Senate
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SEVENTEENTH CONGRESS OF THE)
REPUBLIC OF THE PHILIPPINES)
First Regular Session)

SENATE

S. B. No. **765** RECEIVED BY:

Introduced by **Senator FRANCIS G. ESCUDERO**

AN ACT
ORDAINING THE DEVELOPMENT OF THE DOWNSTREAM NATURAL GAS INDUSTRY, CONSOLIDATING FOR THE PURPOSE ALL LAWS RELATING TO THE TRANSMISSION, DISTRIBUTION AND SUPPLY OF NATURAL GAS AND FOR OTHER PURPOSES

EXPLANATORY NOTE

Natural gas is considered by many modern economies as the fuel of choice because of its abundance, clean-burning properties and versatility as a fuel source. With the successful launching of the Malampaya Deep Water Gas-to-Power Project on October 16, 2001 marked the birth of the country's natural gas industry. The Malampaya gas field discovery signaled a significant leap towards energy self-reliance as it now fuels about one-third of the country's total power generation. A total of 2700 MW of installed capacity of gas-fired power plants make use of the natural gas produced from Malampaya.

Aside from the use of natural gas for power generation, alternative applications in the transport sector is also being pursued. The launching of the Natural Gas Vehicle Program for Public Transport (NGVPPT) on October 16, 2002 served as a banner program for the use of natural gas in the transport sector.

Following the inauguration of the Malampaya Deep Water Gas-to- Power Project, government advocacy has been initiated to create an impetus to the development of the country's downstream natural gas industry. These are the (i) signing on January 18, 2002 by President Gloria Macapagal-Arroyo of Executive Order No. 66 designating the Department of Energy (DOE) as the lead agency for the development of the country's natural gas industry; and (ii) issuance on August 27, 2002 by the DOE of the interim rules and regulations governing the transmission, distribution and supply sub-sectors of the natural gas industry.

However, both issuances are not sufficient to impart a clear, comprehensive and integrated regulatory framework that will provide direction and to accelerate the development of the country's nascent downstream natural gas sector.

As dynamic developments are taking place in this very young sector, it is imperative that conditions favorable to the establishment of the critical infrastructure and natural gas market are put in place to optimize economic efficiency and returns from the downstream natural gas industry.

The foregoing premises thus necessitate the immediate passage of the Natural Gas Bill, which proposal has remained pending for a considerable time to date.

FRANCIS G. ESCUDERO

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ORDAINING THE DEVELOPMENT OF THE DOWNSTREAM NATURAL GAS INDUSTRY, CONSOLIDATING FOR THE PURPOSE ALL LAWS RELATING TO THE TRANSMISSION, DISTRIBUTION AND SUPPLY OF NATURAL GAS AND FOR OTHER PURPOSES

Be it enacted by the Senate and the House of Representatives of the Republic of the Philippines in Congress assembled:

CHAPTER I
TITLE AND DECLARATION OF POLICY

SECTION 1. *Short Title.* – This Act shall be known as the *"Downstream Natural Gas Industry Development Act".*

SEC. 2. *Declaration of Policy.* – It is hereby declared the policy of the State:

(a) To promote the role of natural gas as a socially-acceptable, environment-friendly and economically efficient source of energy by creating favorable conditions for establishing a Downstream Natural Gas Industry for the benefit of all segments of the nation's population and all sectors of its economy;

(b) To ensure the safety, quality, reliability and security of the transmission, distribution and supply of natural gas;

(c) To ensure transparent and reasonable rates and prices of natural gas transmission, distribution and supply in a regime of open and fair competition and full public accountability that will promote greater operational and economic efficiency and the enhanced competitiveness of the Philippine products in the global market;

(d) To encourage the inflow of private capital in providing the infrastructure and services necessary to support an expanded role of natural gas in the nation's energy supply;

(e) To protect the public interest as it is affected by the quality of, and rates charged for, the transmission, distribution and supply of natural gas and related services;

(f) To assure the development of a Downstream Natural Gas Industry infrastructure that is socially-acceptable and compliant with existing environmental laws;

(g) To ensure that the Downstream Natural Gas Industry shall be regulated in a manner that will ensure the quality, reliability, security and reasonableness of charges for the transmission, distribution and supply of natural gas, encourage private investment in the Downstream Natural Gas Industry and promote the efficient and competitive operation thereof;

(h) To develop the necessary trades, technical expertise and skills to support the Downstream Natural Gas Industry;

(i) To facilitate the development of end-uses of natural gas that promotes fuel diversity and compliance with existing environmental laws including, but not limited to, the use of natural gas as a motor vehicle fuel; and

(j) To encourage equity participation in gas transmission utilities and gas distribution utilities by the private sector.

SEC. 3. *Scope.* - This Act shall provide a framework for the development of a Downstream Natural Gas Industry and its transition from an emerging to a mature industry status and competitive natural gas market, and define the responsibilities of various government agencies and private entities in furtherance of this national goal.

All activities of the Department of Energy (DOE) and the Energy Regulatory Commission (ERC) relevant to the development and regulation of the Downstream Natural Gas Industry shall be in accordance with this Act.

SEC. 4. *Definition of Terms.* - As used in this Act, the following terms shall have the following meanings:

(a) "Captive market":

- with respect to the transmission of natural gas, refers to natural gas end-users who do not have a choice of a gas transmission utility;
- with respect to the distribution of natural gas, refers to natural gas end-users who do not have a choice of a gas distribution utility;
- with respect to the supply of natural gas, refers to natural gas end-users who do not have a choice of supplier of natural gas or other economically competitive energy substitute;

(b) "Congress" refers to the Congress of the Republic of the Philippines;

(c) "Contestable market" is a market that is not a captive market;

(d) "Delivery" refers to the transmission or distribution of natural gas and the supply of natural gas, at wholesale or retail;

(e) "Department of Energy" or "DOE" refers to the government agency created pursuant to Republic Act No. 7638, as amended

(f) "Department of Environment and Natural Resources" or "DENR" refers to the government agency created pursuant to Executive Order Nos. 192 and 292, as amended;

(g) "Distribution" refers to the conveyance of natural gas by a gas distribution utility through its gas distribution system;

(h) "Downstream Natural Gas Industry" refers to the transmission, distribution and supply of natural gas and related activities, such as, but not limited to, processing, storing, regasification, interconnection, measurement and/or metering;

