MERALCO

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0300 PHILIPPINES

23 June, 2016

HON. MYLENE C. CAPONGCOL
Undersecretary, Department of Energy
Energy Center, Rizal Drive
Bonifacio Global City, Taguig City

Dear Usec. Capongcol:

We are respectfully submitting our comments and recommendations on the proposed Renewable Portfolio Standards (RPS) Rules, as presented during the public consultations last 16 June, 2016. While we had raised some of our concerns during the public consultation, please allow us to reiterate our recommendation to:

- Defer the promulgation of an RPS target and mandated annual increment until after rigorous economic and technical impact studies have been completed, and
- Conduct additional nationwide public consultations on the draft, which was made available on the DOE website only today (June 23) and which contain numerous substantive differences with the drafts that were subjected to public consultations in 2011 and 2012. Among the new provisions introduced in the 16 June, 2016 draft include the targeting of a 35% share (in MWh) for RE generation, the achievement of such a target by 2030, and the introduction of a more aggressive annual increment of 2.15%.

Need for in-depth technical and economic studies to support the RPS targets

Targeting a 35% share because, "When the RE Law was passed in 2008 it was 35% and that is the reason why we want to bring it back to 35%," is inadequate justification to support a policy that will have far-reaching technical and economic repercussions over the next decade and more.

We are aware of the ongoing study on RE grid integration being conducted by a team composed of the DOE, the National Grid Corporation of the Philippines (NGCP), the Philippine Electricity Market Corporation (PEMC), the Energy Regulatory Commission (ERC), the Grid Management Committee (GMC) the Distribution Management Committee (DMC), the National Transmission Corporation (TransCo), the National Renewable Energy Board (NREB), the National Electrification Administration (NEA), and the Philippine National Oil Company-Renewable Corporation (PNOC-RC).

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As announced during the 16 June, 2016 public consultation, this study will be completed by the third quarter of the year. According to Department Circular No. DC2015-11-0017, the study's objective is to identify potential grid reliability concerns with the scaling of the Variable Renewable Energy (VRE) resources, as well as to identify options to improve system flexibility and power system balance, and we believe that the results of the study will be valuable in developing the RPS. It is but prudent to complete this study and carefully consider its findings, before the setting of any RPS target.

Certain portions of the Visayas grid are already experiencing frequency excursions due to the high penetration of VRE. This has led to "Emergency Load Droppings" (or brownouts) to maintain system security and the wasteful curtailment of geothermal-based generation. We have the opportunity to learn from this experience and avoid its recurrence in other portions of the grid.

As a complement to the technical study, there should also be an economic study to assess the impact of an arbitrary RPS share to the welfare of consumers. As echoed by the stakeholders during the public consultation, the customers, who will eventually bear the cost of the implementation of the policy, should be fully aware of the implications of the RPS.

Already, the Economic Power and Development Program (EPDP) presented initial results of its "Filipino 2040 – Energy: Power Security and Competitiveness" study. As part of the study, it compared a policy regime of maintaining a 30 percent share of renewables against a policy "that favors increased temporary utilization of the lesser-cost resources but takes into account environmental costs."

Their initial results revealed that "... there is a better alternative to the current policy stance of the government, which mandates the maintenance of 30% share of renewables" and that "... the optimal fuel mix is not constant over time but should exploit ... less costly resources while taking environmental (including health) costs into account to bring the price of power down." Their simulations show that maintaining a 30% RE share will cost consumers nationwide **in the order of P100 billion more annually by 2030**. While the study is still to be finalized, the indicative magnitude of the additional costs to consumers is substantial and should give policy-setting cause to step back and more carefully consider the economic implications the proposed targets.

Our own simulations, using certain assumptions, show that Meralco consumers will be made to absorb **additional cumulative costs by 2030 due to the proposed targets and increments in the order of P160 billion.**

RPS will create an artificial sellers' market, to the detriment of consumers

At its core, the RPS will be a government imposition that will create an artificial market for investors in a few chosen power plant technologies. As drafted, the RPS Rules would force a distribution utility (DU), under pain of penalty, to procure a prescribed share (that will increase over time) of its power requirements from certain favored generators. Further, such RPS procurement will have to be made whether or not the power is actually needed by the DU to ensure the provision of adequate, reliable, efficient, and cost effective electric service to customers.

