EXECUTIVE SUMMARY

A. **Introduction**

National Electrification Administration (NEA)

1. NEA was originally created as a national government agency by virtue of RA Nos. 2717 and 6038 dated June 19, 1960 and August 4, 1969, respectively. On August 6, 1973, PD 269 was issued converting NEA into a government-owned and controlled corporation and declaring a national policy objective for the total electrification of the Philippines on an area coverage basis and the organization, promotion and development of viable rural electric cooperatives (ECs) to attain the said objective. Moreover, NEA is geared towards the uplifting of the standard of living in the rural areas by the service of electricity.

2. On June 8, 2001, RA 9136, better known as the Electric Power Industry Reform Act (EPIRA) of 2001, was enacted. Section 58 of the said law gave NEA an additional mandate as follows:

    a. To prepare the electric cooperatives in operating and competing under the deregulated electricity market within five (5) years from the effectivity of the act;

    b. To strengthen the technical capability and financial viability of rural electric cooperatives; and

    c. To review and upgrade regulatory policies with a view to enhancing the viability of the electric cooperatives as electric utilities.

3. The EPIRA increased NEA's authorized capital from P5 billion authorized in 1979 under PD 1645 to P15 billion. However, as of December 31, 2013, the National Government made no additional subscription.

4. Administrative Order (AO) No. 112 dated December 7, 2004 directed the NEA to take full and sole authority and responsibility in the conversion of electric cooperatives into stock cooperatives. Pursuant to the AO, the NEA Board of Administrators promulgated the Guidelines in the Conduct of ECs Referendum (GCECR) to convert into either stock cooperative under the Cooperative Development Authority or stock corporation under the Securities and Exchange Commission.

5. On September 2, 2005, Memorandum Order (MO) No. 187 was issued by the Office of the President setting the guidelines on the conversion of ECs. In compliance with the MO, the NEA Board of Administrators, in its Resolution No. 116 dated October 5, 2005, approved the amendment to the NEA GCECR.

6. On May 7, 2013, then President Benigno S. C. Aquino III signed into law the National Electrification Administration Reform Act of 2013 (RA 10531) which amended the NEA charter (Presidential Decree No. 269). The law aims to:

a. promote sustainable development in rural areas through rural electrification;

b. empower and strengthen NEA to pursue the electrification program, providing electricity through the ECs to the countryside and other economically unviable areas; and

c. empower and enable electric cooperatives to cope with the changes brought about by restructuring of the electric power industry pursuant to RA 9136, otherwise known as the “Electric Power Industry Reform Act of 2001”.

7. Further, this law had increased NEA’s authorized capital stock to P25 billion divided into 250 million shares with a par value of one hundred pesos (P100).

Scope and Objectives of Audit

8. The audit covered the transactions, accounts and operations of NEA for CY 2018. The audit was conducted to determine the (a) level of assurance that may be placed on the management’s assertions on the financial statements; (b) the propriety of transactions as well as the compliance with existing rules and regulation as well as management’s policies; and (c) the extent of the implementation of prior years’ audit recommendations.

B. Financial Highlights (In Thousand Pesos)

Shown below are the financial position and financial performance including budget utilization of NEA for CY 2018.

Financial Position

Particulars	2018	2017	Increase (Decrease)
Assets	20,489,016	23,813,664	(3,324,648)
Liabilities	19,037,329	28,549,014	(9,511,685)
Equity	1,451,687	(4,735,350)	6,187,037

Financial Performance

Particulars	2018	2017	Increase (Decrease)
Gross income	700,584	675,412	25,172
Other income	17,206	32,666	(15,460)
Total income	717,790	708,078	9,712
Operating expenses	381,613	415,996	(34,383)
Other expenses	107,364	68,543	38,821
Total expenses	488,977	484,539	4,438
Net profit before income tax	228,813	223,539	5,274
Income tax expense	70,067	70,891	(824)
Net profit	**158,746**	**152,648**	**6,098**

Budget Utilization

	Budget	**Expenditures**
Personal services	440,159	241,862
Maintenance and other operating expenses	209,348	267,978
Capital outlay	34,057	631
Total	**683,564**	**510,471**

C. Operational Highlights

For CY 2018, NEA reported the following major accomplishments:

a. Total Electrification Program

- The NEA has been the forerunner of the country's electrification program since its creation as an institution in 1969 by virtue of RA 6038. For nearly five decades, the NEA stayed true to its mandate of lighting up provincial towns and the remotest of villages in our country.