(i) "End-user" refers to any person that will receive delivery of natural gas for its own use;

(j) "Energy Regulatory Commission" or "ERC" refers to the independent quasi-judicial regulatory agency created pursuant to Republic Act No. 9136, otherwise known as the "Electric Power Industry Reform Act of 2001", whose expanded functions are provided in this Act;

(k) "Franchise" refers to the right, privilege and authority issued by Congress authorizing a person to engage in the transmission of natural gas and/or distribution of natural gas within a specific geographical area;

(l) "Franchise area" refers to a geographical area assigned or granted under a franchise;

(m) "Gas Distribution Code" refers to the code to be formulated by the DOE pursuant to Section 5(g) of this Act that sets the technical performance standards for operating gas distribution utilities and the minimum financial standards for gas distribution systems;

(n) "Gas distribution system" refers to the system of pipelines and related facilities extending from the delivery points where the gas distribution system receives the natural gas to the point of connection to the premises of the end-user;

(o) "Gas distribution utility" refers to any person that has a franchise to operate a gas distribution system;

(p) "Gas supply contract" refers to a contract between a supplier and a purchaser for the supply of natural gas;

(q) "Gas Transmission Code" refers to the code to be developed by the DOE pursuant to Section 5(g) of this Act that sets the technical performance standards for operating gas transmission systems and the minimum financial standards for gas transmission utilities;

(r) "Gas transmission system" refers to the system to the system of high pressure pipelines, storage and related facilities that are used to transport natural gas from the interconnection with gathering facilities, liquefied natural gas (LNG) regasification facilities or other gas transmission systems to gas distribution systems, other gas transmission systems or end-users;

(s) "Gas transmission utility" refers to any person that has a franchise to operate or intending to operate a gas transmission system except own-use pipelines;

(t) "Gathering facilities" refers to natural gas pipelines and related facilities used to gather gas in the field and bring it to a location for processing or for delivery at an interconnection with the gas transmission system. The terms "gather" and "gathering" shall be construed accordingly;

(u) "Infrastructure development period" refers to the period prescribed in Chapter IV of this Act;

(v) "Joule" refers to the unit of energy or work done when the point of application of a force of one Newton is displaced a distance of one meter in the direction of the force. It is also equal to one watt-second;

(w) "Large end-user" refers to an end-user whose aggregate annual natural gas consumption is one thousand (1,000) gigajoules (gross heating value) or greater, as may be determined by the ERC;

(x) "LNG' refers to liquefied natural gas";

(y) "Natural gas" refers to hydrocarbons, obtained initially from sub-surface reservoirs, primarily methane, which, at atmospheric temperature and pressure, is in a gaseous phase. The term "natural gas" shall include LNG;

(z) "Permit" refers to an authorization issued by the DOE, initially, for the construction, operation, expansion and modification of gas transmission systems, gas distribution systems and for the supply of natural gas;

(aa) "Person" refers to a natural or juridical person, as the case may be, including the national and local government of the Republic of the Philippines, its agencies and instrumentalities, and government-owned and -controlled corporations;

(bb) "Petroleum operations" refers to searching for and obtaining petroleum within the Philippines through drilling and pressure or suction or the like, and all other operations incidental thereto. It includes the transportation, storage, handling and sale (whether for export or for domestic consumption) of petroleum so obtained but does not include any: (1) transportation of petroleum outside the Philippines; (2) processing or refining at **a** refinery; or **(3)** any transaction in the products so refined;

(cc) "Philippine Energy Plan" or "PEP" refers to the overall energy program formulated and updated yearly by the DOE and submitted to Congress pursuant to Republic Act No. 7638, as amended;

(dd) "Service contract" refers to the award granted by the Philippine government to a qualified person to engage in the exploration, development and utilization of natural resources *rough joint venture, co-production, production-sharing or other similar arrangement with the State pursuant to Article XII, Section 2 of the Constitution, including service contracts under Presidential Decree No. 87, as amended;

(ee) "Supplier" refers to any person authorized by the DOE, initially, to engage in the supply of natural gas;

(ff) "Supply" refers to the domestic trading and/or sale of natural gas for wholesale or retail;

(gg) "Transmission" refers to the transportation of natural gas through a gas transmission system; and

(hh) "Unbundled service" refers to the pricing of the energy value of natural gas separately from the rates charged for natural gas transmission or distribution

CHAPTER II
POWERS AND FUNCTIONS OF THE DOE AND THE ERC

SEC. 5. *Powers and Functions of the DOE.* - In addition to its existing powers and functions, the DOE shall have the overall responsibility of supervising and monitoring the development of the Downstream Natural Gas Industry and regulation of the construction and operation of natural gas pipelines and related facilities for the transmission, distribution and supply of natural gas. Towards this end, the DOE shall have the following-powers and functions:

(a) Prepare and periodically update a Downstream Natural Gas Industry Development Plan (DNGIDP) and integrate the same into the PEP. The DNGIDP shall consider and integrate the individual or joint development plans of the Downstream Natural Gas Industry participants pursuant to this Act, which are submitted to the DOE. Appropriate mechanisms shall be provided to protect the confidentiality of any information that is

commercially or competitively sensitive. The DOE shall publish an initial draft of the plan and undertake public consultations thereon prior to its adoption;

(b) Issue permits for the construction, operation and maintenance of pipelines and related facilities for the transmission, distribution and/or supply of natural gas;

(c) Establish standards setting forth the characteristics for classifying pipeline and pipeline-related facilities either as gas transmission systems or gas distribution systems. These characteristics may include both the physical characteristics related to the diameter, size and pressure of pipeline facilities, and the functional characteristics of such facilities;

(d) Before the end of April of each year, submit to the Office of the President and Congress an annual report;

(e) Ensure the safety, reliability, quality and security of supply of natural gas. Consistent with the development of the Downstream Natural Gas Industry, the DOE shall, among others:

(i) Encourage private sector investments in the Downstream Natural Gas Industry and promote the development of domestic markets for natural gas;

(ii) In consultation with the Downstream Natural Gas Industry participants and other government agencies, promote a system of incentives to encourage industry participants, including new producers and end-users, to provide adequate and reliable supply of natural gas; and

(iii) Undertake, in coordination with other governmental agencies, as appropriate, an information campaign to educate the public on the benefits of developing the Downstream Natural Gas Industry and the potential for utilizing natural gas as a source of energy.

