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. President Benigno S. C. Aquino III, in May 7, 2013, 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 Report 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 2016. 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 2016.

Financial Position

Particulars	2016	2015	Increase (Decrease)
Assets	27,038,801	35,954,710	(8,915,909)
Liabilities	32,033,519	30,908,285	1,125,234
Equity	(4,994,718)	5,046,425	(10,041,143)

Financial Performance

Particulars	2016	2015	Increase (Decrease)
Gross income	631,402	737,517	(106,115)
Other income	36,222	59,493	(23,271)
Total income	667,624	797,010	(129,386)
Operating expenses	410,790	416,459	(5,669)
Other expenses	93,787	53,496	40,291
Total expenses	504,577	469,955	34,622
Net profit before income tax	163,047	327,055	(164,008)
Income tax expense	53,655	92,973	(39,318)
Net profit	109,392	234,082	(124,690)

Budget Utilization

	Budget	Expenditures
Personal services	292,389	252,977
Maintenance and other operating expenses	414,441	462,708
Capital outlay	72,633	14,270
Total	**779,463**	**729,955**

C. Operational Highlights

For CY 2016, NEA reported the following major accomplishments:

a. Completion of Sitio Electrification Program

- The NEA together with the ECs nationwide, has completed the energization of the 32,441 sitios under the Sitio Electrification Projects (SEP). NEA has received a total of P30.932 billion subsidy assistance, P20.047 billion of which is for the implementation of the SEP.

  From October 2011 to March 31, 2016, NEA was able to connect to the grid a total of 32,688 sitios (out of the 32,441), bringing the country's sitio electrification level to 82 percent and raising the number of consumer connections to P11.305 million, benefitting the lives of approximately 57 million Filipinos. The overall target for household was pegged by the Department of Energy at 90 percent for 2017.

b. ISO 9001: 2008 Certification

- The NEA has demonstrated anew its compliance to international quality standards after successfully passing last 10 November 2016 the second surveillance audit of the ISO 9001 with upgrade to 2015 standard. This places NEA among the first national government agencies to be upgraded to the 2015 vision and confirms the effectiveness of its Quality Management System (QMS).

c. Don Emilio Abello Energy Efficiency Award

- NEA was among the 10 outstanding recipients of this year's award on "Energy Efficiency and Conservation in Government Buildings," in terms of energy savings generated at 43.53 percent. The award was given by the Department of Energy (DOE) under the Government Energy Management Program (GEMP) anchored on Administrative Order 110 and 126 as amended.

  NEA was cited for its commendable accomplishments in its conservation initiatives which resulted in the realization of energy savings amounting to P6.9 million equivalent to 699 MWH and CO2 avoidance of 358 tons as against the average energy consumption baseline year in 2004. It has been given a grade of 95 percent in its energy audit spot check.

d. Task Force Kapatid "Lawin" and "Nina"

- NEA and ECs mobilized efforts through Task Force Kapatid (TFK): Power Restoration in the Typhoon Lawin-affected areas within the coverage of Cagayan I Electric Cooperative, Inc. (CAGELCO I), Isabela II Electric Cooperative, Inc. (ISELCO II) and Kalinga-Apayao Electric Cooperative, Inc. (KAELCO) on 26 October 2016.

  This is in accordance with the directive of Energy Secretary Alfonso G. Cusi to facilitate immediate power restoration to alleviate living condition in some 294, 321 households in the typhoon-ravaged areas.

  Task Force Kapatid, also dubbed as "Compact of Cooperation" is a re-visit to the tried and tested spirit of Bayanihan. Institutionalized since 2004 by NEA and in partnership with the ECs, this program is anchored on the deeply-entrenched traditions of cooperation, unity and concern among ECs nationwide under the leadership and guidance of NEA, and later joined by other privately-owned distribution utilities.

  There were 31 ECs which voluntarily participated in the Task Force Kapatid Lawin. NEA engineers were deployed to work with the EC teams, in fast-tracking the activities and consolidating all efforts, in the rehabilitation of the damaged distribution lines. For CAGELCO I alone, initial cost of damaged distribution lines is estimated at P89 million.

  As of 12 January 2017, restoration level for household connections is at 95.43 percent. The target date of full restoration is on or before 28 February 2017.

