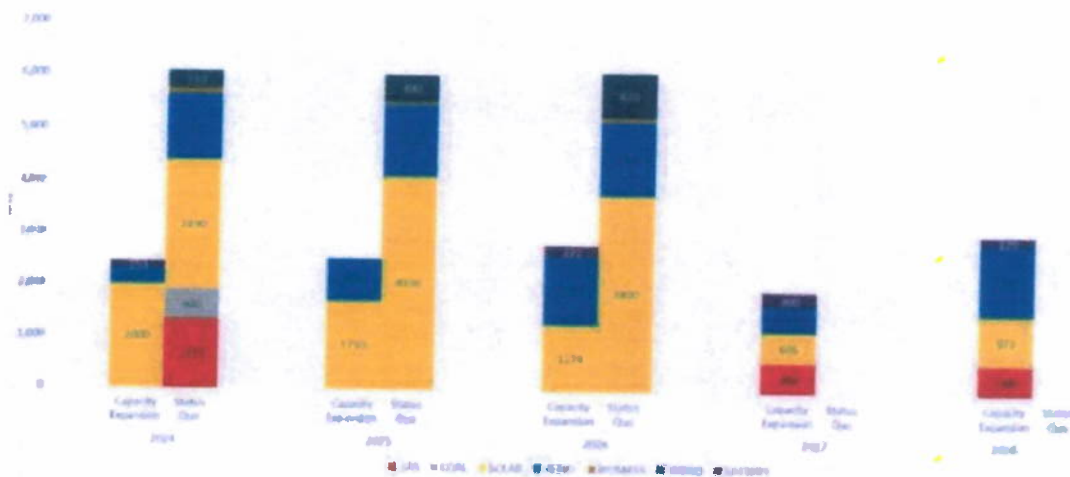
- I. *Any regulation on price control should have a defined process, and appropriate inclusion of its determination under the WESM Rules.*
14. The ERC resolutions issued did not contain clear and definite guidelines and conditions that can be followed when setting the CPT and SPC in the WESM. The resolutions of the ERC directly set the value of the CPT, SPC, and the rolling average days, without providing for conditions that must be fulfilled when determining the values.
15. To illustrate, ERC Resolution No. 20, Series of 2014 only states the following information:
 - a. That the CPT is set to Php 1,512,028, based on the GWAP over a rolling seven (7)-day period or one hundred sixty-eight (168)- hour trading interval, and equivalent to an average spot price of Php9,000/MWh over the period;
 - b. That the breach of the CPT will trigger the imposition of a price cap amounting to Php6,245/MWh; and
 - c. If the price cap is imposed and the market clearing price goes lower than the price cap, the market clearing price will be applied.
16. A Discussion Paper on the Pre-emptive Mitigation Measure was also attached as Annex A to the said ERC Resolution. The discussion paper included a summary of secondary price cap impositions in other jurisdictions. It also stated how the proposed CPT and secondary price cap for the WESM were arrived.
20. (*sic*) The discussion paper, however, is not a rule that can be revised; the only rule available for revision is the value of the CPT, hours of rolling average and SPC.
21. The latest resolution amending the SPC is ERC Resolution No. 7, Series of 2021, which also does not include any rules on the determination of the CPT, rolling average days and SPC.
22. Petitioner proposes that a new set of rules on the imposition of the SPC be issued, that includes specific parameters and processes in updating the values of the SPC and CPT. The Proposed Rules on the Imposition of the SPC ("Proposed

Rules") is herein attached as Annex "B" of this Petition, and should form part of the WESM Rules.

23. Under the Proposed Rules, Petitioner proposes that the SPC be set at PhP9.8526/kWh, which is calculated using the levelized cost of energy ("LCOE") for the best new entrant of a peaking plant. The parameters and the base value for the computation of the LCOE is found at Section 7, Article III of the Proposed Rules.
 24. Meanwhile, Petitioner advocates that the CPT value shall be PhP13,657.38/MWh. The CPT value is derived using the values of the following:
 - a. Year to date 2022 WESM Price and Load Weighted Average Price (LWAP) using Pagbilao Node;
 - b. 24 hours per day was divided into (i) First-off peak - 9 hours, (ii) Peak - 9 hours, (iii) Price Spike - 3 hours, (iv) Second-off Peak-3 hours;
 - c. For the Price Spike, Php32,000/MWh was assigned;
 - d. The corresponding LWAP was assigned to the specific number of hours in a day and was averaged; and
 - e. The hourly CPT was then derived.
 25. Thus, Petitioner urges the ERC to adopt the proposed SPC and CPT values, and the conditions used to determine the values, as part of the WESM Rules.
- II. The current SPC value should be rescinded, as it discourages participants in the energy sector to build new plants, contrary to the mandate of the ERC to promote competition under the Electric Power Industry Reform Act ("EPIRA").
26. Under Section 43 of the EPIRA, the ERC is mandated to promote competition in the restructured electricity industry by monitoring the activities in the generation and supply of the electric power industry.
 27. With due respect, the SPC value of PhP6,245/MWh discourages energy participants from building new power plants. The current value fails to encourage fair competition since the SPC does not provide enough incentive for power players to recover expenses from building plants and to realize reasonable gains. The SPC affects not only peaking plants, but baseload capacities as well.

