

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

IN THE MATTER OF THE
INVESTIGATION CONDUCTED ON
ALLEGATIONS OF ANTI-
COMPETITIVE BEHAVIOR AND
MARKET POWER ABUSE
COMMITTED BY THE POWER
SECTOR ASSET AND LIABILITIES
MANAGEMENT CORPORATION
(PSALM) IN THE WHOLESALE
ELECTRICITY SPOT MARKET

ERC CASE NO. 2007 - 421 MC

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D O C K E T E D

Date: JUL 05 2007

By: [Signature]

ORDER

Before the Commission for deliberation is the Investigatory Unit's (IU) Report dated 4 June 2007, which is hereto attached, detailing the IU's findings and recommendation relative to the allegation of anti-competitive behavior and/or market power abuse committed by the Power Sector Asset and Liabilities Management Corporation (PSALM) during the third billing month of operations of the Philippine Wholesale Electricity Spot Market (WESM).

The instant case stemmed from an Investigation Report issued by the Enforcement and Compliance Office (ECO) of the Philippine Electricity Market Corporation (PEMC) after it investigated the increase in the load weighted average price in the WESM during the third month of operations and the bidding behavior of PSALM's trading teams during the third billing period, which was observed to be the cause of such increase. As a result of its inquiry, the ECO issued its Investigation Report finding that PSALM behaved anti-competitively and abused its market power.



The said ECO Investigation Report was reviewed, and the findings therein confirmed, by the Market Surveillance Committee (MSC) of the PEMC in the MSC Memorandum Report dated 20 November 2006.

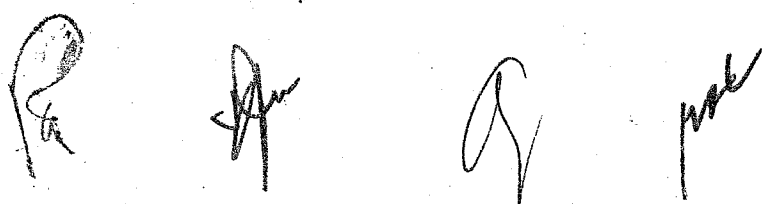
Pursuant to its mandate to penalize abuse of market power under Section 43 of Republic Act No. 9136, otherwise known as the Electric Power Industry Reform Act of 2001 (EPIRA), and in accordance with the Competition Rules and Complaint Procedures, the Commission constituted the IU to determine whether or not there is sufficient evidence to initiate appropriate action against PSALM for anti-competitive behavior and/or market power abuse.

From December 2006 to March 2007, the Investigatory Unit conducted its investigation, directing PEMC and PSALM to provide it with all the relevant documents and information.

On 4 June 2007, after concluding its investigation, the IU submitted to the Commission for its consideration the attached IU Report wherein it states and recommends that:

The IU finds no prima facie case against PSALM for anti-competitive behavior or market power abuse. For this reason, further investigation and proceedings are not warranted. The IU, therefore, recommends that this investigation be terminated.

The Commission is called upon to determine whether or not to accept the IU's recommendation to terminate this investigation based on its findings that there exists no prima facie case against PSALM for anti-competitive behavior or market power abuse. In resolving this issue, however, and consistent with its mandate under the EPIRA to promote competition and





encourage market development, the Commission deems it prudent to dwell on tangential issues concerning irregular behavior and trading arrangements within the WESM, which are anathema to the objectives of competition.

After due deliberation and a comprehensive review of the IU Report and the entire records of the investigation conducted by the IU, the Commission accepts the findings therein and thus adopts the IU's recommendation.

The fundamental objective of the entire restructuring process is competition and for there to be a truly competitive electricity market, there should be sufficient number of buyers and sellers so that individual firms have no control over market conditions of price or quantity supplied. The Commission is fully cognizant that this not the case yet for WESM considering the National Power Corporation's (NPC) and PSALM's market shares. Hence, it is not surprising that any action on their part that impacts on the electricity price is readily viewed with suspicion of market power abuse. It is for NPC and PSALM, therefore, to be more circumspect and transparent in their dealings in the WESM.