  Also, in December 2016, another strong typhoon, locally named "Nina" caused damages in the provinces of Quezon, Oriental Mindoro, Marinduque, Camarines Sur, Albay, Catanduanes and Sorsogon affecting 1,683,012 households in the EC coverage areas.

  There were 43 ECs which participated in the power restoration efforts consisting of 874 EC manpower and 15 NEA ground personnel. A total of 136,116 affected households or 91.91 percent were re-energized as of 25 January 2017.

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, 2016 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.

Other Financial and Compliance Issues

1. The accuracy and reliability of the P18.188 billion year-end balance of account Due to National Treasury which represents Advances by the National Government thru the Bureau of the Treasury on NEA's foreign loans could not be determined due to the existence of an unidentified reconciling item amounting to P3.836 billion per confirmation schedule received from BTr and unreconciled variance of individual old and new loan accounts per NEA's books by the same total amount.

   Recommendations:

   a. *Inquire with the BTr the noted unidentified reconciling item on the interest of advances under old loans amounting to P3,836,006,287.21 for its further analysis and identify to which particular loan account should be recorded;*

   b. *Discuss with the BTr the noted unreconciled individual loan accounts so that necessary adjustments can be made by either NEA or BTr in the respective books of accounts; and*

   c. *Cause the settlement of the outstanding obligations to the BTr, should the request for conversion be not granted.*

2. Overstatement of P452.501 million and understatement of P520.357 million or a net variance of P67.856 million were found existing between the year-end balance of Loans Receivable amounting to P9.445 billion (current and long-term) and the results of confirmation from Electric Cooperatives (ECs) totaling 5.487 billion. The variance was attributed mainly to loans not included in ECs confirmation, difference in net amount of loans, unrecorded amortization, and advance interest in NEA's books.

   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 NEA's books and/or in 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.*

3. Of the total outstanding Miscellaneous Receivables amounting to P56.098 million (net) as of December 31, 2015, only P4.107 million or 7.32 percent was collected at the year-end and the amount of P52.079 million remained unsettled and outstanding in the books for more than 10 years with remote possibility of collection.

   Recommendations:

   a. *Exhaust all possible remedies to collect the receivables from the debtors and the employees who are no longer connected with NEA; and*

   b. *Expedite the evaluation and reconciliation of all overdue accounts to determine its proper disposition and make the necessary adjustment in the books or request for write-off, if warranted.*

4. NEA continuously granted various PRAISE incentives to its officials and employees totaling P21.503 million without approved budget from the Department of Budget and Management (DBM) and supporting computation of monetary savings generated out of superior accomplishments and other personal efforts, as required in Section 15 of Executive Order 518 and Civil Service Commission (CSC) Resolution No. 010112 and CSC Memorandum Circular No. 01 s. 2001.

   Recommendations:

   a. *Stop the grant of PRAISE incentives without an approved budget, and for future grant thereof, provide corresponding budget/allocation in the COB for DBM approval;*

   b. *Submit proof and justification that the superior accomplishments and other personal efforts by individuals or groups have resulted in monetary savings and that PRAISE incentives did not exceed 20 percent of the monetary savings generated; and*

   c. *Cause the refund to NEA the PRAISE incentives granted to the employees.*

5. Grant of monetary retirement award amounting to P2.180 million to honor retiring officials and employees for CYs 2013 to 2016 was not in accordance with the CSC Memorandum Circular No. 7, series of 1998 and Section 28 (b) of Commonwealth Act No. 186 as amended by Republic Act (RA) No. 4968 or the Teves Retirement Law.

Recommendations:

a. *Stop the grant of monetary retirement award to retiring employees; and*

b. *Require the retired/separated employees who received the monetary retirement award to refund the said amount in compliance with the General Provisions of GAA – Use of Appropriations for Retirement Gratuity and Terminal Leave.*

6. Various asset and liability accounts recorded in the subsidiary ledgers were not effectively monitored, resulting in abnormal negative balances amounting to P12.894 million.