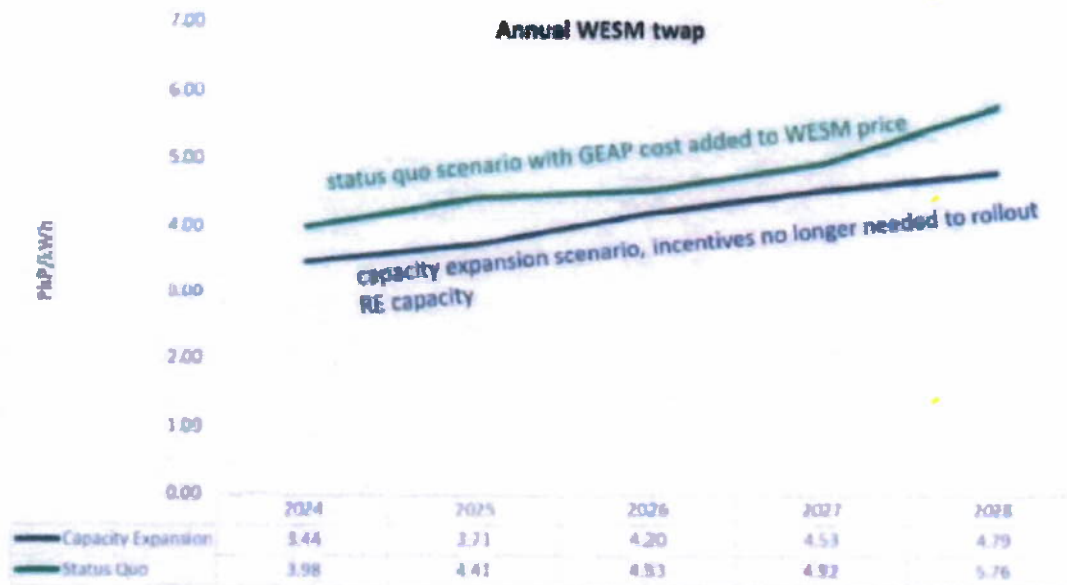
28. Since the current SPC value acts as a deterrent for new players in the power industry, maintaining the SPC value of Php6,245/MWh runs contrary to the mandate of the ERC under the EPIRA to promote competition in increasing the power supply.
29. Petitioner understands that the SPC intends to protect consumers in the short term, in that it insulates consumers from extreme price volatilities in the WESM. Petitioner submits, however, that in the long run, maintaining the current SPC value could produce pervasive adverse effects on energy security.
30. Part of the study on the Proposed Rules was a simulation conducted to determine the effect of removing the SPC and its effect on the WESM prices. The study likewise looked into the capacity addition that will result due to the unconstrained market prices from said removal of the SPC.
31. Figure 1 shows an additional capacity of 2,886MW by 2028, should the SPC be removed. The status quo capacity addition no longer shows the increase in capacity as this is dependent on the Green Energy Auction Program (GEAP) as well as Competitive Selection Process (CSP) of Distribution Utilities (DUs).

