



**Republic of the Philippines
DEPARTMENT OF ENERGY**

Department Circular No. DC2017- __ - _____

**ADOPTING POLICIES FOR THE EFFICIENT TRANSITION TO THE
INDEPENDENT MARKET OPERATOR FOR THE WHOLESALE ELECTRICITY SPOT
MARKET**

WHEREAS, Section 2 of the Republic Act No. 9136, otherwise known as the “Electric Power Industry Reform Act of 2001 (EPIRA)” declared the Policy of the State among others the following:

- a) Ensure the quality, reliability, security and affordability of the supply of electric power;
- b) Ensure transparent and reasonable prices of electricity in a regime of free and fair competition and full public accountability to achieve greater operational and economic efficiency and enhance the competitiveness of Philippine products in the global market;
- c) To enhance the inflow of private capital and broaden the ownership base of the power generation, transmission and distribution sectors;
- d) Protect the public interest as it is affected by the rates and services of electric utilities and other providers of electric power; and
- e) To establish a strong and purely independent regulatory body and system to ensure consumer protection and enhance the competitive operation of the electricity market.

WHEREAS, Section 30 of the EPIRA provides that:

- a) Within one (1) year from the effectivity of the Act, the Department of Energy (DOE) shall establish the wholesale electricity spot market (WESM) composed of the wholesale electricity spot market participants;
- b) The WESM shall be implemented by a market operator (MO) in accordance with the Wholesale Electricity Spot Market Rules;
- c) The market operator shall be an autonomous group, to be constituted by DOE, with equitable representation from electric power industry participants, initially under the administrative supervision of the TRANSCO;
- d) The market operator shall undertake the preparatory work and initial operation of the wholesale electricity spot market., an autonomous group constituted by the DOE with equitable representation from electric power industry participants under the administrative supervision of the National Transmission Corporation (TRANSCO);
- e) Not later than one (1) year after the implementation of the wholesale electricity spot market, an independent entity shall be formed and the functions, assets and liabilities of the market operator shall be transferred to such entity with the joint endorsement of the DOE and the electric power industry participants; and

- f) Thereafter, the administrative supervision of the TRANSCO over such entity shall cease.

WHEREAS, Section 37 of the EPIRA further mandates the (DOE) to supervise the restructuring of the electricity industry, endeavor to provide for an environment conducive to free and active private sector participation and investment in all energy activities, and to exercise such other powers as may be necessary or incidental to attain the objectives of the EPIRA;

WHEREAS, in compliance with its mandate, the DOE promulgated the Implementing Rules and Regulations (IRR) of the EPIRA, Rule 4 of which defines the “Independent Market Operator” (IMO) as *“a person who is financially and technically capable, with proven experience and expertise of not less than two (2) years as a leading independent market operator of similar or larger size electricity markets endorsed jointly by the DOE and Electric Power Industry Participants to assume the functions, assets and liabilities from the Autonomous Group Market Operator (AGMO), pursuant to Section 30 of the Act;”*

WHEREAS, pursuant to the aforementioned mandates, the DOE issued on 9 June 2003, Department Order No. 2003-06-006 entitled “Designating the TRANSCO-MO to Operate the Wholesale Electricity Spot Market”, directing the TRANSCO-MO to operate the WESM under the direction of the DOE until substituted by the IMO which shall take over its functions, assets and liabilities in accordance with the EPIRA;

WHEREAS, on 18 November 2003, through the initiative of the DOE, the Philippine Electricity Market Corporation (PEMC) was incorporated under the Securities and Exchange Commission (SEC) with Company Registration No. CN200323988 as a non-stock, non-profit corporation with the primary purpose of managing, governing, and administering an efficient, competitive, transparent, and reliable market for the wholesale and purchase of electricity and ancillary services in the Philippines, in accordance with the EPIRA;

WHEREAS, in April 2004, the DOE, TRANSCO, and PEMC entered into an Operating Agreement which provided for the delineation of functions between PEMC and TRANSCO-MO in the preparations for establishment of the WESM;