(f) Within six months from the effectivity of this Act, develop plans and programs to encourage market development and customer choice;

(g) Within twelve (12) months from the effectivity of this Act, the DOE shall, preparatory to the holding of public consultations with the Downstream

Natural Gas Industry participants, draft *the* Gas Transmission and Distribution Codes which shall contain, among others, the following:

(i) Technical performance standards for gas transmission and distribution utilities: *Provided,* That in the establishment of the performance standards, the nature and function of the entities shall be considered; and

(ii) Minimum financial capability standards for gas transmission and distribution utilities: *Provided,* That such standards are set to ensure that the Downstream Natural Gas Industry participants meet the minimum financial standards to protect the public interest.

Within eighteen (18) months from the effectivity of this Act, the DOE shall, in consultation with the Downstream Natural Gas Industry participants, issue the final Gas Transmission and Distribution Codes.

(h) By order, revoke, after due notice and hearing, the permit of any person that fails to comply with the rules and regulations promulgated pursuant to this Act, the Gas Transmission Code, *the* Gas Distribution Code, or any requirement of this Act. The DOE shall allow such persons sufficient time to remedy the violation of or for an orderly disgorgement, when applicable, but in no case shall such remediation period exceed twelve (12) months from the date of issuance of the order;

(i) Encourage private enterprises in the Downstream Natural Gas Industry to broaden their ownership base and promote widest public ownership thereof;

(j) Formulate, in consultation with the Downstream Natural Gas Industry participants, the rules and regulations as may be necessary to implement the objectives of this Act;

(k) Exercise original and exclusive jurisdiction over all cases contesting permits, nonprice regulation, fees, fines and penalties imposed by it in the exercise of the abovementioned powers and functions; and

(l) Exercise such other powers and functions as may be necessary or incidental to attain the objectives of this Act. Subject to existing rules and regulations, the DOE is hereby authorized to create offices and appoint personnel thereto as may be necessary to efficiently and effectively perform its functions as stipulated in this Act.

SEC. 6. *Powers and Functions of the ERC.* - In addition to its existing powers and functions, the ERC shall have the sole regulatory responsibility for establishing the rates and related terms and conditions of service for the transmission, distribution and supply of natural gas to the extent that such activities are regulated pursuant to the requirements set forth in this Act. It shall:

(a) Within one year from the effectivity of this Act, promulgate, upon due notice and public consultation, rules and regulations to promote competition and prohibit/penalize abuse of market power, cartelization and any anti-competitive or discriminatory behavior, in order to further the intent of this Act and protect the public interest. Such rules and regulations shall:

(i) Define the relevant product and geographic markets for purposes of establishing anti-competitive conduct;

(ii) Provide criteria to determine the relevant market structure; and

(iii) Establish the periodic reportorial requirements of the Downstream Natural Gas Industry participants as may be necessary to enforce the provisions of this section.

(b) In the public interest, establish and enforce a methodology for setting transmission, distribution and supply rates, taking into account all relevant Considerations, including the efficiency or inefficiency of the regulated entities. The rates must be such as to allow the recovery of just and reasonable costs and a reasonable return to enable the entity to operate viably. The ERC may, upon due notice and public consultation, adopt internationally accepted rate setting methodology. The rate setting methodology so adopted and applied shall promote efficiency and ensure a reasonable price or tariff. The rates prescribed shall be nondiscriminatory;

(c) Apply administrative procedures that will ensure the constitutional right to due process;

(d) Before the end of April of each year, submit to the Office of the President of the Philippines and Congress, copy furnished the DOE, an annual report containing such matters or cases which have been filed before or referred to it during the preceding year, the actions and proceedings undertaken and its decision or resolution in each case. The ERC shall make copies of such report available to any interested party upon payment of a charge which reflects the printing costs;

(e) Publish in newspapers of general circulation all its decisions involving rates and anticompetitive cases; and

(f) Exercise such other powers as may be necessary or incidental to attain the objectives of this Act.

Subject to existing rules and regulations, the ERC is hereby authorized to create offices and appoint personnel thereto as may be necessary to efficiently and effectively perform its functions as stipulated in this Act.

CHAPTER III
ORGANIZATION AND OPERATION OF THE DOWNSTREAM NATURAL GAS INDUSTRY

SEC. *7. Organization.* - For purposes of this Act, the Downstream Natural Gas Industry shall be divided into three sectors, namely: transmission of natural gas, distribution of natural gas and supply of natural gas.

SEC. *8.Regulation* of *Transmission, Distribution and Supply Sectors.* – The transmission, distribution and supply of natural gas are businesses affected with public interest and the regulation of these businesses as provided for in this Act is hereby deemed necessary in the public interest.

SEC. 9. *Franchise Requirement.* –

(a) Transmission and distribution of natural gas declared public utility operations. - The transmission and distribution of natural gas as provided for in this Act are hereby declared to be public utility operations, requiring a franchise;

(b) Franchise. - Any person that seeks to operate for commercial purposes a gas transmission system or gas distribution system shall be required to obtain a franchise, any law to the contrary notwithstanding. The franchise requirement shall apply with respect to all gas transmission systems and gas distribution systems, regardless of the size or pressure of the pipeline. The foregoing, notwithstanding, this franchise requirement shall not apply to:

(i) Holders of service contracts which authorizes the construction and operation of facilities for the transmission of natural gas only to the extent that such facilities are: (1) for own use; (2) used to transport natural gas from the point of extraction or production to the processing or gathering facility; and (3) used to provide service to existing customers or such person under a gas supply contract entered into prior to the effectivity of this Act, which gas supply contract shall not be affected by &e enactment of this Act.

However, the operation of any pipeline facility used to serve or deliver natural gas to third persons, whether or not such facility was, prior to such operation, previously utilized only as a gathering facility, shall require a franchise.

(ii) Operators of pipeline facilities to transport natural gas for their own use: Provided, however, That such operators shall secure a permit from the DOE as provided herein; and

(iii) Operators of related facilities that are operated independently from the pipeline.

