

[DOE DEPARTMENT CIRCULAR NO. DC 2006-01-0002, January 23, 2006]

ON THE MANDATE AND RESPONSIBILITY OF THE DEPARTMENT OF ENERGY OVER THE WHOLESALE ELECTRICITY SPOT MARKET AND THE AUTHORITY OF THE PHILIPPINE ELECTRICITY MARKET CORPORATION IN RELATION TO THE PREPARATION, ADOPTION AND FILING FOR APPROVAL OF THE PRICE DETERMINATION METHODOLOGY

WHEREAS, under Section 30 of Republic Act No. 9136 (otherwise known as the "Electric Power Industry Reform Act of 2001" or "EPIRA"), the Department of Energy ("DOE") is mandated to establish the wholesale electricity spot market ("WESM") composed of the wholesale electricity spot market participants.

WHEREAS, in accordance with Rule 9 Section 3 (a) of the Implementing Rules and Regulations of the EPIRA ("IRR"), the DOE is mandated to organize and establish the appropriate market design and governance structure of the wholesale electricity spot market.

WHEREAS, pursuant to its power to establish the WESM, Section 30 of EPIRA further provides that the DOE is responsible for (a) the formulation of the detailed rules for the WESM ("WESM Rules"), jointly with the electric power industry participants and (b) the constitution of the market operator which shall be an autonomous group responsible for the implementation of the WESM in accordance with the WESM Rules.

WHEREAS, on 28 June 2002, the DOE, with the joint endorsement of electric power industry participants, issued Department Circular No. 2002-06-003 promulgating the WESM Rules, consistent with the provisions of Section 30 of EPIRA that:

- a. the rules shall reflect accepted economic principles and provide a level playing field to all electric power industry participants; and
- b. the rules shall provide, among others, procedures for:
 - i. establishing the merit order dispatch instructions for each time period;
 - ii. determining the market-clearing price for each time period;
 - iii. administering the market, including criteria for admission to and termination from the market which includes security or performance bond requirements, voting rights of the participants, surveillance and assurance of compliance of the participants with the rules and the formation of the wholesale electricity spot market governing body;
 - iv. prescribing guidelines for the market operation in system emergencies; and

v. amending the rules.

WHEREAS, in November 2003, the DOE constituted the Autonomous Group Market Operator ("AGMO") with the incorporation of the Philippine Electricity Market Corporation ("PEMC").

WHEREAS, Section 30 of EPIRA states that the WESM Rules shall provide the mechanism for determining the price of electricity not covered by bilateral contracts between sellers and purchasers of electricity;

WHEREAS, Section 30 of EPIRA provides further that the price determination methodology contained in the WESM Rules shall be subject to the approval of the Energy Regulatory Commission ("ERC").

WHEREAS, on 30 November 2004, the DOE authorized the PEMC to file on its behalf the WESM Price Determination Methodology ("PDM") for the approval of the ERC, and to comply with all directives of the ERC in relation to the PDM.

WHEREAS, there is a need to clarify the scope of PEMC's authority to act on behalf of the DOE in relation to the preparation, adoption and filing for approval of the PDM with the ERC pursuant to the DOE's mandate as regards the design and structure of the WESM.

NOW, THEREFORE, premises considered, the DOE hereby adopts this Circular for purposes stated above and to provide guidance to PEMC in seeking the approval of the PDM;

SECTION 1. Objective of Wholesale Electricity Spot Market - Consistent with its mandate under Section 30 of EPIRA and, more particularly, Rule 9, Section 3(a) of the IRR, the DOE adopted a WESM design and structure that is intended to establish a competitive, efficient, transparent and reliable market for electricity where:

- a) A level playing field exists among the participants;
- b) Trading of electricity is facilitated among participants within the spot market;
- c) Third parties are granted non-discriminatory access to the power system;
- d) Prices are governed as far as practicable by commercial and market forces; and
- e) Efficiency is encouraged.

SECTION 2. Components of Wholesale Electricity Spot Market - The following key components constitute the design of the WESM:

a) Pricing.

- i. Basic to any market design is the method and procedures for determining the price at which electricity will be sold or purchased in the wholesale electricity spot market.
- ii. The main objectives of the pricing method are to --
 - 1. Balance supply and demand;
 - 2. Provide the proper incentives, both short term and long term, to