  As of November 2018, the data on the electrification status of the franchise areas of the Electric Cooperatives show that 78 provinces, 90 cities, 1,385 municipalities, 36,057 barangays, 123,198 sitios and 12.712 million connections have been provided with electricity, benefitting about 60 million Filipinos.

  With the ECs as its implementing arm in the mandated mission of rural electrification, even in missionary of economically unviable areas, the NEA continues to implement Sitio Electrification Program. As of December 31, 2018, out of NEA's target for 2018 sitio electrification of 1,817 sitios. 1,931 sitios were completed/energized. This contributed to the connection of 526,201 additional consumers (from January to November) which is in line with the President's directive to provide electricity access for all.

b. Provision of Loan Facilities to ECs

- NEA has achieved its full-year loan availment target of P1.7 billion by the electric cooperatives (ECs) three months ahead of schedule. Latest data shows P1.985 billion worth of loans, including calamity loans, has been extended to 62 ECs as of December 2018. The agency released a total of P1.820 billion to 56 ECs to finance capital expenditure projects and P99 million to six other ECs for the repair and rehabilitation of damaged distribution facilities due to previous typhoons Lawin, Urduja and Vinta, and other calamities.

  As of September 2018, NEA posted a total collection for the year's operation the amount of P2.237 billion against amortizations due of P2.202 billion or collection efficiency of 100 percent.

c. Capacity Building Program for EC Personnel

- In line with the policy of the state as enunciated in Section 2 C of RA 10531 to empower and enable the ECS to cope with the changes brought about by the restructuring of the power industry, the NEA conducted various competency seminars and training programs for the personnel of the ECs attended by 3,301 participants. Essentially, the seminars and training programs were designed to enhance the core values and Financial, Institutional and Technical (FIT) skills of the personnel of the ECs to bring about marked improvement in the ECs' operational efficiency and financial viability.

d. Corporate Governance

- ISO 9001:2015 Certification

  Anchored on its Good Governance Agenda, the Agency was able to hurdle the ISO 9001:2015 Surveillance Audit conducted by TUV Rheinland Philippines, Inc. on December 5, 2018 covering the scope "Provision of Financial, Institutional, Technical and Legal Assistance to the Electric Cooperatives (ECs) which in turn undertake power distribution on an area coverage basis".

- Customer Satisfaction Survey

  NEA continuously espouses good corporate governance in order to provide better service to the ECs. This was clearly manifested in the result/report submitted by Contact Asia Services Inc. (CASI) Research, the third-party service provider for the conduct of EC Customer Satisfaction Survey (CSS). The overall satisfaction rating garnered by NEA is at 4.50 or 90 percent; both scores translate to the verbal interpretation of "Very Satisfied".

  The CSS covered six items namely: Staff and Organization, Regulatory: Policies, Regulatory: Application, Financing, Information and Communication, and Facilities. Overall, NEA's offices/departments were rated by the respondents with the average levels of satisfaction ranging from "Satisfied" to "Very Satisfied".

e. Passage of Electric Cooperatives Emergency and Resiliency Fund Act (ECERF)

- Passed into law on June 29, 2018, RA 11039 provides an orderly and continuing means of financial assistance to electric cooperatives in the form of grants for disaster mitigation, preparedness and rehabilitation of damaged infrastructure after a fortuitous event or force majeure.

  Under the law, the NEA will manage and administer the ECERF, which will have an initial amount of P750 million to be taken from the National Disaster Risk Reduction and Management (NDRRM) Fund and will be released to the NEA Quick Response Fund for proper release to qualified ECs. In case of fund deficiency, the NEA may seek the allocation of a supplementary budget, subject to the approval of the President.