The franchise so granted shall include a provision that shall honor and protect the forty percent (40%) share of local government units (LGUs) from the proceeds of the gross collection derived by the national government from its share in any coproduction, joint venture or production-sharing agreement in the utilization and development of the national wealth within their territorial jurisdiction, pursuant to Article X, Section 7 of the Constitution and Section 290 of Republic Act No. 7160, otherwise known as the Local Government Code of 1991, as amended. The share of the LGU concerned shall be included automatically in the

General Appropriations Act following the year the revenue was generated.

(c) Prior regulatory approvals. - The grantee of such franchise shall also be required to secure from the DOE a permit as provided herein, and to secure from the appropriate government agencies all other regulatory approvals, licenses, permits and authorizations applicable to such grantee under existing laws. The DOE shall not unreasonably withhold or delay the grant of any permit, and may not reopen any legislative determination in the review and grant of any franchise.

SEC. 10. *Philippine Ownership Requirement.* - As required under Article XII, Section 11 of the Constitution of the Republic of the Philippines, no franchise, certificate, or any other form of authorization of a public utility shall be granted except to citizens of the Philippines or to- corporations or associations organized under the laws of the Philippines at least sixty percent (60%) of whose capital is owned by such citizens.

SEC. 11. *Third Party Access.* –

(a) Third Party Access Obligation. - Gas transmission systems and gas distribution systems excluding those constructed and operated for own use or as part of gathering facilities of service contractors shall be available for nondiscriminatory access by third party users which may include parties to a service contract, suppliers and customers, with due regard to the economic viability of the operation of such facilities. Such operators shall negotiate in good faith with third party users the provisions and terms of access in accordance with the guidelines to be promulgated by the DOE;

(b) Available Capacity. - Third party access obligations shall apply only to the available capacity of the gas transmission systems and gas distribution systems as determined by subtracting from the design capacity of the gas transmission systems and gas distribution systems the volume of capacity that is:

(i) Used by the owner or operator to serve his own customer; and/ or

(ii) Allocated to third parties under transportation contracts. Nondiscriminatory third party access shall be available to users by contract with the gas transmission or gas distribution utility. If the gas transmission or gas distribution utility with available capacity refuses service to a user or offers discriminatory service, the affected party may request for the intervention of the ERC. The gas transmission or gas distribution utility shall be required to file proof that capacity was not available when service was denied.

Gas transmission utilities shall not be obligated to undertake, nor may the DOE require, the expansion of an existing gas transmission system to serve additional customers or the sizing of a gas transmission system for the purpose of increasing capacity to serve load in excess of the load proposed to be served by the gas transmission utility. However, in situations where no entity is interested to build additional transmission capacity in any franchise area, the DOE may conduct a public bidding and award the same to the lowest bidder.

(c) Deferment of Third Party Access Obligation. - As may be provided in the permit, the implementation of third party access to gas transmission systems and gas distribution systems may be deferred where, upon the determination by the DOE:.

(i) It can be demonstrated that such deferment is necessary to enable the efficient planning of the infrastructure and aggregation of the initial demand necessary to justify investments in the gas transmission systems and gas distribution systems; or

(ii) It is in the interest of the customers served by the gas transmission system and gas distribution system to ensure stability of supply.

In either case, the DOE may not defer implementation of third party access for a period longer than three years after completion of construction in the case of gas transmission systems and five years after completion of construction in the case of gas distribution systems: *Provided, however,* That the deferment period may be extended on reasonable grounds.

(d) Approved Access Conditions for Gas Transmission Utilities and Gas Distribution Utilities. - Prior to the conduct of negotiations with third parties, a gas transmission utility and a gas distribution utility shall request the DOE to approve its access conditions in accordance with the third party access guidelines to be promulgated by the DOE in consultation with the industry participants.

SEC. *12.Environmental Protection.* - Gas transmission utilities, gas distribution utilities and suppliers shall comply with all environmental laws, rules, regulations and standards promulgated by the Department of Environment and Natural Resources (DENR) and other appropriate governmental agencies.

CHAPTER IV
NATURAL GAS TRANSMISSION SECTOR

SEC. 13. *Permit.* - No person or entity shall undertake the construction, operation and maintenance of a natural gas transmission system unless it has secured a franchise: *Provided, however,* That for a period not exceeding five years after the effectivity of this Act, the DOE may issue a provisional permit with a maximum term of two years, renewable twice for a maximum cumulative term not exceeding six years for the continued operation of a gas transmission system constructed prior to and in operation as of the date of effectivity of this Act: Provided, further, That during the same period, the DOE may issue a permit for the expansion, extension or modification of a natural gas transmission system.

The DOE shall issue a public notice of all permit applications and afford interested parties reasonable opportunity to comment upon such applications. The DOE shall issue a permit upon its determination that the construction, ownership, control, installation, operation and maintenance of the gas transmission system would be consistent with ;the policy declarations contained in this Act: Provided, however, That if a permit is sought for new service that would be provided within the franchise area of a gas distribution utility, the DOE shall consider the economic effects of granting such a permit upon the gas distribution utility and its customers.

SEC. 14.*Terms and Conditions of Permits.* - In issuing a permit, the DOE shall have the power to impose such reasonable terms and conditions as the public interest may require. Among such conditions shall be the requirement that the permit holder complies in full with the Gas Transmission Code promulgated by the DOE pursuant to Section 5(g) of this Act.

SEC. 15. *Fees.* - The DOE shall have the authority to prescribe and collect fees and charges relating to the issuance and/or review of permits, supervision and regulation of gas transmission systems.

SEC. 16. *Abandonment of Gas Transmission Systems.* - No holder of a permit for the construction, installation, operation or maintenance of a gas transmission system shall abandon or withdraw from service any portion of such gas transmission system without obtaining prior authorization from the DOE, which determination shall be made within one hundred eighty (180) days from the filing of the application for abandonment. Such abandonment shall be done in accordance with existing laws.