Recommendations:

a. *Require the Accounting Division to review, analyze the accounts and identify all abnormal debit/negative balances that remained unreconciled/unadjusted;*

b. *Determine the nature of transaction and reason for the error that caused the abnormal balance and prepare the necessary adjusting entries to correct the account balance; and*

c. *Require the Accounting personnel in charge of monitoring the accounts to regularly monitor the accounts recorded in the subsidiary ledger to avoid incurrence of abnormal negative balances.*

7. No Report of Physical Count of Inventory (RPCI) for supplies and spare parts was prepared and submitted to COA as required in Section 122 of PD 1445;

Stock ledgers maintained by the Accounting Division for Inventory items showed negative balances totaling P12.440 million.

Recommendations:

a. *Require the Senior Supply/Property Officer to prepare and submit Physical Inventory Report of supplies by type as at a given date, showing the balance of all inventory items per count, in compliance with the provision of Section 122, Chapter 3 of PD 1445;*

b. *Designate a dedicated accounting personnel to analyze the 36 Inventory items to determine the causes of the negative balances and* *make the necessary adjustments, if warranted; submit explanation on the existence of negative balances for the 36 inventory items.*

8. Loan granted to Philippine Rural Electric Cooperatives, Inc. (PHILRECA) in October 1991 amounting to P10 million which was disallowed in September 1992 due to lack of legal bases remained unsettled for more than 20 years and recorded under account *Loans Receivable – Others* instead of *Receivables – Disallowance/Charges.*

   Recommendations:

   a. *Reclassify the account Loans Receivable from PHILRECA to Receivables – Disallowance and Charges amounting to P7,816,719.00; and*

   b. *Take appropriate legal action to compel PHILRECA to settle its long outstanding account and determine the propriety of charging interest and surcharges on the said loan taking into account the COA disallowance.*

Subsidy Fund Releases to Electric Cooperatives

9. SEP/BLEP Projects funded out of subsidy releases totaling P5.928 billion have been completed/implemented, but said amount remained unliquidated as of December 31, 2016. The year-end balance of account Due from NGOs/POs amounting to P6.897 billion could have been reduced had prompt liquidation been strictly observed pursuant to Section 2 of COA Circular No. 2012-001 and Sections 3 and 4 of the MOA between ECs and NEA.

   Recommendations:

   a. *Discontinue the grant of subsequent releases to ECs with unliquidated subsidy balances and enforce Section 2 of COA Circular No. 2012-001 by requiring full liquidation of prior releases; and*

   b. *Require ECs to immediately submit all the necessary documents to liquidate the subsidy balances to facilitate the closing out of the books of both NEA and the ECs pertaining to the subsidy fund; and*

10. Unexpended balance of YRRP funds amounting to P274.445 million was realized which have not been returned to NEA pursuant to Sections 2 and 7 of the MOA.

    Also, various disbursements were found improperly charged against YRRP Fund due to:

    a. Payroll salaries of regular employees for several months;
    b. Unutilized materials charged against the subsidy fund;

c. Materials Charge Tickets (MCTs), labor and overhead expenses beyond the issuance of the Certificate of Final Inspection and Acceptance (CFIA);
d. Payment of Honorarium for Task Force Kapatid without NEA's approval;
e. Cash advances not supported with liquidation documents;
f. Expenses not directly related to YRRP project;
g. Unutilized Materials were charged against the subsidy fund; and
h. Undocumented/Unsubmitted disbursement documents.

Further, deficiencies were noted on Materials Charge Tickets (MCTs), As Built Staking Sheets, Bill of Materials and Fuel Stock Requisition and Issuance Slip.

Also, the amount of P4.5 million was utilized for the purchase of vehicles and construction of building in CELCO which was not allowed under the NEA Guidelines on YRRP Implementation and Release of Funds to ECs.

Electric Cooperatives with subsidy deficit (excess disbursements over the subsidy receipts) totaled P35.624 million to be covered with the release of the remaining balance up to the actual amount of disbursements allowed in audit.

