After MERALCO, the country's largest electricity distributor and supplier, announced last April an increase in its generation charges by 51.88 centavos per kilowatt hour (kWh), rumors of a brewing government takeover began spreading like wildfire. Signals are there, experts say, as shares of both the government and the Lopezes each jumped to more than 30%, with the Lopezes having a slight fractional advantage.

The recent government actions to pin down MERALCO and target the Lopezes, however, only serve to narrow the discourse to a simplistic formula: Electricity rates are high; for which MERALCO and the Lopezes are to blame. Meralco is no doubt an easy and guilty target. But there are more reasons for electricity rates in the Philippines being among the highest in Asia. And the Arroyo government is equally to blame, if not more.

10 Reasons Why Electricity Bills Are High

By the Freedom from Debt Coalition

A position paper submitted to the:
Joint Congressional Power Committee (JCPC)

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The Freedom from Debt Coalition (FDC) believes that the issue of high electricity prices is a result of a confluence of factors, from bad governance to corruption to mismanagement to rent-seeking to framework concerns. It is also more complex than what media portrays or what some politicians would want us to believe. We attempt to identify these factors as our contribution to gaining a fuller understanding of the problem of unabated expensive electricity.

FDC argues that the skyrocketing price of electricity emanates from structural, management, policy, governance and paradigmatic causes. FDC believes that these problems cannot be resolved fully without transforming the electricity industry into one that is more responsive and accountable to the people, and more environmentally sustainable. Meanwhile, it would greatly help the consumer for the government to target specific rate-hiking factors and introduce immediate reforms, with the end-in-view of course, of more comprehensive changes sooner rather than later.

We believe electricity is expensive because of the following:

1. **The Energy Regulatory Commission (ERC) allows MERALCO, other distribution utilities (DUs) and the National Transmission Commission (Transco) to earn over and above what used to be the statutory return on rate base of 8-12%.** The Electric Power Industry Reform Act (EPIRA) allowed ERC to change the system of tariff setting, and it did. But the systems it now follows allows both transmission and distribution companies to earn far more than what they were allowed to earn in the past. And as far as generation and supply companies are concerned, the ERC has little if any say in the prices they charge because generation and supply are deregulated under EPIRA.

2. **The Arroyo government wants to attract private investors to purchase NPC's assets, and for the assets to become attractive, electricity rates have to be high.** The higher the winning bidder bids, the higher the electricity price we have to pay in the future so the winning bidder can recover its investment.

   This can be observed with the nature of recent electricity rate hikes. Following the suggestion of the Asian Development Bank (ADB), the National Power Corporation (NPC) petitioned rate hikes in order to attract investors since no investor would invest without proof of financial viability. Out of the PhP1.98/kWh NPC petitioned in 2004, PhP1.03/kWh was approved by ERC in 2005 – the highest rate hike in the history of the ERC. Transmission charges also increased from PhP0.7716/kWh in May 2006 to PhP0.9163/kWh in July 2006 (which is contrasted with almost flat prices from November 2005 up to May 2006) as the privatization and the bidding process is about to start.

3. **The Arroyo government did not renegotiate the contracts with NPC's independent power producers or IPPs.** These contracts require NPC to purchase electricity whether or not these are actually generated or dispatched, and to supply fuel to IPPs that are in operation. The price NPC agreed to pay for this electricity was overstated to begin with, and many of these contracts have clauses that allow the IPP to raise rates over time. NPC also bears the risk of peso devaluation and the risk of the cost of fuel, such as oil and coal, going up.

   We have been paying for these contracts in our electric bills for over a decade, and we continue to pay for these today, although this is less transparent, thanks to unbundling. With world oil and coal prices hitting all time highs, with the peso now at PhP40 to the dollar compared with PhP26:$1 when these contracts were signed, the cost of these contracts are an excessive burden on ordinary Filipino electricity consumers. Even consumers that do not have electricity at home are also made to pay for these contracts because the government guarantees all of NPC's obligations to the IPPs.