Being an artificial market, it can only be expected that the RPS will mean that electric service to customers will be more expensive than it needs to be. Otherwise, the imposition of the RPS obligation on buyers will not be necessary. This imposition on buyers, such as DUs, will distort competition and put them at a disadvantage when procuring supply contracts from RE developers. The latter will naturally take advantage of the leverage accorded to them by an RPS mandate and demand prices higher than what would have been without an RPS requirement. The higher cost of this sourcing will be an additional burden to the electric consumers.

RPS will bring additional bureaucratic burden

On top of higher energy and capacity costs, the implementation of RPS would bring its own bureaucratic burden. Mandated participants such as DUs have been assured that compliance mechanisms will be in place to allow them to meet their RPS obligations. These include the generation from Feed-in-Tariff (FIT) availees and net metering arrangements and through the purchase of Renewable Energy Certificates (RECs) from a Renewable Energy Market (REM).

To simply implement and monitor all these, however, will entail the deployment and maintenance of additional manpower, procedures, and information systems for record-keeping and transaction processing. At present, the industry has yet to understand the full cost of the implementation of the FIT. On top of these, with the RPS, the industry will also need to invest in and operate the REM. It should be stressed that all these costs that will be incurred not only by the agency that will be doing the monitoring, but also by all of the mandated participants as part of their compliance efforts.

Power sourcing is a complex activity requiring in-depth forecasting and planning, comprehensive daily analysis, etc. This is especially true for DUs, which also have to obtain prior regulatory approval of wholesale supply contracts. The RPS will add another level of complication—and cost—to this activity. Eventually, all of these costs will find their way to consumers in the form of higher power prices.

Conclusion

With the ongoing implementation of the FIT and now the proposed RPS, we urge caution on the additional burden on consumers' electricity bills that these will bring. We firmly believe that any additional imposition, just like any other cost throughout the power supply chain (e.g., (distribution, transmission, ancillary charges, taxes, etc.), should be carefully and continuously scrutinized against the objective of providing adequate, reliable, efficient, and cost-effective electric service to all end-users, households and business alike.

Lastly, we share the hopes of the stakeholders to have more public consultations on the draft RPS Rules. We take note that the DOE conducted a total of seven public consultations nationwide in 2011 for a draft that mandates a different RPS target, and a minimum annual increment of 1%. The final draft sets a target of 35% RE share by year 2030, an annual target per grid, and a minimum annual increment 2.15% for each Mandated Participant. With the more aggressive targets, it becomes more imperative to conduct public consultations nationwide.

We fully support the industry's goals of reducing greenhouse emissions, enhancing energy security, and providing reliable and quality electric supply at a reasonable price, and we believe these can be achieved with a well-thought and well-crafted policy mechanisms. Thank you for the opportunity to share our thoughts on the draft Rules and we hope that they can be favourably considered by the Department.

Very truly yours,

LAWRENCE S. FERNANDEZ
Vice President and Head
Utility Economics

cc:
Mario C. Marasigan
OIC-Assistant Secretary

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DRAFT RENEWABLE PORTFOLIO STANDARDS
Meralco's Comments

