Republic of the Philippines
COMMISSION ON AUDIT
Commonwealth Avenue, Quezon City, Philippines
Corporate Government Sector
Cluster 3 – Public Utilities

6 June 2017

POWER SECTOR ASSETS AND LIABILITIES MANAGEMENT CORPORATION
OFFICE OF THE PRESIDENT AND CEO
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MS. LOURDES S. ALZONA
Officer-in-Charge
Power Sector Assets and Liabilities
Management Corporation
Diliman, Quezon City

Madam:

Pursuant to Section 2, Article IX-D of the Philippine Constitution and Section 43 of Presidential Decree No. 1445, otherwise known as the Government Auditing Code of the Philippines, we transmit herewith our report on the results of the audit of the accounts and operations of the **Power Sector Assets and Liabilities Management Corporation** for the year ended December 31, 2016.

The report consists of the Independent Auditor's Report, the Audited Financial Statements, the Observations and Recommendations, and the Status of Implementation of Prior Years' Audit Recommendations.

The Auditor expressed a qualified opinion on the fairness of the presentation of the financial statements of the Corporation due to the following:

The Property, Plant and Equipment (PPE) with a carrying net book value of P25.894 billion and P29.543 billion as of December 31, 2016 and December 31, 2015 respectively, was overstated due to non provision of allowance for depreciation for Assets from Privatized Independent Power Producers (IPPs) with carrying value of P1.416 billion, Electric Plants Leased to Others with carrying amount of P178.446 million, and Other Utility Plants in the amount of P17.979 million and inclusion of transmission related assets amounting to P336.006 million owned by the National Transmission Corporation (TransCo);

The Receivables – Disallowances account was understated due to non-recording of disallowances totaling P13.543 million and P60.960 million as of December 31, 2016 and 2015 respectively, which have become final and executory and which have been covered with Notice of Finality of Decisions and COA Order of Executions.

In addition, the Due from National Government Agencies (NGAs) account in the aggregate amount of P53.709 billion was not reliable due to inclusion of the prepayment accounts totaling P37.668 billion, tax under protest of P10.867 billion and the tax on the disallowed payment of P11.026 million and for which no suit or proceeding has been filed with the BIR.

The accuracy and reliability of the accounts BIR - Input VAT(181), BIR - CWT (136) totaling P36.181 billion and P1.488 billion, respectively were not ascertained due to a significant variance of P13.356 billion between the total amount of Input VAT presented in the VAT Returns or BIR Forms 2550Q of P22.825 billion and the general ledger account balance for

Input VAT account totaling P36.181 billion, inclusion of long outstanding and unsubstantiated balances transferred from NPC with an aggregate amount of P11.103 billion, and deficiency basic VAT of P2.628 billion was recorded as debits to Input VAT account (GL 181), instead of Taxes, Duties and Licenses account.

In addition to the above observations considered in the formulation of the auditor's opinion, we invite your attention to the following other significant observations and recommendations that need immediate action as well:

1. PSALM had not effected adjustments of the prepayment and amortization schedule of the Concession Fees totaling P57.883 billion by deducting NGCP's obligations at the time of prepayment on July 15, 2013 with National Transmission Corporation (TransCo), on the basis of the letter of the President, TransCo to the Officer In Charge, PSALM, dated February 28, 2017 totaling P3.922 billion.

   NGCP's prepayment of concession fees covering the 10th to 30th deferred payments was contrary to Section 6.07 of the Concession Agreement between PSALM and the NGCP as the latter can exercise this option only when it has no outstanding obligations with TransCo as of July 15, 2013.

   Recommendation:

   In case of NGCPs' failure to settle the said obligation within the period stipulated in the formal notice, Management make the necessary adjustment in the recording of the prepayments made by NGCP by deducting first its obligations with TransCo before crediting the balance to deferred concession fees.

2. Independent Power Producers Administration Agreement (IPPAA) expenses totaling ₱27.446 billion was offset against IPPAA income of P35.689 billion and presented in the Statement of Financial Performance under Income line item IPPA net with balance of P8.243 billion, which is not in accordance with paragraphs 48, 49 and 105 of PPSAS 1.

   Recommendations:

   a. Analyze the Income and Expense accounts under the IPPAA transaction and include them with the other income and expense accounts of PSALM that are of similar nature; and

   b. Comply with the provisions of Paragraphs 48, 49 and 105 of PPSAS 1 in the presentation of IPPAA income and expenses in the Statement of Financial Performance

3. Operation and Maintenance Agreement (OMA) expenses totaling P19.163 billion was offset against net utility revenue and presented in the Statement of Financial Performance under Income line item Power Generation (net) with balance of negative P1.552 billion, contrary to paragraphs 48, 49 and 105 of PPSAS 1.

   The yearend balance of the accounts Personnel Services and Capital Outlay pertaining to the OMA related expenses with NPC in the amount of P31.472 million and P911.980 million respectively, were not fairly presented in the Financial Statements due to:

a. The accrual basis of accounting for Personnel Services provided in Note 3.1 of the Notes to the Financial Statement and PPSAS 1 were not complied with; instead, expenses totaling P31.472 million were recorded upon receipt of liquidation reports from NPC regardless of the period it was actually incurred; and

b. Capital expenditures totaling P911.980 million were all recorded under Other Assets instead of the Property Plant and Equipment contrary to PPSAS 17.