4. **EPIRA allows MERALCO to purchase at most half of its electricity requirements from its sister companies or IPPs.** Besides the problem of NPC with the IPPs, we have the problem of MERALCO's contracts directly with its own IPPs. EPIRA also allows cross ownership between generation and distribution. A closer look at the ownership of most of MERALCO's IPPs will show that they are owned by the Lopezes. Examples include the Santa Rita, the San Lorenzo Natural Gas, and the Quezon Coal-fired Power Plants. Whatever guarantees the government gives to its IPPs, MERALCO also gives to its IPPs. MERALCO has always claimed that it doesn't earn from the high generation charges of its IPPs, and that it is merely passing on to its IPPs whatever it charges its customers for generation. MERALCO is telling the truth. But that is not the entire picture. For while MERALCO doesn't itself earn from the high generation charges of its IPPs, the Lopezes do. A simple review of the financial statements of the Lopez holding company and its generation companies will show this.

   This results to a clear case of double-whammy for the consumers. At one end, NPC must still pay for the unsold electricity it gets from IPPs because of the take-or-pay provision – an undue costs which will later be part of NPC's stranded cost to be passed on later to the consumers.

At the other end, MERALCO pays its IPPs more than what it would have paid NPC, if it bought the electricity from NPC during the same hours that MERALCO was buying from its IPPs. As NPC rates vary from hour to hour, becoming more expensive when demand for electricity peaks, we must compare on an hourly basis what MERALCO pays its IPPs with what it would have paid NPC if it bought electricity from NPC instead of its IPPs.

Fortunately during the May 6, 2008 dialogue at the ERC, members of FDC and EmPower Consumers were able to obtain a copy of Meralco's electricity suppliers and their respective cost and share for the months of March and April. Data shows that the cost of power from Meralco's IPPs is higher than that of NPC's.

Supplier	**March 2008**		**April 2008**		**Increase / Decrease**	
	Feb '08 cost	Energy Share	Mar '08 cost	Energy Share	Cost	Energy Share
NPC and WESM	4.8673	42.13%	5.3692	45.11%	0.5020	2.98%
NPC	**4.5231**	**31.87%**	**4.0173**	**35.96%**	**(0.5058)**	**4.09%**
WESM	5.9356	10.27%	10.6822	9.15%	4.7466	-1.12%
Major IPPs	4.0588	57.84%	4.5496	54.87 %	0.4908	2.98%
QPPL	**3.7253**	**12.28%**	**6.4340**	**6.87%**	**2.7088**	**-5.41%**
Sta. Rita	**4.1659**	**29.69%**	**4.2749**	**31.31%**	**0.1090**	**1.62%**
San Lorenzo	**4.1165**	**15.87%**	**4.2888**	**16.68%**	**0.1723**	**0.81%**
Philpodeco	5.7245	0.02%	3.9352	0.02%	(1.7893)	0.00%
Total	4.3998	100.00%	4.9192	100.00%	0.5194	

(Source: Meralco)

NPC generated electricity is cheaper, also because there is a PhP0.30/kWh mandated reduction required by EPIRA for electricity generated by NPC or its IPPs. The electricity MERALCO buys from its IPPs are not subjected to this 30 centavo mandated reduction.

5. **High electricity prices breed inefficiencies, which further raise the cost of electricity.** The power sector is inherently inefficient. Average capacity utilization of Transco's transmission lines, according to an ADB report, is only at 12%. We are paying for the investment and loans incurred to set up a transmission grid and on the average, only 12% of the capacity is being utilized. With regard to generation, dependable capacity in the Philippines amounted to 13,639MW at the end of 2006, but that same year, peak demand for electricity was only 8,760MW. We pay for capacity we don't use, and this is such a heavy burden on consumers that we economize on our use of electricity even further. However, the less we consume of electricity, the more we have to pay of unused capacity. This is a vicious cycle similar to a debt trap. Industries cannot survive such a set-up. Poor consumers, even less so.

   This is manifested in electricity consumption data obtained from the Department of Energy: Electricity consumption grew by 10.6% in 2003, then by a lower 3.2% in 2004, then by an even lower 2.5% in 2005. In 2006 electricity consumption grew by only 1.1%. Today it is residential and commercial users who hold a bigger share of total consumption. The thing is, residential and commercial consumers have peak hours when their demand for electricity is strong. Beyond that, demand is very low. This leaves the power sector with a huge inefficient setup: Base load demand is weak but you have to have extra capacity for use during the peak hours. This also means that you have to spend on additional capacity that will most likely get used only during peak hours. This is clearly wasteful and inefficient.