The NEA may also accept donations in the form of funds, materials and equipment intended for the restoration and rehabilitation of the ECs' damaged infrastructure, subject to existing auditing rules and regulations and shall be exempt from taxes and duties. In turn, the ECs shall implement the rural electrification program nationwide as well as ensure the preparedness and mitigation measures to protect the infrastructure from the adverse impact of any fortuitous event or force majeure.

The Proposed Implementing Rules and Regulations (IRR) of ECERF was approved by the NEA Board of Administrators on December 7, 2018 under Board Resolution No. 208

f. Mobilization of Task Forces

➢ Task Force Ompong

In September 2018, Typhoon Ompong (Mangkhut) made landfall in Baggao, Cagayan. Ompong has maximum winds of 205 km/h and gustiness of up to 285 km/h. Though it was not a super typhoon under PAGASA's classification system, it was a powerful tropical cyclone with a huge diameter of 900 kilometers.

A task force composed of 22 electric cooperatives from Regions I, II, III, IV-A and CAR headed north to help restore power in areas left in the dark. Dubbed as "Power Restoration Rapid Deployment Task Force Ompong," the team augmented the manpower of the typhoon-affected ECs and provided the necessary assistance to restore the electricity service as safely and as quickly as possible.

➢ Task Force Rosita

Typhoon Rosita (Yutu) made landfall in Dinapigue, Isabela on October 30, 2018. The storm came more than a month after Typhoon Ompong left a path of destruction in19 provinces in Luzon, including Isabela and Quirino. This prompted NEA and ECs to mobilize the Task Force Kapatid (TFK) to help restore power in the provinces of Isabela and Quirino.

TFK is a time and tested spirit of Bayanihan among ECs' Compact of Cooperation. TFK pools together volunteers from different ECs to render volunteer service to other ECs which need technical help like energization of hard-to-reach places, to the rehabilitation of dilapidated or damaged electric distribution lines.

D. **Auditor's Opinion**

The Auditor rendered an unqualified opinion on the fairness of the presentation of the financial statements of the NEA as at December 31, 2018 as stated in the Independent Auditor's Report in Part I.

E. **Summary of Significant Audit Observations and Recommendations**

Although the Auditor rendered an unqualified opinion, there are significant audit observations that need immediate action. These, together with the audit recommendations are presented below. Details are discussed in Part II of this Report.

1. The accuracy and reliability of the year-end balance of Loans Receivable - ECs amounting to P10.934 billion (current and long-term) is doubtful as the results of confirmation from Electric Cooperatives (ECs) disclosed net understatement variance amounting to P45.388 million, attributed mainly to inclusion of interest/surcharge, advance payment for interest, and paid amortization in the EC confirmation, excess payments not deducted in EC's confirmation, and loans and capitalized interest not recorded in NEA books. Likewise, advance payment included/excluded in EC's confirmation, unpaid amortization per NEA's books, and loans not included in EC's confirmation renders the balance of loans receivable per NEA books overstated, affecting the fair presentation of accounts affected which is not in conformity with paragraph 27 of PPSAS 1.

   Recommendations:

   a. *Analyze and identify all possible causes of variances between book balance and ECs confirmed balances;*

   b. *Reconcile variances and upon acceptance by both parties, immediately make the necessary adjustments in the books and the ECs records to present the actual outstanding loan balance as of reporting date; and*

   c. *Conduct regular reconciliation of loans receivable with the ECs to thresh out differences in the accounts.*

2. The accuracy and reliability of the year-end balance of Loans Receivable – Others (PSALM) amounting to P2.155 billion is doubtful as the results of confirmation from PSALM disclosed material variance amounting to P369.652 million, overstating the Loans Receivable - Others – PSALM, contrary to one of the qualitative characteristic of financial reporting which is reliability of information under Appendix B of PPSAS 1.