SEC. 17. *Gas Transmission Code Compliance.* - All gas transmission utilities shall ensure the safety,- reliability, adequacy, security, stability and integrity of their gas transmission systems in accordance with the technical specifications and performance standards set forth in the Gas Transmission Code to be promulgated by the DOE. Each gas transmission utility shall submit to the DOE a statement of its compliance with such technical specifications and performance standards prescribed in the Gas Transmission Code. Any gas transmission utility that does not comply with any of the prescribed technical specifications or performance standards shall include in such statement of compliance an undertaking to comply with said technical specifications and performance standards within a reasonable time as may be necessary to ensure safety and reliability, or prevent environmental harm. The DOE shall, within sixty (60) days upon receipt of such plan, evaluate the same and notify the gas transmission utility concerned of its decision thereon. Failure to submit a feasible and credible plan and/or failure to implement the same shall serve as grounds for the imposition of appropriate sanctions, fines or penalties pursuant to Section 39 of this Act.

SEC. 18. *ERC Rate Regulation of Gas Transmission Utilities.* - Gas Transmission Rate. Except as otherwise provided during the infrastructure development period, the ERC shall review and approve the rates, charges and other amounts proposed to be charged by the gas transmission utilities as provided under Section 33 of this Act. Where such rates are applicable to services provided to captive markets, the ratemaking methodology to be applied by the ERC shall be based on the principle of full recovery of prudent and reasonable costs incurred, including a reasonable return on rate base that is consistent with the encouragement of private investment and goal of developing a Downstream Natural Gas Industry infrastructure, or such other principles that will promote the determination of just and reasonable rates. Where a rate applicant successfully demonstrates that its rates will be applicable to contestable markets, the ERC shall have the authority to permit negotiated rates.

CHAPTER V
DISTRIBUTION SECTOR

SEC. 19. *Permit.* - No person or entity shall undertake the construction, operation and maintenance of a natural gas distribution system unless it has secured a franchise: Provided, however, That for a period not exceeding five years after the effectivity of this Act, the DOE may issue a provisional permit with a maximum term of two years, renewable twice for a maximum cumulative term not exceeding six years for the continued operation of a gas distribution system constructed prior to and in operation as of the date of effectivity of this Act: Provided, further, That during the same period, the DOE may issue a permit for the expansion, extension or modification of a natural gas distribution system.

The DOE shall issue a public notice of all permit applications and afford interested parties an opportunity to comment on such applications. The DOE shall issue a permit upon its determination that the construction, ownership, control, installation, operation and maintenance of the gas distribution systems would be consistent with the policy declarations contained in this Act: Provided, however, That if a permit is sought for new service that would be provided within the franchise area of another gas distribution utility, the DOE shall consider the economic effects of granting such a permit upon the gas distribution utility and its customers.

SEC. 20. *Terms and Conditions of Permits.* - In issuing a permit, the DOE shall have the power to impose such reasonable term and conditions to a permit as the public interest may require. Among such conditions shall be the requirement that the permit holder comply in full with the Gas Distribution Code promulgated by the DOE pursuant to Section 5(g) of this Act.

SEC. 21. *Fees.* - The DOE shall have the authority to prescribe and collect fees and charges relating to .the issuance and/or review of permits, supervision and regulation of gas distribution systems.

SEC. 22. *Abandonment of Gas Distribution Systems.* - No holder of a permit for the construction, installation, operation or maintenance of a gas distribution system shall abandon or withdraw from service any portion of such gas distribution system without obtaining prior authorization from the DOE, which determination shall be

made within one hundred eighty (180) days from the filing of the application for abandonment. Such abandonment shall be done in accordance with existing laws.

SEC. 23. *Gas Distribution Code Compliance.* - All gas distribution utilities shall be required to ensure and maintain the safety, reliability, adequacy, security, stability and integrity of their gas distribution systems in accordance with the performance standards set forth in the Gas Distribution Code to be promulgated by the DOE. Each gas distribution utility shall submit to the DOE a statement of its compliance with the technical specifications prescribed in the Gas Distribution Code and the performance standards prescribed in the implementing rules and regulations promulgated by the DOE pursuant to Section 43 of this Act. A gas distribution utility that fails to comply with any of the prescribed technical specifications or performance standards shall include within such statement of compliance a plan for achieving compliance with the said technical specifications and performance standards within a reasonable time as may be necessary to ensure safety and reliability, or prevent environmental harm. The DOE shall, within sixty (60) days from receipt of such plan, evaluate the same and notify the gas distribution utility concerned of its decision thereon. Failure to submit a feasible and credible plan and/or failure to implement the same shall serve as grounds for the imposition of appropriate sanctions, fines or penalties pursuant to Section 39 of this Act.

SEC. 24. *Gas Distribution Rate.* - Except as provided for during the infrastructure development period, the distribution rates charged by gas distribution utilities shall be subject to regulation by the ERC based on the principle of full recovery of prudent and reasonable economic costs incurred, including a reasonable return on rate base that is consistent with the encouragement of private investment and goal of developing the Downstream Natural Gas Industry infrastructure, or such other principles that will promote the determination of just and reasonable rates by the ERC. Where a rate applicant successfully demonstrates that its rates will be applicable to contestable markets, the ERC shall have the authority to permit negotiated rates.

SEC. 25. *Functions of Gas Distribution Utilities.* - All gas distribution utilities shall have the following functions:

(a) Obligation to provide distribution services and connections to its gas distribution system for any end-user within the area covered by its permit

consistent with the Gas Distribution Code. Any gas distribution utility engaged therein shall provide nondiscriminatory access to its gas distribution system to suppliers and/or end-users entitled to retail access under Section 30 of Chapter VII of this Act. Any gas distribution utility shall be entitled to impose and collect from such suppliers and/or end-users distribution charges and connection fees as approved by the ERC after due notice and hearing;

(b) Ensure the safety, reliability, adequacy, security, stability and integrity of their gas distribution systems in accordance with the technical specifications and performance standards set forth in the Gas Distribution Code to be promulgated by the DOE pursuant to Section *5(g)* of this Act. Each gas distribution utility shall submit to the ERC a statement of its compliance with such technical specifications and performance standards. Any gas distribution utility that fails to comply with any of the prescribed technical specifications or performance standards shall include in such statement of, compliance an undertaking to comply with said technical specifications and performance standards within a reasonable time as may be necessary to ensure safety and reliability, or prevent environmental harm. The ERC shall, within sixty (60) days upon receipt of such plan, evaluate the same and notify the gas distribution utility concerned of its decision thereon. Failure to submit a feasible and credible plan and/or failure to implement the same shall serve as grounds for the imposition of appropriate sanctions, fines or penalties pursuant to Section 39 of this Act;

(c) Provide universal service within the area covered by its permit except as provided herein. Compliance with the universal service obligation shall be addressed as part of the annual development and maintenance plan of a gas distribution utility. A gas distribution utility shall be obliged to develop and maintain an efficient system for the distribution of natural gas at the reasonable request of end-users within its franchise area including:

(i) The installation of pipes where the connection to the end-user is within twenty-five (25) meters of the gas distribution system; or

(ii) Increasing the capacity of existing gas distribution systems: Provided, however, That no new service shall be required if such service would not be economically viable. A determination by a

gas distribution utility that it cannot viably serve a portion of its franchise area shall be subject to review by the ERC upon filing of a complaint by the requesting end-user.