WHEREAS, on 22 October 2004, TRANSCO and PEMC entered into a Memorandum of Agreement providing for transfer of personnel, assets, contracts, and liabilities from TRANSCO-MO to PEMC;

WHEREAS, the PEMC is governed by its board of directors (PEM Board) constituted with equitable representation from the electric power industry participants, and chaired by the Secretary of the DOE and is the AGMO tasked to undertake the preparatory work and initial operation of the WESM pursuant to the EPIRA;

WHEREAS, the WESM started commercial operations in Luzon on 26 June 2006 and in the Visayas on 26 December 2010;

WHEREAS, in February 2010, the Asian Development Bank (ADB) provided technical assistance to DOE to study the IMO; and in December 2011 and July 2014 the DOE conducted public consultations on the structure of the IMO;

WHEREAS, on 8 December 2015 and 26 January 2016, hearings were held by the Senate Committee on Energy to discuss, among others, the transition of the AGMO to the IMO and the formation of a Technical Working Group (TWG) to propose the structure of, and the manner of transition to, the IMO;

WHEREAS, the recommendations of the TWG were submitted to the DOE;

WHEREAS, on 28 July 2017, the DOE issued Department Order No. DO2017-07-0010 creating the Transition Committee for PEMC, which was tasked among others, to propose a way forward for the WESM to adapt to the current environment and prepare it to meet the challenges of the future;

WHEREAS, after due study, the Transition Committee formulated an IMO transition proposal that provides for the formation of an independent entity separate from PEMC to become the IMO, while PEMC shall remain to be the governance arm of the WESM;

WHEREAS, the said IMO transition proposal was presented for consultation with the PEM Board and with the WESM Members, and was also published in the market information website. Upon the results of the consultations, the Transition Committee completed the IMO transition plan and thereafter presented the same to the PEM Board and the PEMC membership for approval and endorsement;

WHEREAS, in meetings duly called for the purpose, the DOE Secretary as the Chairman of the PEM Board instructed PEMC to present and subject to public consultation "*Plan for Transition to the Independent Market Operator of the Philippine Wholesale Electricity Spot Market*" (IMO Transition Plan);

NOW, THEREFORE, for and in consideration of the foregoing, the DOE issues, adopts and promulgates the following policies for the efficient transition of the WESM to the Independent Market Operator as embodied in the EPIRA and full attainment of the objectives of the law:

Section 1. Joint Endorsement of the DOE and the Electric Power Industry Participants. Upon the endorsement by the electric power industry participants, represented by the PEM Board and the WESM members, the DOE shall promulgate and adopt the IMO Transition Plan that sets out the formation and structure of the IMO, the resulting WESM governance structure, and the manner by which transition to the IMO shall be accomplished.

Section 2. Guiding Principles. The formation of the IMO shall be subject to the following guiding principles:

- 2.1. The objectives of the WESM are to establish a competitive, efficient, transparent and reliable market, where a level playing field exists, prices are governed as far as practicable by commercial and market forces, and efficiency is encouraged. These objectives are to be achieved consistent with the policies declared in the EPIRA to ensure the quality, reliability, security and affordability of the supply of electric power, and to ensure transparent and reasonable prices of electricity in a regime of free and fair competition and full public accountability to achieve greater operational efficiency and enhance the competitiveness of Philippine products in the global market.
- 2.2. The WESM shall be operated by the IMO, which shall be independent from electric power industry participants and from the government and which shall operate the WESM on a non-profit basis.
- 2.3. The continued provision of service for the trading of electricity in the WESM shall be ensured during the transition to the IMO.
- 2.4. A governing board with representation from the electric power industry participants shall ensure balanced decision making with respect to governance functions over the WESM.

Section 3. Formation of the IMO.