SECTION IN THE DRAFT RULES	PROVISION IN THE DRAFT RPS RULES	COMMENTS/CLARIFICATIONS/ PROPOSED REVISIONS
Rule 1, Sections 1 and 2	**Section 1. Short Title.** – This Department Circular shall be known as the "RPS Rules" and shall hereinafter be referred to as the "Circular." Section 2. Purpose of the RPS. The RPS Rules is hereby adopted in order to contribute to the growth of the RE industry by diversifying energy supply, spur socio-economic development in rural areas, and help address environmental concerns of the country by reducing harmful emissions.	For clarity; it is suggested to use as reference the "RPS Rules" and omit the use of "Circular" in order to be more specific. As an example of confusion, Section 1 states "hereinafter be referred to as the "Circular," but on the very next Section 2, "RPS Rules" was used to refer to the present Circular.
Rule 2, Section 6	**Section 6. Implementation of RPS Rules.** Upon the effectivity of this Circular, the RPS Rules shall be implemented in Luzon, Visayas and Mindanao grids: Provided, That the DOE will issue separate rules for the operationalization of RPS in Mindanao until the operationalization of a Wholesale Electricity Spot Market (WESM) in Mindanao: Provided further, That public consultation with Mindanao stakeholders and electric power industry participants no later than one (1) year for the effectivity of this Circular will be required. For purposes of this Section, Luzon, Visayas and Mindanao shall be treated as separate and distinct grids: Provided, That the DOE may reclassify the grids.	"xxx Provided further, That public consultation with Mindanao stakeholders and electric power industry participants no later than one (1) year ~~for~~ **from** the effectivity of this Circular will be ~~required~~ **conducted.**
Rule 2, Section 7	**Section 7. Minimum Annual RPS Requirement.** - To maintain the RE share in the national energy mix to at least thirty five percent (35%) by 2030, the minimum annual target per grid shall be equal to the sum of the minimum target of all Mandated	1) What is the basis of the 35% initial requirement? It appears that it has no legal and factual basis. The RPS Rules do not state such basis and do not provide for any study that was undertaken to conclude that 35% will actually be

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	Participants in the grid. The minimum annual RPS requirement per Mandated Participant shall be computed by the Composite Team in coordination with the NREB: Provided, That the annual RPS requirement shall be calculated in accordance with the following formula, all expressed in MWh: xxx Provided further, That the Baseline Year shall be the calendar year immediately preceding the start of mandatory compliance as provided in Section 23, Rule 8 of this Circular. A Sample Computation of the Minimum Annual RPS Requirement is provided in Annex "A".	beneficial to consumers in terms of lower rates. 2) The minimum annual target should first consider the actual demand and forecasted growth of the customers of each Mandatory Participant. This is also to establish the capacity that can be accommodated by each distribution system. 3) We seek clarification on how the intermittency of RE and its impact on the grid, which would affect the reliability of the supply of power, will be addressed. 4) How will mandating 35% affect DUs that are fully contracted? Has DOE determined the impact of enforcing this minimum annual RPS requirement vis-à-vis the electricity rates of consumers? Also, given the intermittency of RE sources, has DOE considered this and its effect on the blended generation cost of DUs, especially when DUs are forced to take from WESM when the RE source's generation is low or on outage? It bears emphasis that the RE Law did not provide for development of RE at the expense of consumers who will shoulder the higher rates resulting from this. 5) Has DOE determined how the 35% RE share can be achieved vis-à-vis DOE's indicative lineup of Luzon Visayas Mindanao Power Projects? 6) Will contracting with RE sources for supply of electricity be exempt from the requirements of competitive selection process (CSP) given that it

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		will not pass the least-cost obligation of DUs as compared to other alternative sources of supply? Moreover, if the cost of conventional sources that will have to replace the energy that an RE source fails to generate is factored in, then the cost will increase further. 7) Before setting a 35% RE share, the DOE has to establish first its fuel mix policy. This policy is significant because it will define the requirement for other sources of power like coal and gas, and the implications therefrom. There should also be a study on this.
Rule 2, Section 8	**Section 8. Minimum Annual Incremental RE Percentage –** The minimum annual increment in the RPS level shall be initially set at 2.15 percent (2.15%) to be applied to the actual total supply portfolio of the Mandandated Participant in each grid for the previous year. This is to determine the current year's requirement for RECs of the Mandated Participant: Provided, That the minimum annual percentage may be adjusted by the NREB when: a. There are substantial changes in relevant to the market in the grid; or b. b. The set percentage is deemed insufficient to attain the target set by the DOE.	Spelling error of "Mand~~an~~dated Participant" It appears that there is no clear logic and rationale for mandating this and setting a 35% target (with 2.15% increase every year), especially at a time when there is insufficient capacity in the country. What is the basis for annual increment of RE portfolio, particularly the initial increment in RPS level of 2.15% applied to actual total supply portfolio in the previous year?
Rule 3, Section 9	**Section 9. Eligible RE Technologies.** For purposes of compliance with the RPS, the following RE resources shall be eligible: a. Biomass; b. Waste to energy technology;	RE sources should be consistent with the RE Law. It should not be limited to emerging REs (i.e. those entitled to FITs). It should be all REs in general. For letter (f) – "Impounding of hydropower sources" is not clear. A

