

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Energy Development (EDC) Corporation
Merritt Road, Fort Bonifacio
Taguig City

We have audited the accompanying financial statements of Energy Development (EDC) Corporation (formerly PNOC Energy Development Corporation), a subsidiary of Red Vulcan Holdings Corporation, which comprise the parent company balance sheets as of December 31, 2008 and 2007, and the parent company statements of income, parent company statements of changes in equity and parent company statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Philippine Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Philippine Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance 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 audit opinion.



Opinion

In our opinion, the parent company financial statements referred to above present fairly, in all material respects, the financial position of Energy Development (EDC) Corporation as of December 31, 2008 and 2007, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.



Betty C. Siy-Yap

Partner

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PTR No. 1566469, January 5, 2009, Makati City

March 30, 2009



ENERGY DEVELOPMENT (EDC) CORPORATION
(Formerly PNOC Energy Development Corporation)
A Subsidiary of Red Vulcan Holdings Corporation

PARENT COMPANY BALANCE SHEETS

	December 31	
	2008	2007
ASSETS		
Current Assets		
Cash and cash equivalents (Notes 5 and 40)	₱773,817,457	₱2,797,581,577
Trade and other receivables - net (Notes 6, 28 and 40)	5,290,943,531	4,925,681,584
Current portion of concession receivable (Notes 32 and 40)	2,048,110,310	2,199,986,327
Available-for-sale (AFS) investments (Notes 9, 29 and 40)	674,494,128	1,177,589,987
Parts and supplies inventories - at cost (Note 7)	1,561,388,667	1,140,044,062
Due from a related party (Notes 37 and 40)	95,475,959	-
Derivative assets (Note 40)	614,081,623	-
Other current assets (Notes 8, 37 and 40)	600,325,982	535,582,774
	11,658,637,657	12,776,466,311
Noncurrent assets held for sale (Note 10)	1,797,587,000	1,672,516,100
Total Current Assets	13,456,224,657	14,448,982,411
Noncurrent Assets		
Concession receivable - net of current portion (Notes 32 and 40)	32,647,323,888	34,695,434,198
Intangible assets - net (Notes 12 and 32)	9,389,193,091	8,738,836,827
Deferred income tax assets - net (Note 30)	3,410,392,338	3,052,792,587
Exploration and evaluation assets (Notes 13 and 26)	999,757,259	1,171,922,174
Property and equipment - net (Notes 11 and 32)	1,137,814,405	1,111,020,356
Investments in subsidiaries (Note 14)	5,836,311,024	-
Other noncurrent assets - net (Notes 15, 20, 28 and 40)	1,365,986,414	1,851,746,313
Total Noncurrent Assets	54,786,778,419	50,621,752,455
TOTAL ASSETS	₱68,243,003,076	₱65,070,734,866

LIABILITIES AND EQUITY

Current Liabilities

Loan payable (Notes 17 and 40)	₱2,000,000,000	₱-
Trade and other payables (Notes 3, 16 and 40)	2,738,961,006	3,637,782,267
Due to a related party (Notes 37 and 40)	47,213,065	-
Income tax payable (Note 30)	84,802,074	418,986,388
Derivative liabilities (Note 40)	54,250,018	-
Current portion of:		
Long-term debt (Notes 20 and 40)	8,217,253,830	2,031,565,879
Obligations to a power plant contractor (Notes 19 and 40)	112,187,446	246,719,220
Royalty fee payable (Notes 18, 33 and 40)	1,688,282,467	456,273,707
Total Current Liabilities (Carried Forward)	14,942,949,906	6,791,327,461



	December 31	
	2008	2007
Total Current Liabilities (Brought Forward)	₱14,942,949,906	₱6,791,327,461
Noncurrent Liabilities		
Long-term debt - net of current portion (Notes 20 and 40)	21,099,796,908	20,809,947,547
Royalty fee payable - net of current portion (Notes 18, 33 and 40)	-	1,277,653,457
Obligations to a power plant contractor - net of current portion (Notes 19 and 40)	-	96,287,392
Retirement and other post-retirement benefits (Note 38)	1,026,394,482	919,828,294
Other long-term liabilities (Note 21)	312,816,858	322,410,109
Total Noncurrent Liabilities	22,439,008,248	23,426,126,799
Equity		
Common stock (Note 22)	15,000,000,000	15,000,000,000
Preferred stock (Note 22)	75,000,000	75,000,000
Additional paid-in capital (Note 22)	6,278,075,648	6,278,075,648
Cost of treasury stock held (Note 22)	(404,219,068)	-
Accumulated unrealized gain on AFS investments (Note 9)	30,826,354	368,549,253
Retained earnings (Note 22)	9,881,361,988	13,131,655,705
Total Equity	30,861,044,922	34,853,280,606
TOTAL LIABILITIES AND EQUITY	₱68,243,003,076	₱65,070,734,866

See accompanying Notes to Parent Company Financial Statements.



