FEB 02 2023

LEGAL ADVISORY NO. 01, S. of 2023

TO	:	**ALL ELECTRIC COOPERATIVES (ECs)**
SUBJECT	:	**COMPUTATION OF TAXABLE GROSS RECEIPTS OF ECs BY LOCAL GOVERNMENT UNITS (LGUs)**

All ECs are reminded to strictly comply with the pronouncement earlier made on the matter by the Bureau of Local Government Finance, Department of Finance (BLGF-DOF) dated 28 November 2014, more particularly on the computation of the taxable gross receipts of ECs by LGUs, thus:

> "x x x
>
> In summary and for purposes of local taxation, ECs' gross receipts shall be as follows:
>
> Gross receipts:
> Less: Generation Charges
> Transmission Charges
> Reinvestment Fund
> Universal Charges
> System Loss Charges
>
> This accordingly modifies any other rulings or opinions which are inconsistent hereof, that this Bureau may have previously issued interpreting Section 3(b)(2) of LFC 1-07.
>
> x x x"

The copy of the subject letter from the BLGF-DOF addressed to then PHILRECA General Manager Wendell B. Ballesteros dated 28 November 2014 is hereto attached for ready reference.

For your information and guidance.

Atty. ROSSAN SJ ROSERO-LEE
Deputy Administrator for Legal Services

Noted by:

ANTONIO MARIANO C. ALMEDA
Administrator

NATIONAL ELECTRIFICATION ADMINISTRATION
Office of the Administrator
NEA-OA271077

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November 28, 2014

Mr. WENDELL B. BALLESTEROS
General Manager
Philippine Rural Electric Cooperative
Association, Inc.
4th Floor CASMAN Bldg
1198 Quezon Avenue
Quezon City

Sir:

This refers to your letter dated November 25, 2014, requesting on behalf of the electric cooperatives (ECs) throughout the country which comprises the membership of the Philippine Rural Electric Cooperatives Association, Inc. (PHILRECA), for a review and consideration of the exclusion of Generation Charges, Transmission Charges, System Loss Charges, Reinvestment Fund and Universal Charges from the taxable Gross Receipts of ECs.

Representations are made that currently, some of the member-electric cooperatives and may be sooner or later all of them will be encountering similar disagreeing interpretations on the provisions of the Local Finance Circular (LFC) No. 1-07, particularly on the exclusion of the Generation Charges, Transmission Charges, System Loss Charges, Reinvestment Fund and Universal Charges from Taxable Gross Receipts of the ECs which the LGUs contend that their revenues will be significantly reduced.

It is claimed that LGUs based their contention on the response of the Bureau of Local Government Finance (BLGF) to the letter of then Acting City Mayor of Laoag City, Hon. Edward Domingo on the same issue on August 12, 2008. While the letter expounded on the provisions of LFC No. 1-07, it seems that the confusion surfaced on the contents of said letter and may I quote:

> *"On the issue of generation charges, transmission charges, systems loss charges, universal charges and reinvestment fund, being excluded from the definition of gross receipts claimed by the ECs, which in your view partakes of the nature of the tax exemption, it may be clarified that even if such charges are not specifically spelled out in the definition it does not mean that it is excluded. Such charges, except reinvestment fund, are charges that are included in the Distribution Wheeling and Captive Market Supply and therefore cannot be regarded as exemption.*
>
> *To clarify further, LFC 1-07 does not exclude generation charges, transmission charges and system loss charges from gross receipts of ECs. Section 3 of said LFC is quoted, for guidance, as follows:……………*

Clearly, the only items excluded from the GR of ECs are NPC charges, Transmission Charges, Reinvestment Fund and Universal Charges. Apparently therefore, generation, transmission and system loss charges are not deductions from ECs' gross receipts."

To amplify the concerns of the ECs, PHILRECA apprised this Bureau of the series of events as follows:

1. Before the enactment into law of Republic Act No. 9136, "Electric Power Industry Reform Act of 2001", otherwise known as "EPIRA", the National Power Corporation (NPC) was the sole generation company that provides the power requirements of the electric cooperatives. Even though there were already Independent Power producers (IPPs) then, their capacities were being contracted by the NPC for sale to the Distribution Utilities including ECs and other NPC Customers. For the power to reach the NPC customers, it has to be transmitted through the transmission lines which were then owned by the National Transmission Company (TRANSCO). In these cases, the amounts collected by these two companies from their customers, are universally termed as Generation and Transmission Charges, respectively.

2. One of the declared policies of EPIRA was the privatization of the assets and liabilities as well as IPP contracts of the NPC which led to the creation of the PSALM. Such direction created a new set-up of the power industry where the ECs have to procure their power requirements from private generation companies other than from NPC. The situation was similar with the transmission system when it was acquired by the National Grid Corporation of the Philippines (NGCP) from TRANSCO through a concession agreement.