Recommendations:

a. Comply with the provisions of Paragraphs 48, 49 and 105 of PPSAS 1 in the presentation of income and expenses in the Statement of Financial Performance;

b. Follow the accrual method of accounting for OMA expenses in compliance with Note 3.1 of the Notes to the Financial Statements and PPSAS 1;

c. Reclassify to the appropriate *Property, Plant and Equipment* account the capital expenditures with an aggregate amount of P911,979,754 and prior years' capital expenditures recorded under *Other Assets* and

d. Consider revisiting the OMA specifically on how PSALM can effectively monitor the liquidation of the funds transferred to NPC.

4. PSALM's mandate to manage the sale, disposition and privatization of NPC-transferred real estate assets may not be properly carried out due to:

a. Incomplete records of all the 6,160 lots transferred from NPC, and only 720 lots are documented with Transfer Certificates of Title (TCTs) turned over to PSALM;

b. Physical inventory of lots, land survey and profiling were not conducted since the creation of PSALM to ascertain validity, existence and accuracy; and

c. The land area shown in figures in the TCTs differs with the land area in words, showing a total discrepancy of 73,222 sq.m in the land area of inventoried Transfer Certificates of Title.

Recommendations:

a. Identify and confirm with NPC the final list of PSALM real estate properties;

b. Conduct a regular ocular inspection and inventory of these real estate properties and submit a copy of the report to COA;

c. Undertake immediately land survey and profiling to facilitate the titling of the land;

d. Request from NPC copy of all the remaining land TCTs for complete documentation; and

e. Coordinate with the local Registry of Deeds on the difference in figures and in words in the land areas in the TCTs.

The other audit observations, together with the recommended courses of action which were discussed by the Audit Team with concerned Management officials and staff during the exit conference conducted on May 29, 2017 are discussed in detail in Parts II and III of the report.

We respectfully request that the recommendations contained in Parts II and III of the report, be fully implemented and that this Commission be informed of the actions taken thereon by accomplishing the Agency Action Plan and Status of Implementation form (copy attached) within 60 days from the date of receipt hereof.

We acknowledge the support and cooperation that the Management extended to the Audit Team, thus facilitating the completion of the report.

COMMISION ON AUDIT

By:

Pearl L. Ramos

PEARL L. RAMOS
Director III
Officer-in-Charge

Copy furnished:

The President of the Republic of the Philippines
The Vice President
The Speaker of the House of Representatives
The Chairperson – Senate Finance Committee
The Chairperson – Appropriations Committee
The Secretary of the Department of Budge and Management
The Governance Commission for Government-Owned or Controlled Corporations
The Presidential Management Staff, Office of the President
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Republic of the Philippines
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Commonwealth Avenue, Quezon City, Philippines

INDEPENDENT AUDITOR'S REPORT

THE BOARD OF DIRECTORS
Power Sector Assets and Liabilities
Management Corporation
Diliman, Quezon City

Report on the Financial Statements

We have audited the accompanying financial statements of Power Sector Assets and Liabilities Management Corporation, which comprise the Statement of Financial Position as at December 31, 2016 and 2015, and the Statement of Financial Performance, Statement of Changes in Net Assets/Equity, Statement of Cash Flows and Statement of Comparison of Budget and Actual Amount for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Philippine Public Sector Accounting Standards, , and for such internal control as Management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Philippine Public Sector Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Basis for Qualified Opinion

The Property, Plant and Equipment (PPE) with a carrying net book value of P25.894 billion and P29.543 billion as of December 31, 2016 and December 31, 2015 respectively, was overstated due to non provision of allowance for depreciation for Assets from Privatized Independent Power Producers (IPPs) with carrying value of P1.416 billion, Electric Plants Leased to Others with carrying amount of P178.446 million, and Other Utility Plants in the amount of P17.979 million and inclusion of transmission related assets amounting to P336.006 million owned by the National Transmission Corporation (TransCo);

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Qualified Opinion

In our opinion, except for the effects and the possible effects of the matters discussed in the Basis for Qualified Opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the **Power Sector Assets and Liabilities Management Corporation** as at December 31, 2016 and 2015, and its financial performance and its cash flows for the year then ended in accordance with Philippine Public Sector Accounting Standards.

Emphasis of Matter

We draw attention to Note 37 to the Financial Statements which describes the uncertainties relating to the outcome of the various legal and administrative proceedings including litigation and proceedings related to electricity charges and challenges to certain provisions of the EPIRA and the judgment on the back wages claims of the NPC Drivers and Mechanic Association (DAMA) for which NPC and PSALM were the Respondents. Our opinion is not qualified in respect of this matter.

Other Matter

PSALM failed to adjust from NGCP's concession fees of P57.883 billion the amount of P3.922 billion as settlement of its obligations with National Transmission Corporation (TransCo). NGCP's concession fees prepayment is contrary to Section 6.07 of the Concession Agreement between PSALM and the NGCP.

Report on the Supplementary Information Required Under BIR Revenue Regulation 15-2010

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information on taxes, duties and license fees in Note 34 to the financial statements is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such information is the responsibility of Management. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

COMMISSION ON AUDIT

Eyren M. Yulde

EYREN MARANAN-YULDE
OIC - Supervising Auditor
May 29, 2017