PHILIPPINE STOCK EXCHANGE, INC.
Philippine Stock Exchange Centre
Exchange Road, Ortigas Center
Pasig City

Attention: Ms. Janet A. Encarnacion
Head, Disclosure Department

Re: DENR Fine Imposed on Manila Water

Gentlemen:

We write to you in response to your letter dated 16 November 2009 requesting Manila Water Company, Inc. (MWCI) to explain in writing within twenty-four (24) hours from receipt hereof why the non-disclosure of the imposition of penalty on the Company by the PAB does not constitute a violation/s of the Disclosure Rules of the Philippine Stock Exchange (PSE). This matter is also connected to our previous disclosure made by MWCI on 5 November 2009.

As a background, the above matter relates to a pending case, docketed as DENR-PAB NCR-00794-09, before the Pollution Adjudication Board (PAB) of the Department of Environment and Natural Resources (DENR) filed by the Regional Directors of DENR against Metropolitan Waterworks and Sewerage System (MWSS), MWCI and Maynilad Water Services, Inc. (MWSI) for violation of Republic Act No. 9275 otherwise known as the “Clean Water Act” particularly Sec. 8 thereof which provides that:

SECTION 8. Domestic Sewage Collection, Treatment and Disposal. — Within five (5) years following the effectivity of this Act, the agency vested to provide water supply and sewerage facilities and/or concessionaires in Metro Manila and other highly urbanized cities (HUCs) as defined in Republic Act No. 7160, in coordination with LGUs, shall be required to connect the existing sewage line found in all subdivisions, condominiums, commercial centers, hotels, sports and recreational facilities, hospitals, market places, public buildings, industrial complex and other similar establishments including households to available sewerage system: Provided, That the said connection shall be subject to sewerage services charge/fees in accordance with existing laws, rules or regulations unless the sources had already utilized their own sewerage system: Provided, further, That all sources of sewage and septage shall comply with the requirements herein.

In areas not considered as HUCs, the DPWH in coordination with the Department, DOH and other concerned agencies, shall employ septage or combined sewerage-septage management system.
For the purpose of this section, the DOH, in coordination with other government agencies, shall formulate guidelines and standards for the collection, treatment and disposal of sewage including guidelines for the establishment and operation of centralized sewage treatment system.

Despite the valid explanations of MWCI and the other respondents, the PAB issued its Order dated 7 October 2009 imposing a fine of P29.4 M plus P200,000.00 per day counted from 7 May 2009 to 30 September 2009.

Under the Rules of Procedure of the PAB, MWCI has fifteen (15) days from receipt of the Order within which to file its motion for reconsideration. On 29 October 2009, MWCI timely filed its Motion for Reconsideration dated 22 October 2009 before the PAB. Hence, for all intents and purposes, the case is still pending and the Order of the PAB imposing the fine against MWCI is not final and executory and cannot be enforced.

MWCI did not disclose the imposition of the fine in the above-mentioned Order based on several grounds. First, MWCI believes that the judgment of the PAB is void for having been issued with grave abuse of discretion amounting to lack or in excess of jurisdiction. Second, granting arguendo that the imposition of fine was a mere error in judgment and not of jurisdiction, the same is not yet final and executory to be enforceable as against MWCI. Third, based on the standards of the Exchange under Sec. 4.3 of the Revised Disclosure Rules, MWCI honestly believed that such an event did not pass the threshold established therein for a disclosure to be made. These reasons are elaborated further hereunder.

First of all, based on the merits of the case, one can clearly see that the questioned Order of the PAB was void for having been issued with grave abuse of discretion amounting to lack of or in excess of jurisdiction. Considering that such Order is void for errors of jurisdiction, the same should neither be enforced against MWCI nor should it prejudice MWCI in any way. This can be gleaned clearly in the Motion for Reconsideration filed by MWCI.

The Motion for Reconsideration was filed because the Order dated 7 October 2009 of the PAB is replete with reversible errors, both procedural and substantial, not to mention jurisdictional. In fact, as stated by MWCI in its prefatory, “orderly administration of justice dictates that governmental agencies be allowed to correct themselves, respondent MWCI hereby submits this motion to allow this Honorable Office to rectify a foreboding injustice and oppressive treatment of respondent MWCI in the hands of its regulators.”

Further, the said Motion for Reconsideration was submitted based on meritorious grounds which include the following:

1. The PAB committed grave and serious error when it ruled that MWCI violated the Clean Water Act despite the absence of the condition precedents necessary and required for its compliance. In particular, contrary to the provision of the law, the Department of Public Works and Highways (DPWH) has failed to formulate and establish the National Sewerage and Septage Management Program (NSSMP) which is the foremost condition precedent for the implementation of the Clean Water Act. The elementary rules of fair play dictate that the
NSSMP must first be formulated and established before MWCI could be held accountable for the violation of the Clean Water Act. After all, one must know what he is complying with before he can actually tailor his activities to conform thereto.