   Recommendations:

   a. *Reconcile with PSALM the P369.652 million discrepancy and identify the causes for consideration of settlement;*

   b. *Analyze the P2.22 billion collection covering June 27, 2001 to March 3, 2003 to establish legitimacy; and*

   c. *Adjust as necessary and enforce settlement of any unpaid balance.*

3. The advance payment of loans consisting of principal and interests by Electric Cooperatives (ECs) amounting to P99.579 million and P58.148 million, respectively, or a total of P157.727 million for CY 2018 were recognized as credits to Loans Receivables and Interest Receivables, respectively, instead of credits to

Deferred Credits and Other Unearned Income, respectively, contrary to COA Circular No. 2015-010, thereby understating the year-end balance of both Loans Receivables and Interest Receivables.

Recommendations:

a. *Make the necessary adjustments in the books to reflect the correct balance of the affected accounts; and*

b. *Record future advance payments of principal to Other Deferred Credits and future advance payments on interest to Other Unearned Revenue for proper presentation in the financial statements pursuant to COA Circular No. 2015-010.*

4. The accuracy and reliability of the year-end balance of Property, Plant and Equipment (PPE) amounting to P201.019 million is doubtful due to:

   - Inclusion of unidentified items described as "For Adjustment" in the PPE Schedule and Subsidiary Ledger maintained by Accounting Division costing P36.454 million contrary to paragraphs 13, 26 and 27 of PPSAS No. 17;

   - Over provision of depreciation of some items with an aggregate cost of P5.510 million by P185,727.43;

   - Overstatement of Accumulated Depreciation by P6.109 million and understatement of Retained Earnings by same amount due to over depreciation by P4.963 million of some unidentified PPE costing P11.295 million and provision of depreciation by P1.145 million of PPE with no cost; and

   - Variance between Subsidiary Ledger (SL) and Lapsing Schedule balance for IT Equipment and Software amounting to P36,279.41 was noted.

   Recommendations:

   a. *Require the Accountant and Property Officer to coordinate and reconcile Accounting and Property records, respectively, to be able to identify the PPE items with no specific descriptions. If such PPE items do not really exist with proper documentation, make the necessary adjustments in the books for proper presentation in the financial statements;*

   b. *Require the Accountant to review and ensure that provision of depreciation of PPE should not exceed the residual value to avoid over depreciation. Effect the accounting adjustments in the books to reflect the correct balance of the account; and*

   c. *Analyze and reconcile the variance noted on the balance of IT Equipment and Software and make the necessary adjustments in the books.*

5. Employees who retired/resigned were given terminal leave benefits in CY 2018 totaling P2.936 million without complying with the prescribed documentary requirements under Section 5.13 of COA Circular No. 2012-001 and GSIS Memorandum Circular No. 003, s. 2015, hence the amount paid cannot be ascertained.

   Moreover, NEA paid monetization of leave credits to employees without observing the required accumulated fifteen (15) days vacation leave (VL) credits, minimum ten (10) days and at least five (5) days retained after monetization which is not in accordance with Section 22 of Omnibus Rules on Leave.

   Recommendations:

   a. *Require the Human Resource and Management Office (HRMO) to submit the lacking documents pursuant to Section 4.6 of PD No. 1445;*

   b. *Require the HRMO and Accountant to closely monitor leave credit balances of the employees to ensure that only employees with accumulated fifteen (15) days VL should be allowed to monetize the minimum ten (10) days and at least five (5) days is retained after monetization; and*

   c. *Henceforth, strictly comply with the documentary requirements under COA Circular No. 2012-001 and GSIS Memorandum Circular No. 003, s. 2015 on the payment of terminal leave benefits and observe the rules on monetization of leave provided under Section 22 of Omnibus Rules on Leave.*

6. The subsidy balance ranging from 1 to 56 percent totaling P2.499 billion pertaining to the 1,773 liquidated SEP/BLEP/PAMANA projects remained unreleased to the concerned ECs as of December 31, 2018 contrary to Section 4.5.3 of COA Circular No. 2007-001, hence, casts doubt on the reliability of the evaluated project cost.