Figure 1. Capacity Roll Out



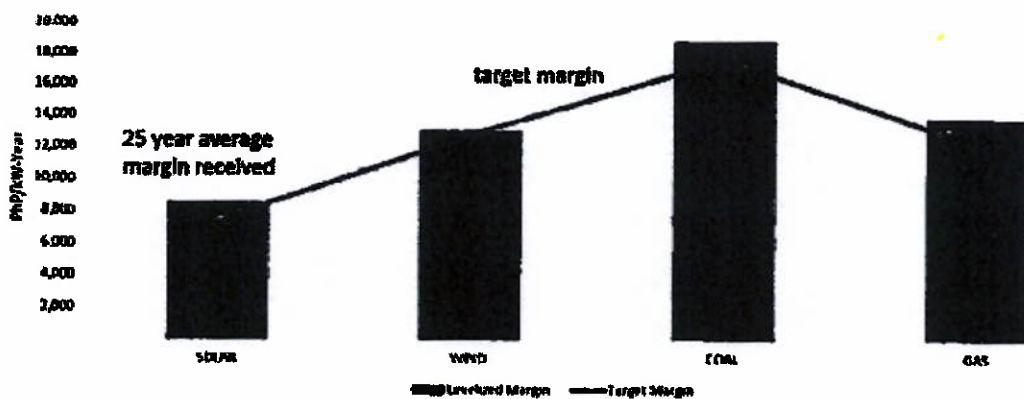
32. The projected WESM price for 2028, with the removal of the SPC, is at Php4.79/kWh as shown in Figure 2. Figure 2 further illustrates the impact of the inclusion and exclusion of the SPC and the GEAP cost to WESM prices. Under status quo scenario where the GEAP cost is included, the WESM prices are comparatively higher than the proposed capacity extension scenario where the SPC and the GEAP costs are removed from WESM prices. The capacity expansion scenario shows that RE capacity can naturally recover from the spot market.

Figure 2. WESM Prices with the removal of the SPC



33. The higher prices under the status quo scenario are caused by the limitation of investments in baseload plants, instead, only the Variable Renewable Energy ("VRE") sources from GEAP are able to increase supply. On the other hand, the removal of the SPC under the capacity expansion scenario will create and/or result in merchant opportunity for renewable energy, with a weighted average cost of capital ("WACC") of 11.3%, and gas, with a WACC of 13%, within the corresponding twenty-five (25)-year capture gross margin, as shown in Figure 3.

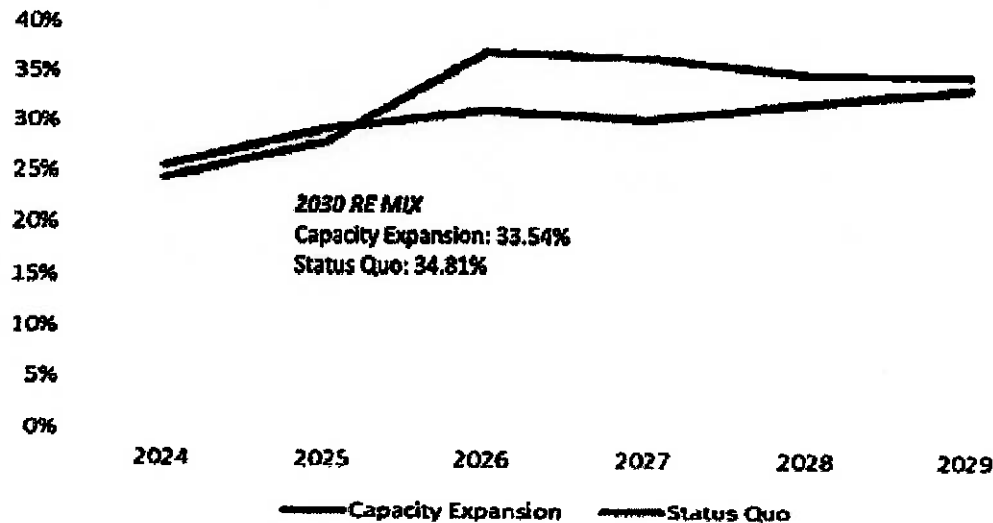
Figure 3. Target Margin vs. Levelized Margin (Php/kW-Year)



34. It must be emphasized that the study does not discriminate against RE technology. The capacity expansion scenario will, in fact, help attain the target RE share of thirty five percent (35%), without the need for add-on costs to the grid, which would then display a smoother RE roll out. The lump sum capacity additions in the early years would have implications

in grid operations (e.g., need for higher ancillary services at the onset).