3. Under the new environment, the treatment of ECs generation and transmission costs remained as a pass through cost (revenue neutral for the ECs), the regulatory principle applied remained the same. As such, the collections of these charges do not result to any monetary benefit to the ECs as they are for the account of the Generation and Transmission Companies.

4. Another account that we seek for consideration to be excluded in the gross receipts of ECs is the system loss charge. The system loss charge is an account for recovery of generation and transmission costs influenced by the actual system loss of the ECs or the allowable system loss whichever is lower. The recovery of such costs is authorized by ERC under its Resolution No.16, Series of 2009, "Rules Governing the Automatic Cost Adjustment and True-Up Mechanism and Corresponding Confirmation Process for Distribution Utilities". Therefore, such amount is intended for the account of Generation and Transmission Companies.

5. Finally, Rule 7, Section 4(q) of the Implementing Rules and Regulations (IRR) of the Republic Act 9136 provides that: "A distribution Utility shall pay a franchise tax only on its distribution wheeling and Captive Market supply revenues"

Hence the request for the review and reconsideration of your concerns relative to the BLGF issuances, most especially at these times that the electric power industry is encountering a lot of difficulties.

Based on the representations made by PHILRECA, it would appear that even before the effectivity of the EPIRA, NPC was the sole generation company that provides the power requirements of the electric cooperatives to be transmitted through the transmission lines which were then owned by the National Transmission Company (TRANSCO).

This was the basis of the provisions of Section 3 (b) of Local Finance Circular (LFC) 1-07, dated June 28, 2007, quoted as follows:

> Section 3. Tax on Gross Receipts of ECs. – a) x x x
>
> b) For this purpose the franchise and business taxes shall be based on EC's gross receipts as follows:
>
> 1. Before the effectivity of the EPIRA Law (1997-2001), franchise and business taxes shall be based on the total gross receipts pursuant to Section 131(n) of the LGC;
>
> 2. Upon the effectivity of the EPIRA Law (2002), the basis shall be as follows:
>
> Gross receipts:
> Less: NPC Charges
> TransCo Charges
> Reinvestment Fund
> Universal Charges

In this connection and for purposes of clarification, this Bureau takes cognizance of the following terms:

"Generation Rate" shall mean the cost of power generated and sold to the distribution utility by the National Power Corporation (NPC) as well as the Independent Power Producers (IPPs), which shall be passed on to the DU's customers, as calculated in the formula prescribed in these Guidelines. *(ERC Guidelines for the Automatic Adjustment of Generation rates and system loss rates by Distribution Utilities, October 13, 2004)*

"Transmission Charge" refers to the regulated cost or charges for the use of a transmission system which may include the availment of ancillary services. *(Section 4 [aaa], R.A. No. 9136: Electric Power Industry Reform Act.*

On the basis of the above definition of terms, it is safe to infer that the NPC Charges and TransCo Charges would also mean generation charges and transmission charges, respectively, which do not form part of the gross receipts of ECs.

Moreover, as mentioned above, the privatization of the assets and liabilities as well as IPP contracts of the NPC led to the creation of the PSALM. Hence a new set-up of the power industry where the ECs have to procure their power requirements from private generation companies other than from NPC. The situation was similar with the transmission system when it was acquired by the National Grid Corporation of the Philippines (NGCP) from TRANSCO through a concession agreement on December 1, 2008.

In view of the new set-up and for purposes of uniformity, the charges collected for the generation of power and the charges collected for the transmission of power should be universally termed as generation charges and transmission charges, respectively. These generation and transmission charges do not form part of the gross receipts of ECs, which is in conformity with the provisions of Section 4(q), Rule 7, of the Implementing Rules and Regulations (IRR) implementing R.A. No. 9136 which states that " Distribution Utility shall pay a franchise tax only on its distribution wheeling and Captive Market supply revenues. x x x."

With respect to the system loss charge, considering the claim of PHILRECA that the charge is an account for recovery of generation and transmission costs influenced by the actual system loss of the ECs thus, intended for the account of Generation and Transmission Companies, the same does form part of the gross receipts of ECs.

It must be stressed that LGUs may directly impose local taxes on charges being remitted by ECs to the entities concerned such as NPC and other private generation companies, as well as transmission company and/or NGCP.

In summary and for purposes of local taxation, ECs' gross receipts shall be as follows:

Gross receipts:
Less:
- Generation Charges
- Transmission Charges
- Reinvestment Fund
- Universal Charges
- System Loss Charges

This accordingly modifies any other rulings or opinions which are inconsistent hereof, that this Bureau may have previously issued interpreting Section 3(b)(2) of LFC 1-07.

We hope that this will help clarify issues that may have cause confusion relative to various charges excluded in the computation of gross receipts of ECs for local taxation purposes.

Very truly yours,

SALVADOR M. DEL CASTILLO
OIC-Executive Director