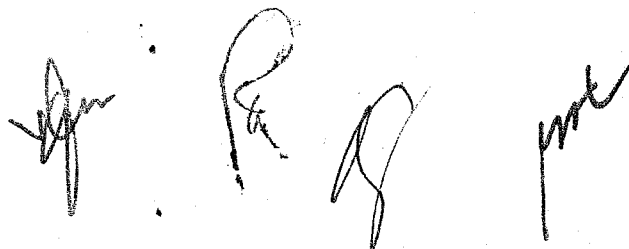
Mere suspicions, however, cannot substitute for proof and the absence of proof to constitute a prima facie case against PSALM does not justify the conduct of formal proceedings against it. The Commission cannot simply rely on speculation, conjectures or guesswork, no matter how appealing, to establish the act or conduct of PSALM that amounts to anti-competitive behavior or market power abuse.



The Commission, however, notes the letters of NPC President Cyril C. del Callar to PSALM, attributing the losses incurred by NPC and PSALM during the first two billing months to the PSALM trading teams' strategies at the WESM and urging PSALM to adopt certain recommendations that ultimately affects how the PSALM trading teams submit their offers in the market.

It is highly inappropriate and irregular for NPC to write such letters to PSALM. The participants in the market are expected to act judiciously and be circumspect in their dealings with each other to thwart any notion of collusion or any tacit agreement or understanding among them. To the mind of the Commission, NPC's proposal may in fact be taken as an invitation to collaborate so as to vary market results and it is no secret that the dominant position of PSALM can enable it to capitalize on such to easily dictate the prices in the WESM. The influencing capacity of NPC over PSALM and the bidding behavior of the trading teams, whether intended or not, cannot be discounted. Market participants, specifically NPC, should refrain from making such recommendations to PSALM that may have an impact on the market conditions.

The Commission also observes that while the PSALM is possessed with market power as a seller in the WESM, the safeguards that have been put in place, in an attempt to diminish its dominant position, are insufficient. The division of the entire capacity held by PSALM into four (4) trading portfolios is not sufficient. Apart from the need to reduce the influence or define the authority of upper management over these trading teams, policies and protocols must be strengthened to ensure independence of these trading teams from each other and from upper management.



Finally, the Commission draws PEMC's attention to its deficient compliance to the IU Order dated 11 December 2006 issued in the course of the IU's investigation. The IU is one constituted by the Commission as a fact-finding body upon whom the Commission's powers of inquiry have been duly delegated. When an industry participant is called upon by the IU to assist it in or submit to its investigation, its compliance and full cooperation are expected.

WHEREFORE, PREMISES CONSIDERED, the Commission hereby adopts the findings of the Investigatory Unit as contained in the attached IU Report dated 4 June 2007 and approves the recommendation to terminate this investigation.

As for NPC's conduct, which was found to be highly inappropriate and irregular under the circumstances, the Commission hereby issues a stern warning for NPC to refrain from such conduct that is inimical to the objectives of free competition. Let it be a warning also to all other industry participants that conduct of similar nature shall be dealt with more severely by this Commission.

The Commission also directs PSALM to adopt policy measures that will strengthen the independence of its trading teams from one another and from PSALM management insofar as dealings in the WESM are concerned and PEMC to make the necessary changes in its registration policies to reflect the same, within thirty (30) days from their receipt hereof. PSALM and PEMC are further directed to immediately apprise the Commission of the measures so adopted.

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Finally, the Commission issues this warning to PEMC for its failure to fully comply with a valid directive of the Investigatory Unit.

SO ORDERED

Pasig City, 06 June 2007.


RODOLFO B. ALBANO, JR.
Chairman


RAUF A. TAN
Commissioner


ALEJANDRO Z. BARIN
Commissioner


MARIA TERESA R. CASTANEDA
Commissioner


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