- 3.1. **Nature of the IMO.** The IMO shall be an independent entity, formed separate from PEMC, and incorporated as a private corporation under the Corporation Code of the Philippines. No electric power industry participant, nor any of their subsidiaries, affiliates, stockholders, directors, officers or their relatives within the fourth degree of consanguinity or affinity shall hold any interest, whether directly or indirectly, in the IMO. In performing its functions as the Market Operator, the IMO shall allocate resources to enable it to operate the WESM on a non-profit basis, consistent with the Guiding Principles stated in Section 2 of this Circular and the relevant provisions of the WESM Rules.
- 3.2. **Functions.** The IMO shall assume all the functions of the Market Operator as provided for under Section 30 of the EPIRA, Section 6, Rule 9 of the EPIRA IRR, the WESM Rules and market manuals, and other relevant rules, regulations and issuances.
- 3.3. **Assets and Personnel.** The necessary personnel with experience in market operations shall be transferred from PEMC to the IMO, in accordance with relevant laws. PEMC shall likewise execute the necessary operating agreements with the IMO for, among other things, the use of the Market Management System and other related infrastructure that support the operations of the WESM.

Section 4. The IMO Board.

- 4.1. **Composition.** The IMO Board shall be composed of at least five (5) members whose composition and specific qualifications are approved by the DOE.
- 4.2. **Independence.** The directors of the IMO Board shall be independent from the electric power industry participants and from government. A member of the IMO Board shall be deemed independent, if that person:
 - a) is not a director, officer, employee, contractor, consultant, agent, adviser, legal counsel, manager, or shareholder of a WESM member or of the System Operator;
 - b) is not a relative of a person, within the fourth civil degree of consanguinity or affinity, of a director, officer, manager, or shareholder of a WESM member or System Operator;
 - c) is not an officer, manager, director, shareholder, agent, employee, consultant, adviser, legal counsel, or contractor of, or is not a person directly or indirectly, through one or more intermediaries controls, is controlled by a company, affiliate, or any other entity related to or associated with a WESM member or System Operator, where:
 - i. A related company or body, is a parent, holding company, subsidiary or affiliate of the WESM member or System Operator; and
 - ii. An associate is a person who is director, officer, manager or shareholder of that related company or entity or a relative of such a person within the fourth civil degree of affinity or consanguinity; and

- iii. An affiliate is any person that, alone or together with any other person, directly or indirectly, through one or more intermediaries, controls or is controlled by, or is under the common control with another person;

Provided, that the term shareholder shall exclude a member of an electric cooperative who is not involved in its operation and management and an end-user required to subscribe to or purchase a share in a distribution utility as an incident to the provision of service by the same distribution utility, and provided the interest of the end-user is not more than the minimum required to avail of the distribution utility's service;

- d) is not an official or employee of the Philippine government, or its agencies or instrumentalities, but this will not apply to members of the academe in public schools and universities;
- e) has not been employed as an officer, or in a supervisory or managerial capacity, by any electric power industry participant, or a company or body related to or associated with a WESM member or the government within one (1) year prior to the nomination date;
- f) agrees not to be employed by and does not accept any employment with a company, affiliate, or any other entity related to or associated with a WESM member or the System Operator within one (1) year after the person ceases to be a member of the IMO Board.

4.3. **General qualifications.** Each member of the IMO Board shall be independent in accordance with Section 4.2, and shall possess the following qualifications:

- a) the member will have a proven track record for sound strategic thinking and judgment;
- b) the member will be an independent thinker with an objective perspective;
- c) the member will have an exemplary professional background and meaningful experience in the relevant skill-set sought;
- d) the member shall possess the specific qualifications as may be identified by the PEM Board under the IMO Transition Plan; and
- e) the member will be committed to representing the long-term interests of the WESM and the general public.

4.4. **Selection Process.** Subject to DOE approval, the PEM Board shall provide for a detailed nomination and selection process for the election of the initial and subsequent members of the Board of Directors of the IMO. The selection process shall include details on the tenure and composition of the IMO Board with necessary expertise and/or qualifications to ensure that the operations of the IMO are entrusted to highly capable individuals.

Section 5. WESM Governing Board and Governance Structure

5.1. PEMC shall remain to be the governance arm of the WESM. Its board of directors, the PEM Board, shall perform its functions as set out in the WESM Rules and its Market Manuals.

