

Research Brief on Energy

Financial Assessment of NGCP

Office of Senator Win Gatchalian

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Version 1

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Financials

1. The consortium that eventually became the National Grid Corporation of the Philippines must pay the Power Sector Asset Liability Management Corporation a total of \$3.95 billion (₱196.6 billion in current peso) for the concession rights. The 25% of the concession fee was payable immediately while the remaining 75% is payable in 40 semi-annual payments. The deferred payments are subject to interest rates initially at a rate “10 Year PDST-F” plus 2.3% and subject to review after the second regulatory period. NGCP, as the concessionaire is entitled to prepay the deferred payment for as long as they have no account due to Transco or PSALM. NGCP’s motivation to prepay the deferred concession stems from the interest expense the company is incurring for the deferred payments. From 2009 to 2012, NGCP spent Php 43 billion on interest expense alone.
 - On January 2009, NGCP paid PSALM \$987.5 million which represents 25% of concession fee.
 - The remaining \$2.962 billion converted into peso at a fixed rate of Php 42.65/USD for a total of Php 126.6 billion is payable in 40 semi-annual payments.
 - On July 2013, NGCP prepaid the concession fees for the period of January 2014 to January 2024 for a total amount of Php 57.88 billion. The prepayment was financed by NGCP through a combination of peso corporate bond and dollar denominated loans. Significant reduction in interest expense of NGCP can be observed after the prepayment of the concession fee. This means that the rates for the loans availed by NGCP were much lower than the interest rate of the deferred payments to the government.
 - As of 2015, NGCP has a remaining concession fee payable amounting to Php 54.3 billion. These payments are due from 2024 to 2034 and can also be prepaid by NGCP if they intend to.
2. The National Grid Corporation of the Philippines took over the operation of transmission facilities with a starting capital of Php 46 billion or around \$1 billion. The \$ 1 billion was used to pay for the 25% concession fee.
3. National Grid Corporation has been profitable since the start of its transmission operations in 2009. In 2009, NGCP reported revenues of Php 39.53 billion and net income of Php 15.42 billion. As of 2015, revenues of NGCP reached Php 45.70

billion while net income reached Php 22.51 billion. (Refer to Table 1 for yearly financials of NGCP).

4. Being a regulated entity, revenues of NGCP is dictated by the Energy Regulatory Commission. The ERC sets a Maximum Allowable Revenue (MAR) for NGCP every year. This means that the revenue of NGCP is controlled by the government. The ERC follows the Transmission Wheeling Rate Guidelines (TWRG) in setting the MAR of NGCP. The MAR of NGCP is shown in Table 1. The NGCP's MAR closely match the actual revenues of NGCP. The difference is mostly from connection charges that NGCP charge new customers. There are also instances where the MAR is not approved by the ERC prior to the year of implementation. These causes differences in MAR and actual revenues

Table 1. NGCP Key Financials from 2009 to 2015, Php Billions

Year	Maximum Allowable Revenue (Set by ERC)	Revenue	EBITDA	Operating Income	Net Income
2009	39.51	39.53	33.32	26.42	15.42
2010	44.99	45.21	36.45	28.76	18.57
2011	44.89	45.61	38.01	30.89	21.60
2012	42.90	44.60	37.32	30.18	20.84
2013	44.57	44.52	36.24	28.77	21.19
2014	42.51	45.19	36.60	29.08	22.06
2015	43.08	45.70	37.36	29.57	22.51

Source: Securities and Exchange Commission

5. NGCP's ample earnings for the past seven years has allowed it to cover concession fees, capital expenditures, and at the same time return money to its investors. Table 2 shows the income, capex, free cash flow, and dividends of NGCP. The company generated abundant free cash flow available for dividend distributions from 2009 to 2015. NGCP declares yearly dividends to return excess cash to its shareholders. In fact, the investors in NGCP (State Grid, Sy Family, Coyiuto) recouped their initial \$ 1 billion investment in NGCP in just a matter of four years in operation. The cumulative dividends they received from 2009 to 2012 reached Php 61.84 billion. By 2015, cumulative dividends received totaled Php 130.84 billion, more than double their initial investments.
6. NGCP's concession agreement for the operations of transmission grid lasts until 2034. The company provides stable earnings for its investors. The income of the company is more than enough to cover capital expenditures which means

consistent dividends for shareholders moving forward. Reports also indicate that NGCP is keen on listing the company in the stock market¹. An Initial Public Offering of NGCP can provide the company additional capital to prepay concession fees due 2024 to 2034 without compromising dividend declaration.

Table 2. NGCP Cash Flows and Dividends, Php Billions

Year	EBITDA	Capex and Concession Fee*	Estimated Free Cash Flow	Dividends	Cumulative Dividends
2009	33.32	2.81	30.51	6.84	6.84
2010	36.45	6.66	29.79	15.00	21.84
2011	38.01	13.58	24.43	22.00	43.84
2012	37.32	9.33	27.99	18.00	61.84
2013	36.24	12.36	23.88	24.00	85.84
2014	36.60	12.55	24.05	24.00	109.84
2015	37.36	16.40	20.96	21.00	130.84

Source: Securities and Exchange Commission, Computation from O/S Gatchalian *Excludes the initial 25% concession fee and the prepaid concession fees

Tax Treatment of NGCP

7. R.A. 9511, which granted NGCP the franchise to operate our transmission assets provides preferential tax treatment to NGCP. Section 9 of RA 9511 states ***“the Grantee, its successors or assigns, shall pay a franchise tax equivalent to three percent (3%) of all gross receipts ...in lieu of income tax and any and all taxes, duties, fees and charges of any kind, nature or description levied, established or collected by any authority whatsoever, local or national, on its franchise, rights, privileges, receipts, revenues and profits, and on properties used in connection with its franchise, from which taxes, duties and charges, the Grantee is hereby expressly exempted”***.
 - An ERC decision in 2010 stated that the **3% franchise tax cannot be deducted from NGCP’s maximum allowable revenue** but will be recovered through a surcharge on customer’s invoices. **The franchise tax is essentially passed on to consumers. The consumers are paying the franchise tax of NGCP. NGCP is paying no taxes at all on its income.**

¹ <http://www.philstar.com/business/2017/05/08/1697635/ngcp-commits-offer-shares>

8. The special tax treatment of NGCP can be included in the current tax reform of the Duterte administration. Levying a regular corporate income tax to NGCP would give the government significant revenues. Table 3 shows tax revenues the government could have generated if we tax NGCP at 30%.

Table 3. Tax Revenue lost due to Preferential Tax Treatment of NGCP

Year	2009	2010	2011	2012	2013	2014	2015
Tax Revenues	4.63	5.57	6.48	6.25	6.36	6.62	6.75

Source: Securities and Exchange Commission, Computation from O/S Gatchalian