6. **Other ERC decisions have rendered the cost of electricity high.** One such decision is the ERC's dismissal of the Power Sector Assets and Liabilities Management Corporation (PSALM) market abuse case alleged by the Philippine Electricity Market Corporation (PEMC), the operator of the Wholesale Electricity Spot Market (WESM). The ERC dismissed this for lack of sufficient evidence, despite the detailed market data submitted by PEMC clearly showing that PSALM exercised its market power to raise the WESM spot price. The dismissal by ERC will cost consumers an additional PhP14B.

7. **EPIRA-mandated removal of subsidies.** Following the logic of privatization and market-reforms, EPIRA states that instruments such as cross-subsidies which distort the “real” price of electricity should be removed. This is in keeping with the transformation of electricity industry from a public service industry to a commodity market. The prices should be subjected to market rules alone – and considerations such as equity and justice in the provision of electricity should be abolished. Households no longer enjoy subsidies from the industrial and commercial sectors, and households in Mindanao and Visayas are no longer being subsidized by households in Luzon. These households that no longer enjoy the subsidies of the pre-EPIRA days have experienced a hike in rates as a result of the removal of these subsidies.

   Even the lifeline rate today is not what it used to be. In the logic of subsidy, better off consumers subsidize the more disadvantaged ones. This may work in cities like Manila but in areas that are by and large poor, the lifeline rate is symbolic more than real and it is actually the less poor who are subsidizing the poorer.

8. **Unfair and unjust practices of industry players that the ERC is ineffectual to regulate, or may even condone.** ERC is known to have been powerless in providing more substantial solutions to recurrent abuse (overcharging and corporate malpractice) of DUs such as MERALCO. There had already been a number of times when MERALCO was proven to have engaged in such unscrupulous practice, yet MERALCO can and will probably engage in such practice because of the lack of fundamental action on the part of the ERC. For example:

   - In 2002, ERC discovered PhP0.50/kWh unjustified over-recoveries of MERALCO from the PPA. It reached PhP12.3 billion as based in December 2001 computations. MERALCO was asked to refund it to the consumers.

   - In 2003, the Commission on Audit discovered that MERALCO overcharged its customers by PhP0.017/kWh through inclusion of income tax as operation expense which it passed on to consumers from 1994 to 2002. The Supreme Court subsequently ordered MERALCO to stop this practice and to refund the consumers by as much as PhP30 billion.

   - Also in 2003, FDC questioned ERC’s giving of provisional authority to MERALCO to raise their rates by as much as PhP0.12/kWh. Fortunately for the consumers, the Supreme Court junked the ERC decision in January 2004 because it violated certain rules during its own hearings.

- In June 2004, MERALCO again applied for PhP0.1327/kWh increase through Generation Rate Adjustment Mechanism (GRAM). The Supreme Court again junked the petition in February 2006 as MERALCO did not follow the prescribed process (lack of hearing and publication).

But MERALCO is not the only one engaged in abusing and deceiving the consumers. The Panay Electric Company (PECO), also known to be owned by the Lopez family, had also been asked by the ERC to refund the consumers PhP2/kWh it earned due to overcharging.

9. **Value Added Tax (VAT)**. Because of the ballooning fiscal deficit of the government, which is in part caused by guaranteed obligations of Government-Owned and -Controlled Corporations (GOCCs) like NPC, the 12% VAT now includes oil and electricity which was exempted before (zero-rated) in the previous consumption tax regime because it was categorized as “socially-sensitive” – raising its prices will translate to rising prices of other commodities. According to some studies, VAT raises electricity prices by PhP0.60/kWh to PhP0.90/kWh. It is estimated that the government earned at least PhP7.668 billion from VAT in the electricity industry in 2005.

One of the more controversial applications of VAT in electricity is the imposition of VAT to system loss, electricity which had been generated but not used***. It is unjust to impose consumption tax on goods and services not actually consumed.***

10. **Corruption and Mismanagement**

- **In NPC.** Corruption in National Power Corporation (NPC) artificially inflates generation charges. This includes allegations of “overpricing” in the process of buying coal and oil supply for NPC-owned power plants and NPC-IPP’s.

- **In PSALM**. The privatization of NPC plants is anomaly-ridden, the most outstanding proof of which is the halted sale of the Masinloc Power Plant to the winning bidder – the YNN. Aside from the fact that YNN capacity is questionable (it failed to pay down payment despite three extensions), sale of Masinloc to YNN will only raise electricity prices form PhP2.80 to PhP4.80/kWh. What is more revolting is this case is that, according to a COA report, PSALM officials gave themselves PhP10-million bonus because of the “successful” closing of the failed transaction with YNN.