Recommendations:

a. *Require the concerned ECs to return/refund to NEA the unexpended/ unutilized balance of the subsidy received in accordance with Sections 2 and 7 of the MOA and other NEA Memoranda on the proper use of subsidy funds, furnishing immediately the COA Office a photocopy of the official receipt, for monitoring purposes;*

b. *Require the ECs to request approval from NEA for any deviations from the MOA and furnish COA Office of the approved copy, if any;*

c. *Ensure compliance on the submission of documentary requirements required under NEA Memorandum dated Nos. 2013-022 and 2013-023 and YRRP Memorandum Guidelines dated February 20, 2014;*

d. *Compel the NEA audit team to conduct examination of the liquidation of documents as required in the NEA guidelines for YYRP;*

e. *Require the ECs to make a thorough review of the Accounting of Funds to ensure accuracy/correctness of the reports submitted.*

f. *Refrain from charging to the YRRP funds expenses that are not within the coverage of the YRRP Memorandum Guidelines, otherwise, charge these expenses to EC's General Fund;*

g. *Charge only actual materials utilized per MCTs and not the total materials purchased;*

h. *Require the EC to return immediately to NEA the amount of P4.5 million used in the purchase of vehicles and construction of a new building,* *etc. as these are not valid expenses pursuant to Section 7 of the MOA; and*

i. *For ECs with subsidy deficit, release the remaining balance but only up to the amount allowed in the audit;*

11. Unallocated/Unobligated Disbursement Acceleration Program (DAP) Funds as of December 31, 2016 amounting to P434,249 remained in NEA's books of account and not returned to the Bureau of the Treasury (BTr) in violation of COA Circular No. 94-013.

    Likewise, the remaining balance or 10 percent retention of DAP subsidy funds for implemented and liquidated projects totaling P82.056 million had not been returned to BTr.

    Recommendation:

    a. *Return to the BTr the additional unallocated subsidy fund totaling P434,249.15 and the remaining unreleased balance for projects already implemented and liquidated totaling P82,055,991.67.*

12. DAP Funds released for Rural Electrification under the 2011 OPAPP/TISP, OVLP/LGSF and 2012 SEP Funds totaling P194.544 million remained unliquidated as of December 31, 2016 in violation of Item No. 2 of COA Circular No. 2012-001 and Sections 3 and 4 of the MOA between NEA and ECs. Likewise, 97 ECs with substantial amount of unutilized/unexpended balances have not returned nor requested for realignment of sitios allied to the projects.

    Recommendation:

    a. *Require the ECs to immediately liquidate the subsidy receipts to facilitate the closing of the books. And for ECs with substantial amount of unexpended balances, expedite the request for realignment to other sitios, otherwise, return the unutilized balance to facilitate the closing of the books of both ECs and NEA.*

13. EC's inclusion of Input Value Added Tax (VAT) in the presentation of subsidy Accounting of Funds amounting to P145.688 million pursuant to NEA Memorandum No. 2015-036 resulted in the overstatement of the charges made in the Accounting of Funds and reduced the government revenue as ECs VAT remittance to the Bureau of Internal Revenue (BIR) included the subsidy funded Input VAT.

    Recommendations:

    a. *Require the aforementioned 14 ECs and other ECs that have not been audited yet to return to NEA the input VAT and any Input VAT charged to the liquidated subsidy funds as indicated in the AOF upon* *the effectivity of the NEA Memorandum No. 2015-36 furnishing COA Office of the Official Receipts on the remittance; and*

b. *Revisit NEA-Memorandum No. 2015-36 and consider revising the provisions to exclude Input VAT in the Accounting of Subsidy Fund so that proper Input VAT will be remitted to the BIR.*

14. The required posting of Performance Security on the subsidy fund released to the Electric Cooperatives (ECs) remained unenforced, thus, posing risk of non-compliance with project implementation within the prescribed completion date and not in conformity with COA Circular No. 2007-001.

Recommendations:

a. *Enforce the ECs to post performance security to guarantee completion of projects funded out of government subsidy within 90 days as required under Section 4.5.7 of COA Circular No. 2007-001; and*

b. *Include a provision in the MOA between NEA and ECs requiring the mandatory posting of performance security by the latter and no release of subsidy should be made unless the performance security is presented to NEA.*

F. Status of Implementation of Prior Year's Audit Recommendations

Of the 117 audit recommendations embodied in the 2015 Annual Audit Report, 50 were implemented, 40 were partially implemented and 27 were not implemented. Details are presented in Part III of this Report.