   Recommendations:

   a. *Review the evaluation of project cost to determine the right amount to release based on the causes of unreleased funds ranging from 1 to more than 50 percent for more efficient budget allocation of subsidized projects and to maximize the use of funds released by the National Government (NG) thru the BTr;*

   b. *Evaluate thoroughly the ECs request for subsidy in accordance with the evaluated project cost and to release only what is required; and*

   c. *Conduct confirmation/inspection of the reported potential household/population unenergized as per Barangay Certification.*

7. The 90 percent initial release of subsidy fund to electric cooperatives (ECs) in CY 2018 for the implementation of electrification projects totaling P1.479 billion (gross) was found to be excessive which is not in accordance with Item 4.2 of COA Circular No. 2007-001.

   Forty-two ECs were released with subsidy funds for 2018 SEP projects amounting to P1.208 billion even if there were subsidy balances totaling P529 million that were not yet fully liquidated, contrary to Section 2 of COA Circular No. 2012-001.

   Also, subsidy for the construction of distribution lines were released to 40 ECs simultaneously with the release of subsidy for the installation of kwhr meters, duplex service drop wires and housewiring materials which is not in conformity with Section 2 of COA Circular No. 2012-001.

   Recommendations:

   a. Stop the grant of 90 percent initial release of subsidy fund to ECs in conformity with COA Circular No. 2007-001;

   b. Process only request for subsidy releases which previous subsidy balances are fully liquidated;

   c. Demand the concerned ECs to immediately liquidate the completed and energized projects pursuant to COA Circular No. 2012-001 and the MOA between NEA and ECs; and

   d. Release subsidy funds for the installation of kwhr meters, duplex service drop wires and housewiring materials, after partial liquidation of construction of distribution lines by EC's submission to NEA the Certification of Construction of Completed (COCC) projects duly certified by the Barangay Chairman of the respective sitios and the authorized officials of ECs.

8. Unliquidated subsidy balance amounting to P23.903 billion covering the period from CYs 2011-2018 for the SEP, BLEP, PKKV, TISP-ARMM, YRRP and other calamity grants projects was reduced to P1.052 billion, however, remained unliquidated as of December 31, 2018, which is not in conformity with Section 2 of COA Circular No. 2012-001 and Section 4 of the Memorandum of Agreement (MOA) between NEA and ECs.

   Recommendations:

   a. Require ECs to:

      i. liquidate all subsidy releases that are already due for liquidation by submitting all the required liquidation together with Accounting of Funds with its supporting documents to validate the charges made to the subsidy fund; and

      ii. return the unliquidated funds of all completed projects from prior years considering that the projects are already more than three years since its inception;

b. Refrain from releasing additional subsidy until ECs fully liquidation of prior releases; and

c. Comply strictly with Section 4 of the MOA as agreed by NEA and ECs.

9. The Accounting of Funds (AFs) submitted by some ECs for 170 liquidated subsidies under Regular Subsidy, SEP, BLEP, YRRP and Calamity Grant with reported unexpended/unutilized balance totaling P43.684 million were not returned/remitted immediately upon liquidation due to NEA's non enforcement of Section 7 of the MOA, hence, deprived the government of funds to utilize for other projects.

   Deficiencies/discrepancies were noted on the ECs' supporting documents, resulting in the increase of the reported unexpended balance of P43.684 million per AFs to P94.660 million (net of amount already returned) and the same was not returned/remitted to NEA contrary to Section 4.5.6 of COA Circular No. 2007-001 and Sections 2 and 7 of the MOA and NEA Memorandum No. 2013-023.

   ECs with subsidy deficit of P19.232 million is to be covered with the release of the 49-50 percent remaining/retention balance but not to exceed the actual disbursement under Section 4 of the MOA.

   Unexpended balance amounting to P105.247 million remained unreturned for projects audited in CYs 2014 – 2017.

   Liquidated subsidies were not reversed and unexpended subsidy balances per audit were not recognized in NEA's books contrary to Section 112 of PD No. 1445. Hence, the reliability of the account Due from NGOs/POs was doubtful.