2. MWCI is only mandated to connect “existing sewage lines” to “available sewerage systems” which it has achieved over the past twelve (12) years of its existence. MWCI has been connecting sewage lines to available sewerage systems and continues to build the necessary infrastructure to add more wastewater lines and systems. At present, a total of two hundred eighteen (218) kilometers of sewer lines have been utilized by MWCI to service its customers. This is part of the network of Sewage Treatment Plants (STPs) and other networks that have been built over the service area. Other STPs have also been built in the cities of Makati, Quezon, Pasig, and Taguig. In addition to these projects, MWCI acted on areas without sewerage systems by expanding its sanitation or septage management services. At present MWCI has completed two (2) septage projects: the North Septage Treatment Plant (SpTP) in San Mateo and the South SpTP in Taguig. Moreover, MWCI has also undertaken the procurement of vacuum desludging tankers expanding MWCI’s fleet to ninety-three (93) vacuum trucks to improve and expand sanitation/septage management services throughout the East Zone.

3. The system for coordination among various government agencies for the implementation of the Clean Water Act has not been established. It is the DPWH who has the obligation to coordinate with the concessionaires for the preparation of a compliance plan with regard to the Clean Water Act. However, despite the requirement of a condition precedent under the law, the DPWH has not initiated such efforts in order that a comprehensive compliance plan could be formulated.

4. The timetable of five (5) years under the Clean Water Act admits of exceptions. There is a regime for wastewater services in the MWSS franchise areas and such arrangement is governed by the respective concession agreements of the concessionaires. The only logical explanation why the Implementing Rules subjected the provision of sewerage facilities and sewage lines to the concession agreements of the MWSS and its concessionaires is the fact that MWSS, being a public functionality, benefits from the presumption that its functions are performed in a regular manner in accordance with its mandate under the MWSS Charter. Moreover, the Implementing Rules recognized that MWSS, being the public utility for the water sector, is imbued with necessary expertise to determine the proper and feasible timetable for the implementation of sewerage projects.

5. The PAB committed serious and grave error when it disregarded the accomplishment of MWCI. The truth is MWCI has made significant improvement in wastewater service and management since its entry in 1997. The East Zone of the MWSS franchise area covers a population of about seven (7) million, of which more than five (5) million have direct access to water supply services provided by MWCI and MWSS. The improvements and expansion in water services in the East Zone have been significant in the last twelve (12) years of MWCI’s operations. Twenty four-hour water availability increased from 26% to 99% in the Central Distribution System, water losses dropped from 63% to 20% and an additional two (2) million people have been provided water services. While MWCI continues to expand water services, it is also now concentrating on expanding the provision of wastewater services in its service area.
From the original sewer coverage of 3%, MWCI has expanded its coverage to 12% as of 2007. This was achieved through the construction of new treatment plants. MWCI is now operating a total of thirty one (31) sewage treatment plants, with a total capacity of 85 million liters per day (MLD).

6. The PAB committed serious and grave error when it violated its own Rules of Procedure by directing the respondents (including MWCI) to pay the penalty without the Order becoming final and executory. The palpable error of the PAB is a display of its utter disregard of the rights of the respondents (including MWCI) to either file a motion for reconsideration or an appeal against its Order. Moreover, this clearly demonstrates the persecution, rather than the prosecution, aspect of the whole exercise.

Second, granting arguendo that the imposition of fine was a mere error in judgment and not of jurisdiction, the same is not yet final and executory to be enforceable as against MWCI. Under the PAB Rules of Procedure, only final and executory orders of the PAB may be enforced and they will be implemented in the same manner as orders, resolutions and decisions of the Regional Trial Court (RTC). Hence, considering that with the same is not yet final and executory, the same is not, in any way, prejudicial to the shares of MWCI. The trigger event which would signify the possibility that the Order will be enforced is the issuance of a writ of execution. However, such a writ will only be issued once the Order becomes final and executory. Until such time and unless a writ of execution is issued, the Order shall not prejudice MWCI's financials.

Third, based on the standards of the Exchange under Sec. 4.3 of the Revised Disclosure Rules, MWCI honestly believed that such an event did not pass the threshold established therein for a disclosure to be made. Under Sec. 4.3, it is stated therein that:

Section 4.3 STANDARD AND TEST IN DETERMINING WHETHER DISCLOSURE IS NECESSARY -

a. Where the information is necessary to enable the issuer and the public to appraise their position or standing, such as but not limited to, those relating to the Issuer’s financial condition, prospects, development projects, contracts entered into in the ordinary course of business or otherwise, mergers or acquisitions, dealings with employees, suppliers, customers and others, as well as information concerning, a significant change in ownership of the Issuer’s securities owned by insider’s or those representing control of the Issuer;

b. where such information is necessary to avoid the creation of a false market for its securities;

c. where such information may reasonably be expected to materially affect market activity and the price of its securities.
Based on the above provision, the circumstances enumerated in paragraphs (a) and (b) are not applicable in this case. However, one may argue that paragraph (c) may be applicable. Nevertheless, upon closer examination, the application of paragraph (c) in this particular case is more apparent than real. This is because the fine or imposition of the PAB against MWCI, assuming it can be enforced, cannot materially affect the market activity or the price of MWCI's securities. As can be gleaned from the other provisions of the Revised Disclosure Rules, the latter sometimes pegs the threshold or standard at ten percent (10%). In Sec 4.4 (b) the threshold is 10% of total current assets, in (f) losses must be 10% of consolidated assets, etc. In this case, the P29M fine is relatively small considering the size of MWCI and is not even ten percent (10%) of its total assets. Hence, using the PSE's own threshold amount, the fine imposed against MWCI will not materially affect its market activity or the price of its securities.

We hope we have sufficiently clarified this matter and that the above explanation has passed the test of reasonableness.

Best regards.

Sincerely,

JHOEL P. RAQUEDAN
Legal and Corporate Governance Head