- 5.2. The members of the PEM Board shall be appointed by the DOE in accordance with the WESM Rules and its Market Manuals. Towards this end, the DOE shall revisit the composition and responsibilities of the PEM Board as set out in the WESM Rules and its Market Manuals, in such manner that it achieve a level of independence necessary for the protection of public interest in accordance with the EPIRA.
- 5.3. The PEM Board, shall perform its functions as set out in the WESM Rules and its Market Manuals.
- 5.4. The PEM Board shall have the primary obligation to protect the public interest and ensure the transparency and efficiency of the WESM.
- 5.5. The PEM Board shall be supported by WESM governance committees in accordance with the WESM Rules and market manuals. In this regard, PEMC is directed to review the WESM Rules and relevant market manuals as regards the functions and duties of the governance committees to ensure that such functions and duties enhance and complement the changes in the WESM governance structure. As the overall supervisor of the WESM, the DOE shall continue to have representation in the governance committees to observe and as necessary, to provide guidance in so far as consistency with the EPIRA and related DOE policies are concerned.
- 5.6. Pursuant to the WESM Rules, the PEM Board shall monitor and supervise the Market Operator, and, for this purpose, shall adopt and enforce market operator performance standards approved by the DOE. The performance standards shall include both operational and financial performance standards. Among other things, the financial performance standards shall provide for an executive compensation policy that outlines the process and procedures that will be applied by the PEM Board in reviewing and approving the total compensation paid to senior executives and key employees of PEMC and the IMO.
- 5.7. The revenue requirements of PEMC and the IMO for the operation and administration of the WESM shall be recovered from the market fees. Upon approval of the PEM Board, the IMO shall file the same with the Energy Regulatory Commission for approval.

Section 6. Conditions for Transition. The transition to the IMO is deemed to have occurred upon fulfilment of the following:

- 6.1. Approval by the DOE of the IMO Transition Plan.
- 6.2. Amendment of the WESM Rules and market manuals in accordance with this Circular. Towards this end, PEMC is hereby directed to submit the necessary amendments to the Rules Change Committee within _____ days from effectivity of this Circular;
- 6.3. Amendment of the Articles of Incorporation and By-Laws of PEMC in accordance with this Circular. Towards this end, PEMC is hereby directed to secure the necessary approval of its amended Articles of Incorporation and By-Laws; and
- 6.4. Incorporation of the IMO company, assumption of the members of the IMO Board, and transfer of functions, assets and personnel from PEMC to the IMO through execution of a relevant agreement between PEMC and the IMO company.

Section 7. Mandate of the DOE. Jointly with the electric power industry participants, the DOE shall formulate the detailed rules for the wholesale electricity spot market. Said rules shall provide the mechanism for determining the price of electricity not covered by bilateral contracts between sellers and purchasers of electricity users. The price determination methodology contained in said rules shall be subject to the approval of ERC. Said rules shall also reflect accepted economic principles and provide a level playing field to all electric power industry participants. The rules shall provide, among others, procedures for:

- 7.1. Establishing the merit order dispatch instructions for each time period;
- 7.2. Determining the market-clearing price for each time period;
- 7.3. 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;
- 7.4. Prescribing guidelines for the market operation in system emergencies; and
- 7.5. Amending the rules.

Section 8. Separability. If for any reason, any section or provision of this Circular is declared unconstitutional or invalid, the other parts or provisions hereof which are not affected thereby shall continue to be in full force and effect.

Section 9. Repealing Clause. Except insofar as may be manifestly inconsistent herewith, nothing in this Circular shall be construed as to repeal any of the mechanisms already existing or responsibilities already provided for under existing rules.

Section 10. Effectivity and Publication. This Circular shall take effect immediately upon its publication in at least two (2) newspapers of general circulation, and shall remain in effect until otherwise revoked.

Issued on _____ 2017 at the Energy Center, Rizal Drive, Bonifacio Global City, Taguig City.

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Secretary