The obligation of the gas distribution utility to provide universal access involves both an obligation to connect end-users within twenty-five (25) meters from the main pipeline and an obligation to supply such end-users, to the extent the distribution utility is the sole gas supplier. Upon implementation of third party access, the utility shall be relieved of its obligation to supply end-users eligible for retail access as defined in the guidelines to be promulgated by the DOE, but not its obligation to provide connection to its distribution system to such end-users. Whether or not the gas distribution utility is the sole gas supplier in the area, prices charged by the said utility for the supply of gas shall be negotiated for the contestable market and regulated by the ERC for the captive market; and

(d) Submit annually to the ERC its plan for maintaining and developing its gas distribution system in compliance with the obligations prescribed in this Act.

CHAPTER VI
SUPPLY SECTOR

SEC. 26. *Permit Requirement.* - Any law to the contrary notwithstanding, no person may engage in any supply activity unless it has obtained a permit from the DOE, initially: Provided, however, That a gas transmission utility or gas distribution utility that has secured a permit as such pursuant to Section 9(c) of this Act and that supplies natural gas to its own customers shall not be required to secure a separate permit to engage in its supply activity. For this purpose, the DOE shall promulgate rules and regulations prescribing the qualifications of suppliers which shall include, among other requirements, a demonstration of their technical capability, financial capability, creditworthiness and compliance with safety standards. The DOE shall have the authority to require suppliers to furnish a bond or other evidence of their ability to withstand market disturbances or other events that may increase the cost of providing service.

SEC. 27. *Supplier Rate and Service Regulation.* –

(a) The rates and service of suppliers to captive markets shall be regulated by the ERC; and

(b) The rates and service of suppliers to contestable markets shall not be subject to regulation by the ERC Provided, however, That suppliers shall be subject to the rules and regulations concerning abuse of market power, cartelization and other anti-competitive or discriminatory behavior promulgated by the ERC.

(c) The supply of natural gas for electric generation and large end-users is hereby deemed to be a contestable market. In all other cases, suppliers shall bear the burden of 'demonstrating that a market is contestable.

SEC. 28. *Conditions for Retail Access to Gas Distribution Systems.* - Following the infrastructure development period, retail access to gas distribution systems shall be available to large end-users meeting criteria set forth in the rules and regulations promulgated by the ERC pursuant to this Act. The ERC shall determine when retail access may Be available to other end-users or classes of end-users, giving consideration to relevant factors including whether such end-users or class of end-users constitute a contestable market-end the financial consequences of any assets potentially stranded by expanding retail access.

CHAPTER VII
TAXATION

SEC. 29. *Taxes.* - Gas transmission utilities, gas distribution utilities and suppliers of natural gas shall be subject to the payment of all taxes, duties, fees or charges and other impositions under the National Internal Revenue Code (NIRC) of 1997, as amended, and other applicable laws: Provided, however, That, in recognition of the substantial investments needed for the construction, operation and maintenance of gas transmission and gas distribution systems, gas transmission utilities and gas distribution utilities shall, upon prior endorsement by the DOE and approval by the Board of Investments, be entitled to income tax holiday and such other incentives granted to pioneer enterprises under the Omnibus Investment Code, as amended. The commodity price of gas shall be the only component of the gas retail rate which shall be subject to excise taxes under Republic Act No. 8424, otherwise known as the Comprehensive Tax Reform Law.

SEC. 30. *Withdrawal of Exemptions.* - Any law to the contrary notwithstanding, to achieve the declared policies of this Act, particularly in relation to the promotion of fair and nondiscriminatory treatment of public and private sector entities in the development of the Downstream Natural Gas Industry infrastructure, all existing tax exemptions applicable to persons engaged in the transmission or the distribution of natural gas; insofar as such exemptions relate to revenues derived from the transmission or the distribution of natural gas, shall be deemed revoked upon the effectivity of this Act.

CHAPTER VIII
RATEMAKING REQUIREMENTS AND PROCEDURES

SEC. 31. *Ratemaking Requirements and Procedures of the ERC.* - (a) Just and reasonable rates and charges. - All rates and charges for transmission, distribution or supply of natural gas to the captive market and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable. Any such rate or charge that is not just and reasonable is hereby declared to be unlawful;

(b) Undue preferences and unreasonable rates and charges are prohibited. - No gas transmission utility, gas distribution utility or supplier shall, with respect to the transmission, distribution or supply of natural gas to the captive market: (1) make or grant any undue preference or advantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, between locations or between classes of service;

(c) Filing of rate schedules. - Under such rules and regulations as the ERC may prescribe, after due notice and public consultation, the ERC may require reports or documents from gas transmission utilities, gas distribution utilities or suppliers to the captive market showing all rates and charges for the transmission, distribution or supply of natural gas to the captive market and the classifications, practice and regulations affecting such rates, charges, and classifications and services: Provided, That the ERC shall provide appropriate mechanisms to protect the confidential& of any information that is commercially or competitively sensitive; and

(d) Changes in rate and charges. - Within thirty (30) days upon filing for an adjustment in rates, the ERC shall issue an order accepting, rejecting or setting for hearing such adjustment. The ERC may, upon the filing of an application therefor or at any stage thereafter, with or without prior hearing, on the basis

of supporting papers duly verified or authenticated, and with such notice to the affected parties and opportunity for such parties to make such submissions as the ERC determines to be appropriate in the circumstances, grant provisional relief fixing interim rates for the transmission of natural gas or distribution of natural gas or supply of natural gas to the captive market applicable during the pendency of the hearing on the application, on motion of a party in the case or on its own initiative, without prejudice to a final decision after hearing, should the ERC find that the pleadings, together with such affidavits, documents and other evidences which may be submitted in support of the motion, substantially support the provisional order. The final order fixing the applicable rates shall provide for over- or under-recovery of costs occasioned by the application of ERC-approved interim rates. At any hearing involving rates adjustment, the burden of proof to show that the increased rates are just and reasonable shall be upon the gas transmission utility, gas distribution utility or supplier to the captive market.