Figure 4. RE Mix by 2030 - Capacity Expansion vs Status Quo



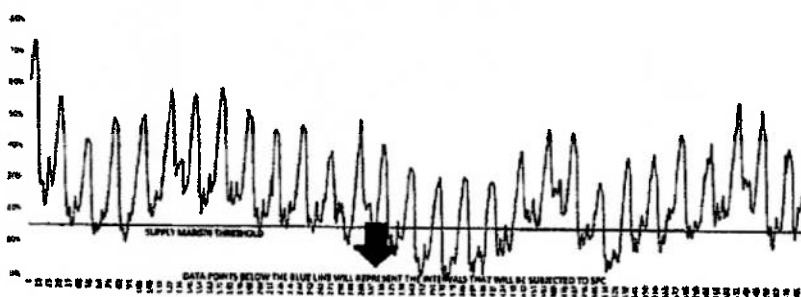
35. The results from the above simulation gives a conclusion that price caps do not necessarily work for the benefit of consumers. In the long run, the price caps deprive consumers of a secure and stable power supply and lower WESM prices arising from competition pressure due to the entry of more investors.
- III. Without prejudice to Petitioner's position on rescinding the SPC altogether, the current values for CPT, SPC and hours of rolling average should at least be amended.
36. Without prejudice to Petitioner's position that the SPC should be rescinded, the Petitioner created a technical working group ("TWG") among its members to update the SPC based on the prevailing market conditions.
37. The study of the TWG proposes a PhP9,8526/MWh SPC based on the levelized cost of energy ("LCOE") for Best New Entrants ("BNE"). Petitioner further identified three (3) conventional BNEs for peaking, mid-merit and baseload.
38. Petitioner proposes that the Supply Margin shall be the primary indicator of the tightness of electricity supply and extraordinary events in the grid. The calculation of the CPT and the eventual implementation of the SPC shall be primarily triggered when the Supply Margin breaches lower than the threshold of fifteen percent (15%). For avoidance of doubt, the CPT shall not be calculated by the Market Operator if the Supply Margin is still equal to or above the Supply Margin threshold.

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39. The Supply Margin threshold shall be computed through the following formula:

$$\text{SUPPLY MARGIN (SM) (\%)} = \frac{\text{TOTAL SUPPLY OFFERS} + \text{PRIORITY \& MUST DISPATCH RES}}{\text{DEMAND}}$$

40. Below is a sample illustration on how the Supply Margin was calculated during the October 2022 period.



Note that Supply Margin is calculated per interval, separate for each of Visayas and Luzon Grids.

41. Petitioner, thus, recommends adopting a fifteen percent (15%) threshold level which is based on the total ancillary services requirement divided by the peak demand for Luzon. The result of the supply margin is $15\% = (480\text{MW RR} + 668\text{MW CR} + 668\text{MW DR}) / 12000\text{MW}$.³
42. Additionally, Petitioner has calculated and arrived at the proposed CPT level of PhP13,657.29/MWh using the 2022 YTD Load Weighted Average Price (LWAP).
43. Petitioner further advocates increasing the rolling average hours to one hundred sixty-eight (168) hours from seventy-two (72) hours when calculating the CPT.
44. To recall, ERC Resolution No. 20, Series of 2014 initially imposed a seven (7)-day rolling average in the calculation of CPT. Petitioner posits that a period of seven (7) days, instead of the three (days) under ERC Resolution No. 7, Series of 2021, is a more appropriate period to consider as the trigger mechanism of the SPC. A more detailed calculation of the CPT is included under the Proposed Rules.
45. Moreover, Petitioner urges that the SPC be calculated using the LCOE for a BNE of a peaking plant. For the purpose of setting the SPC, the BNE for peaking plants is determined to be an LNG single cycle gas turbine. Parameters for the calculation of LCOE shall be as follows:

³ Where "RR" refers to Regulating Reserve, "CR" refers to Contingency Reserve, and "DR" refers to Dispatchable Reserve.

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Parameters	Base Value
Investment Cost, USD/kkWh	713
FOM, PhP/kW-year	389.61
VOM, PhP/kWh	0.2505
Type of Fuel	LNG
Fuel Cost, USD/BtuTU	12.8667
Heat Rate (Btu/kWh)	8,000
FX	55.66
Cost of Debt	9.1365%
Cost of Equity	15%
Debt-Equity Ratio	70:30
Economic Life	25
Capital Recovery Fee	114.91
Total LCOE, PhP/kWh	9.8526

- IV. Additional trigger mechanisms should be considered in the implementation of the Secondary Price Cap.
46. The purpose of the SPC is to "establish a pre-emptive mitigation measure to limit the impact of extreme price volatilities and excessive levels of prices in the WESM". However, it is unfortunate that extreme price volatilities and excessive levels were never defined and measured. Most price volatilities may have been normal occurrences and are part of the characteristics of a competitive market.
47. Petitioner proposes the inclusion of an additional mechanism to trigger the SPC. Instead of relying only on the CPT and the number of days of rolling average price, the determination of supply margin should also be considered.
48. Petitioner further proposes that the calculation on the CPT and the roiling average should only proceed if the supply margin is below fifteen percent (15%) of the peak demand for the current month. This additional consideration will separate normal price volatility with the extreme ones.
- V. Pending determination of a more appropriate level of the SPC components of Additional Compensation should include all FOM, VOM and Fuel costs of all affected generators
49. The Independent Electricity Market Operator of the Philippines ("IEMOP") is the Market Operator of the WESM and is in charge of the evaluation and recovery of the

additional compensation of affected generators. IEMOP's current practice of disallowing additional compensation for the items enumerated above results in financial losses to Petitioner's Member Generators which will affect its loan covenants and debt service coverage ratio ("DSCR") compliance.