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	c. Wind energy; d. Solar energy; e. Run of river hydropower sources; f. Impounding hydropower sources that meet internationally accepted standards; g. Ocean energy; h. Hybrid systems as defined in the RE Act; i. Geothermal energy; and j. Other RE technologies that may be later identified by the DOE, through a separate issuance, upon the recommendation of the NREB.	competitive hydropower should be allowed for purposes of compliance with the RPS Rules.
Rule 3, Section 11	**Section 11. RPS Mandated Participant.** - The following entities are mandated to comply with the RPS: a. All DUs for all its existing customers and subsequently, upon commencement of the Retail Competition and Open Access (RCOA), for its captive customers; b. All licensed RES for the Contestable Market upon commencement of RCOA; c. All local RES upon commencement of RCOA; d. Any SOLR as may be identified upon commencement of RCOA; e. Generating companies only to the extent of their actual supply to their DCCs; f. Entities duly authorized to operate as distributors within the economic zones; and Other entities as may be recommended by NREB and approved by the DOE.	In view of the uncertainty of the demand of SOLR, SOLR should be one of the enumerated exemptions. It is extremely difficult to monitor customer demand for SOLR as its customers are expected to come and go. Besides, the SOLR's most likely source of supply for their customers is the WESM, considering the lack of visibility on potential customers.
Rule 4, Section 15	**Section 15. General Principles on the Establishment of the REM and the**	This provision provides that PEMC may impose transaction fees. In the case of

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	RE Registrar. The DOE shall establish the REM to facilitate the issuance, commercialization and verify compliance with the annual RPS requirement. As part of the REM, the PEMC, under the supervision of the DOE shall establish the RE Registrar and shall issue, keep and verify RECs corresponding to energy generated from eligible RE facilities. The following principles shall be considered in the establishment of the rules and guidelines governing the REM and the RE Registrar: Xxx i. A transaction fee may be imposed by PEMC for transactions undertaken in the REM and RE Registrar subject to the setting of operational charges to be approved by the ERC: Provided, That a separate issuance will be issued to serve as guidelines for the same.	the DUs, how will the DUs recover transaction fee costs?
Rule 8, Sec. 23	**Section 23. Transition Period**. A Transition Period of one (1) year from the commencement of operations of the REM is hereby provided to ensure an orderly, efficient and effective imposition of the RPS Rules. The period will allow the participants to prepare all information and data required in the establishment of the baseline to be determined by the DOE, prepare their respective compliance mechanisms as well as prepare the consumers for the impact of the RPS Rules. Upon the lapse of the Transition Period, mandatory compliance with the RPS shall commence.	We seek clarification on whether the intention of this Section is for the RPS Rules not to become effective until the REM is operational and the transition period has already lapsed. If RE-sourced long term power supply contracts will have to undergo CSP, the transition period of one (1) year may be too short.

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Rule 8, Sec. 24	**Section 22. Reportorial Requirements**. - The DOE shall establish a reliable database to serve as the baseline in the calculation and monitoring of the compliance of the Mandated Participants: xxx a. All DUs shall submit the following information covering the period that will be defined by the DOE: i. Purchases broken down by generating facility, power source and/or through the WESM; ii. For purchases from the PSALM/NPC, all purchases shall be segregated into RE and non-RE based resources on the proportionate share of the non-Value Added Tax allocation from PSALM/NPC; and iii. Output from Embedded Generation facilities, and iv. Such other reports that the DOE may require. xxx xxx xxx	For (a.): Please clarify when referring to Purchases, does this pertain to volumes in MW or MWh?