CHAPTER IX
PROMOTION OF COMEPTITION

SEC. 32. *Anti-Competitive Behavior.* - No gas transmission utility, gas distribution utility or supplier, or affiliate thereof, may engage in any anti-competitive behavior or abuse of market power including, but not limited to:

(a) Agreements, decisions and concerted practices of persons or associations of persons to fix prices and/or fix output; and

(b) Other practices and/or conduct by a person or groups of persons that restrict, prevent or distort competition such as, but not limited to, predatory pricing and practices, excessive pricing, bundling and other vertical restraints, denial of access to essential facilities on fair terms, discriminatory conditions on transactions that restrict, prevent or distort competition.

SEC. 33. *Measures to Promote Competition.* - Subject to the provisions of relevant laws, the ERC shall adopt measures and/or corresponding remedies *to* promote competition following an investigation of the relevant circumstances and a definitive finding of:

(a) Price and/or output fixing; or

(b) Other practices/conduct that are the subject of investigation restrict and/or prevent and/or distort competition.

Such remedies shall, without limitation, include the imposition of price controls, issuance of injunctions or disgorgement of excess profits and imposition of administrative fines and penalties pursuant to this Act.

SEC. 34. *Functional and Structural Unbundling.* - When prevailing market conditions so require, any Downstream Natural Gas Industry participant shall functionally and structurally unbundle its business activities and rates in accordance with the sectors as identified in Section 7 hereof. The ERC shall ensure full compliance with this provision.

SEC. 35. *Complaint Procedures.* - The ERC shall, within one year from the effectivity of this Act, promulgate rules and regulations providing for a complaint procedure that, without limitation provides the party alleged to have engaged in anti-competitive or abusive activities with notice and an opportunity to be heard.

SEC. 36. *Affiliated Suppliers.* - In order to prevent anti-competitive conduct, service contractors, gas transmission utilities and gas distribution utilities that own or control affiliates that are suppliers shall conduct their business as follows:

(a) No preference will be given to the affiliated supplier over other persons through contracting for available capacity, scheduling, balancing, curtailment priority or tariffs;

(b) Marketing information provided to the affiliated supplier will be provided to any nonaffiliated supplier that is a competitor or potential competitor;

(c) Employees of the affiliated supplier shall, to the maximum extent possible, function independently in making business decisions; and

(d) Books of accounts and records of the affiliated supplier shall be maintained separately.

As used herein, "affiliate" refers to any person or entity which, alone or together with any other person or entity, directly or indirectly, through one or more intermediaries, controls, or is controlled by another person or entity. As

used herein,"control" shall mean the power to direct or cause the direction of the management policies of a person by contract, agency or otherwise.

SEC. 37. *Administrative Fines and Penalties.* –

(a) The administrative fines and penalties that may be imposed by the ERC or the DOE, as the case may be, for any violation of or noncompliance with this Act or its implementing rules and regulations shall range from a minimum of Fifty thousand pesos (P50,000.00) to a maximum of Fifty million pesos (P50,000,000.00);

(b) Any person who is found to have engaged in any of the prohibited acts pursuant to Section 34 ***of*** this Act shall suffer the administrative penalty or fine ranging from Ten thousand pesos (P10,000.00) to Ten million pesos (P10,000,000.00), at the discretion of the ERC or the DOE, as the case may be;

(c) The members of the board of directors or any person that violates the provisions of this Act may be fined by an amount not exceeding double the amount of damages caused by the offender at the discretion of the ERC or the DOE, as the case may be. This rule shall apply to the members of the Board who, knowingly or by neglect, allow the commission or omission under the law;

(d) Any party to an administrative proceeding may, at any time, make an offer to the ERC or the DOE, as the case may be, conditionally or otherwise, for a consent decree, voluntary compliance or desistance and other settlement of the case. The offer and any or all of the ultimate facts upon which the offer is based shall be considered for settlement purposes only and shall not constitute an admission by the party making the offer of any violation of the laws, rules, regulations, orders and resolutions of the ERC or the DOE, as the case may be, nor as a waiver to file any warranted criminal actions; and

(e) Congress may, upon recommendation of the ERC or the DOE, as the case may be, revoke such franchise or privilege granted to the party found in violation of the provisions of this Act.

CHAPTER X
ANTI-PILFERAGE AND ANTI-THEFT PROVISIONS

SEC. 38. Pilferage. - It is hereby declared unlawful for any person to:

(a) Tap, make or cause to be made any connection with any gas transmission system or gas distribution system without previous authority or consent of the gas transmission utility or gas distribution utility concerned;

(b) Tamper, install or use tampered meters or any other device which interferes with proper or accurate registry or metering of natural gas flows or otherwise results in its diversion in a manner whereby natural gas is stolen or wasted;

(c) Damage or destroy any natural gas meter, equipment, pipeline or conduit or any part of a gas transmission system or gas distribution system or allow any of them to be so damaged or destroyed as to interfere with the proper or accurate metering of natural gas flows; and

(d) Knowingly use or receive the direct benefit of natural gas delivery service obtained through any of the acts mentioned in paragraphs (a), (b) and (c) above.

SEC. 39. *Theft of Equipment and Materials.* - It is hereby declared unlawful for any person to:

(a) Cut, saw, slice, separate, split, severe, smelt or remove any portion of a gas transmission system or gas distribution system, including pipeline materials and meters, from any installation or place of installation or any other place or site where it may be rightfully or lawfully stored, deposited, kept, stocked, inventoried, situated or located, without the consent of the gas transmission utility or gas distribution utility concerned, whether or not the act is done for profit or gain;

(b) Take, carry away or remove or transfer, with or without the use of a motor vehicle or other means of conveyance, load, carry, ship or move from one place to another, whether by land, air or sea, any portion of a gas transmission system or gas distribution system, including pipeline materials or meters, from any installation or place of installation, or any place or site where it may be rightfully or lawfully stored, deposited, kept, stocked, inventoried, situated or located without the consent of the gas transmission utility or gas distribution utility concerned, whether or not the act is done for profit or gain; and

(c) Store, possess or otherwise keep in his premises, custody or control, without lawful purpose, any portion of a gas transmission system or gas distribution system, including pipeline materials or meters, without the consent of the gas transmission utility or gas distribution utility concerned, whether or not the act is done for profit or gain.