   Recommendations:

   a. Require the 11 ECs audited in CY 2018 to return/remit the unexpended balances amounting to P94.660 million;

   b. Ensure that only related/allowed expenses are charged in the AF;

   c. Inform the concerned EC's to submit required documents for the release of the remaining balances amounting to P17.779 million but not to exceed the actual disbursements pursuant to Section 4 of the MOA only after the unexpended balances have been settled, if any;

   d. Refund to CENPELCO and ISELCO I the excess returns/remittances amounting to P300,205;

   e. Require the EC's to submit the required documents to validate the charges made in the AFs together with the supporting schedule of the previous and the revised AFs, for verification and adjustment of the total unexpended balances, otherwise, return to NEA the total amount of P105.247 million;

   f. Prepare the necessary accounting entries in NEA's books to reflect the correct amount of Due from NGOs/POs account and to be able to monitor *the status/movement of the unexpended/unutilized subsidy balances pursuant to Section 112 of PD No. 1445; and*

g. *Strictly enforce the provision of Section 7 of the MOA on the return/remittance of unutilized funds.*

10. The Disbursements Acceleration Program (DAP) under 2011 OPAPP/TISP, OVLP/LGSF and 2012 Subsidy Funds allocated for rural electrification totaling P102.565 million remained unreleased as of December 31, 2018 and not returned to the Bureau of the Treasury (BTr) in violation of Section 83 of the General Provisions of General Appropriation Act of 2018.

    Likewise, the DAP funds released to Electric Cooperatives (ECs) totaling P31.767 million remained unliquidated as of December 31, 2018, in violation of Section 4.5.6 of COA Circular No. 2007-001 and Sections 3 and 4 of the MOA between NEA and ECs.

    Recommendations:

    a. *Immediately return to the Bureau of the Treasury the unreleased subsidy fund amounting to P102.565 million in compliance with Section 83 of the General Provisions of General Appropriation Act of 2018 and the Supreme Court decision;*

    b. *Stop the practice of granting subsidies to ECs without liquidating first the previous subsidy granted in compliance with the MOA and Section 4.5.6 of the COA Circular No. 2007-001;*

    c. *Strictly require the concerned ECs to immediately liquidate subsidy funds received pursuant to Sections 3 and 4 of the MOA, with attached schedule or summary to support the charged disbursements properly arranged and labeled to facilitate the closing of the books of both ECs and NEA; and*

    d. *Direct the ECs to strictly comply with the agreed provisions specifically Sections 3 and 4 of the MOA.*

11. Obligated/Allocated SEP and/or BLEP projects aged two to seven years totaling P70.135 million remained unreleased as of December 31, 2018 which is not in accordance with Section 2 of P.D. No. 1445, thus, deprived the intended beneficiaries of the unenergized sitios of much-needed funds for electrification.

    Recommendations:

    a. *Submit explanation/justification on the non-release of obligated/allocated subsidy funds to 12 ECs for more than two to seven years and the unreleased subsidy funds for ALECO;*

    b. *Re-evaluate thoroughly the ECs' requested subsidy funds, if any, and expedite the obligation allocation and release of the said request to ECs specifically sitios that are in dire need of the energization; and* *c. Return the funds if no longer needed.*

F. **Summary of Total Disallowances, Suspensions and Charges as of December 31, 2018**

Based on the Notice of Disallowances issued, total audit disallowances found in the audit of various transactions of NEA, as of December 31, 2018, after the effectivity of the Rules and Regulations of Settlement of Accounts (RRSA) amounted to P124,883,630.31. There was no Notice of Suspension and Notice of Charge issued as of December 31, 2018. Details are found in Part II of this Report.

G. **Status of Implementation of Prior Year's Audit Recommendations**

The status of audit recommendations contained in the AAR for CY 2017, is presented in Part III of this Report. Out of the 100 audit recommendations, 48 were implemented, 35 were partially implemented and 17 were not implemented.