50. On 23 November 2022, the IEMOP through a letter addressed to the ERC sought to clarify the allowed cost of claims for additional compensation specifically for Variable Operation and Maintenance Items ("VOM").
51. In addition to the above, Petitioner reiterates the request of IEMOP for guidance on how to treat costs that are not considered as part of VOM such as maintenance cost, personnel services, ER 1-94, Market Fees, NGCP ancillary services charges and wheeling charges which are necessary and legitimate costs. Said costs are incurred when the Member Generators are dispatched during market suspension or intervention, must run or constrain on generating units and when price mitigating measures are applied [i.e., the SPC). The situation of delayed compensation again makes the operation of the power plant financially unviable which dampens new investments.

PRAYER

WHEREFORE, Petitioner respectfully prays that this Honorable Commission to:

- a. RESCIND the implementation of ERC RESOLUTION NO, 07, SERIES OF 2021 and any and all issuances related to the imposition of the Secondary Price Cap;
- b. ADOPT the Rules on the Imposition of Secondary Price Cap (Annex B) as herein proposed;
- c. SUSPEND the implementation of ERC RESOLUTION NO. 07, SERIES OF 2021, and any and all issuances related to the imposition of the Secondary Price Cap;
- d. Urgently GRANT all VOM, FOM and fuel components as part of recoverable costs for Additional Compensation mechanism in the WESM.

Other just and equitable reliefs are likewise prayed for.

The Commission has set the *Petition* for hearing and public consultation on the following dates and online platform for the conduct thereof, pursuant to Resolution No. 09, Series of 2020⁴ and

⁴ A Resolution Adopting the Guidelines Governing Electronic Applications, Filings and Virtual Hearings Before the Energy Regulatory Commission.

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Resolution No. 01, Series of 2021⁵ (ERC Revised Rules of Practice and Procedure):

Date and Time	Venue	Activity
19 January 2024 (Friday) at nine o'clock in the morning (9:00 A.M.)	Microsoft Teams Application	Determination of compliance with jurisdictional requirements and expository presentation for Luzon, Visayas, and Mindanao Stakeholders
26 January 2024 (Friday) at nine o'clock in the morning (9:00 A.M.)		Public Consultation for Luzon Stakeholders
02 February 2024 (Friday) at nine o'clock in the morning (9:00 A.M.)		Public Consultation for Visayas Stakeholders
09 February 2024 (Friday) at nine o'clock in the morning (9:00 A.M.)		Public Consultation for Mindanao Stakeholders

All interested stakeholders may submit their comments and/or clarifications (both in hard and soft copies) on the proposed Rule-change on or before **12 January 2024**. Electronic copies may be sent to doCKET@erc.ph, and copy furnish the Legal Service through legal@erc.ph. The Commission shall give priority to the stakeholders who have duly submitted their respective comments and/or clarifications, to discuss the same and propound questions during the course of the expository presentation.

Any interested person may access the copy of the *Petition* and PIPPA's "Proposed Rules on the Imposition of the SPC" on the Commission's official website at www.erc.gov.ph.

⁵ A Resolution Adopting the Revised Rules of Practice and Procedure of the Energy Regulatory Commission.

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Finally, PIPPA, including its authorized representatives and witnesses, are hereby directed to provide the Commission, thru legal.virtualhearings@erc.ph, their respective e-mail addresses upon receipt of this *Order*. The Commission will send the access link/s to the aforementioned hearing platform within five (5) working days prior to the scheduled hearing and public consultation.

WITNESS, the Honorable Commissioners **ALEXIS M. LUMBATAN**, **CATHERINE P. MACEDA**, **FLORESINDA G. BALDO-DIGAL**, and **MARKO ROMEO L. FUENTES**, Energy Regulatory Commission, this 7th day of December 2023 in Pasig City.

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MONALISA C. DIMALANTA
Chairperson and CEO

LS: CNR/LSP/MCCG