SEC. 40. *Penalties.* –

(a) Violation of Section 40. - The penalty of prision mayor or a fine ranging from Ten thousand pesos (Pl0,000.00) to Twenty thousand pesos (P20,000.00) or both, at the discretion of the court, shall be imposed on any person found guilty of violating Section 40 of this Act.

(b) Violation of Section 41. - The penalty of reclusion temporal or a fine ranging from Fifty thousand pesos (P50,000.00) to One hundred thousand pesos (Pl00,000.00) or both, at the discretion of the court, shall be imposed on any person found guilty of violating Section 41 of this Act.

(c) Provision common to violations of Sections 40 and 41 hereof. – If the violation of Section 40 or Section 41 of this Act is committed by, or in connivance with, an officer or employee of the gas transmission utility or gas distribution utility concerned, such officer or employee shall, upon conviction, be punished with a penalty one degree higher than the penalty provided herein, and forthwith be dismissed and perpetually disqualified from employment in any public or private utility or service company and from holding any public office.

If the violation of Section 40 or Section 41 of this Act is committed by a partnership, firm, corporation, association or any other legal entity, including a government-owned or -controlled corporation, the penalty shall be imposed on the president, manager and each of the officers thereof who shall have knowingly permitted, failed to prevent or was otherwise responsible for the commission of the offense.

CHAPTER XI
FINAL PROVISIONS

SEC. 41. *Implementing Rules and Regulations.* - The DOE shall, in consultation with the ERC, appropriate government agencies, the Downstream Natural Gas Industry participants, nongovernmental organizations and end-users, promulgate

implementing rules and regulations (IRR) within six months from the effectivity of this Act.

SEC. 42. *Natural Gas Oversight Commission.* - Upon the effectivity of this Act, a congressional commission, hereinafter referred to as the "Natural Gas Oversight Commission", is hereby constituted. The Natural Gas Oversight Commission shall be composed of ten (10) members, with the chairmen of the Committee on Energy of the Senate and the House of Representatives and four additional members from each House, to be designated by the Senate President and the Speaker of the House of Representatives, respectively. The minority shall be entitled to pro rata representation but shall have at least one representative in the Natural Gas Oversight Commission.

(a) The Natural Gas Oversight Commission shall, in aid of legislation, perform the following functions, among others:

(b) Set the guidelines and overall framework to monitor the proper implementation of this Act;

(c) Look into the appropriateness of creating a single independent regulatory body when the conditions prevailing so require;

(d) Conduct a periodic review of this Act at least once every three years;

(e) Determine inherent weaknesses in the law and recommend necessary remedial legislation or executive measures;

(f) Approve the budget for the programs of the Natural Gas

(g) Oversight Commission and all disbursements therefrom, including compensation of all personnel;

(h) Submit periodic reports to the President of the Philippines and Congress; and

(i) Perform such other powers and functions as may be necessary to attain its objectives.

To carry out its powers and functions, the initial sum of Fifteen million pesos (P15,000,000.00) shall be charged against the current appropriations of the Senate.

Thereafter, such amount necessary for its continued operation shall be included in the annual General Appropriations Act.

The Natural Gas Oversight Commission shall adopt its internal rules of procedure; conduct hearings and receive testimonies, reports and technical advice; invite or summon by subpoena *ad testificandum* any public official, private individual or any other person to testify before it, or require any person by subpoena *duces tecum* to produce before it such records, reports, documents or other materials as it may require; and generally require all the powers necessary to attain the purposes for which it is created. The Natural Gas Oversight Commission shall be assisted by a secretariat to be composed of personnel who may be seconded from the Senate and the House of Representatives and may retain consultants. The secretariat shall be headed by an executive director who has sufficient background and competence on the policies and issues relating to the Downstream Natural Gas Industry reforms as provided in this Act.

SEC. 43. *Separability Clause.* - If, for any reason, any provision of this Act 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.

SEC. 44. *Nonretroactivity, Applicability and Repealing Clause.* - The provisions of Republic Act No. 387, otherwise known as the "Petroleum Act of 1949", as amended, Presidential Decree No. 87, Republic Act No. 8997, and all other laws, decrees, executive orders, rules and regulations, circulars and other issuances inconsistent with the provisions of this Act are hereby repealed or modified accordingly.

SEC. 45. *Transitory Provision.* - Gas transmission systems and gas distribution systems that have been constructed and have commenced operation prior to the date of effectivity of this Act shall continue to operate under their existing authorities: Provided, That they have complied with existing laws, rules and regulations prior to the effectivity of this Act and have secured a provisional permit from the DOE as provided in Sections 15 and 21 of this Act. Suppliers who have entered into gas sales and purchase contracts with customers and have delivered indigenous or imported natural gas under said contracts prior to the date of effectivity of this Act shall continue to sell natural gas under their existing authorities provided they have complied with existing laws, rules and regulations prior to the effectivity of this Act.

Nothing in this Act shall be deemed to revoke or otherwise modify the powers and functions of the Philippine National Oil Company and its subsidiaries under Presidential Decree No. 334, as amended, any existing concession granted under the Petroleum Act of 1949, as amended, certificate of public convenience or certificate of public convenience and necessity granted pursuant to the Public Service Law, as amended, specific franchise for the transmission, distribution or supply of natural gas or other administrative or regulatory permit or contract, which concession, certificate, franchise, permit or contract shall be allowed to its full term but may not be renewed except pursuant to the provisions of this Act.

For a period not exceeding five years after the effectivity of this Act, the DOE may issue provisional permits, with a maximum term of two years, renewable twice for a maximum cumulative term not exceeding six years, for the construction, operation and maintenance of pipelines and related facilities for the transmission, distribution and supply of natural gas.

SEC. 46. *Effectivity Clause.* - This Act shall take effect on the fifteenth (15th) day following its publication in the Official Gazette and in at least two national newspapers of general circulation.

Approved,