ENERGY DEVELOPMENT (EDC) CORPORATION
(Formerly PNOC Energy Development Corporation)
A Subsidiary of Red Vulcan Holdings Corporation

PARENT COMPANY STATEMENTS OF INCOME

	Years Ended December 31	
	2008	2007
REVENUES		
Revenue from sale of electricity (Notes 36 and 44)	₱11,134,709,615	₱11,291,898,705
Revenue from sale of steam (Note 34)	4,242,467,491	4,521,232,474
Interest income on service concession	2,107,841,224	2,236,906,585
Construction revenue (Notes 12 and 32)	932,254,227	108,813,951
Revenue from drilling services	726,145,231	624,777,831
	19,143,417,788	18,783,629,546
OPERATING EXPENSES		
Operations and maintenance (Notes 24 and 43)	(4,924,600,921)	(3,069,862,420)
Purchased services and utilities (Note 23)	(1,523,933,710)	(3,037,996,158)
General and administrative (Notes 25, 29 and 43)	(1,106,470,637)	(2,375,691,381)
Construction costs	(803,667,437)	(101,137,594)
Depreciation and amortization	(364,191,569)	(220,109,054)
	(8,722,864,274)	(8,804,796,607)
FINANCIAL INCOME (EXPENSES)		
Interest income - net of final tax (Note 15)	321,333,946	648,736,545
Interest expense (Notes 18, 20, 26 and 43)	(1,796,883,078)	(1,567,038,735)
	(1,475,549,132)	(918,302,190)
OTHER INCOME (CHARGES)		
Foreign exchange gains (losses) - net (Note 28)	(8,968,427,847)	3,900,346,224
Revenue from arbitration award (Notes 16 and 28)	2,067,343,343	-
Derivatives gain - net (Note 40)	384,715,411	56,011,571
Miscellaneous - net (Notes 15 and 29)	159,010,698	(204,412,937)
	(6,357,358,395)	3,751,944,858
INCOME BEFORE INCOME TAX	2,587,645,987	12,812,475,607
PROVISION FOR INCOME TAX (Note 30)	(1,335,505,832)	(4,160,994,421)
NET INCOME	₱1,252,140,155	₱8,651,481,186

See accompanying Notes to Parent Company Financial Statements.



ENERGY DEVELOPMENT (EDC) CORPORATION

(Formerly PNOC Energy Development Corporation)

A Subsidiary of Red Vulcan Holdings Corporation

PARENT COMPANY STATEMENTS OF CHANGES IN EQUITY

	Common Stock	Preferred Stock	Cost of Treasury Stock Held	Additional Paid-in Capital	Accumulated Unrealized Gain on AFS Investments	Retained Earnings		Total
						Appropriated	Unappropriated	
Balance, January 1, 2007	₱15,000,000,000	₱-	₱-	₱6,278,075,648	₱131,462,811	₱1,653,315,043	₱4,311,859,476	₱27,374,712,978
Net income	-	-	-	-	-	-	8,651,481,186	8,651,481,186
Unrealized gain on AFS investments recognized in equity (Note 9)	-	-	-	-	245,024,166	-	-	245,024,166
Unrealized gain on AFS investments removed from equity and recognized in profit and loss (Notes 9 and 29)	-	-	-	-	(7,937,724)	-	-	(7,937,724)
Total recognized income for the year	-	-	-	-	237,086,442	-	8,651,481,186	8,888,567,628
Cash dividends (Note 22)	-	-	-	-	-	-	(1,485,000,000)	(1,485,000,000)
Issuance of preferred shares (Note 22)	-	75,000,000	-	-	-	-	-	75,000,000
Balance, December 31, 2007	₱15,000,000,000	₱75,000,000	₱-	₱6,278,075,648	₱368,549,253	₱1,653,315,043	₱11,478,340,662	₱34,853,280,606
Balance, January 1, 2008	₱15,000,000,000	₱75,000,000	₱-	₱6,278,075,648	₱368,549,253	₱1,653,315,043	₱11,478,340,662	₱34,853,280,606
Net income	-	-	-	-	-	-	1,252,140,155	1,252,140,155
Unrealized loss on AFS investments recognized in equity (Note 9)	-	-	-	-	(291,399,507)	-	-	(291,399,507)
Unrealized gain on AFS investments removed from equity and recognized in profit and loss (Notes 9 and 29)	-	-	-	-	(46,323,392)	-	-	(46,323,392)
Total recognized income for the year	-	-	-	-	(337,722,899)	-	1,252,140,155	914,417,256
Cash dividends (Note 22)	-	-	-	-	-	-	(4,052,999,997)	(4,052,999,997)
Adjustment of related deferred tax liability of properties stated at appraised values and designated as deemed cost (Notes 22 and 30)	-	-	-	-	-	-	(449,433,875)	(449,433,875)
Purchase of treasury stock (Note 22)	-	-	(404,219,068)	-	-	-	-	(404,219,068)
Reversal of appropriations for exploration projects (Note 22)	-	-	-	-	-	(1,653,315,043)	1,653,315,043	-
Balance, December 31, 2008	₱15,000,000,000	₱75,000,000	(₱404,219,068)	₱6,278,075,648	₱30,826,354	₱-	₱9,881,361,988	₱30,861,044,922

See accompanying Notes to Parent Company Financial Statements.



ENERGY DEVELOPMENT (EDC) CORPORATION
(Formerly PNOC Energy Development Corporation)
A Subsidiary of Red Vulcan Holdings Corporation

PARENT COMPANY STATEMENTS OF CASH FLOWS

	Years Ended December 31	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Income before income tax	₱2,587,645,987	₱12,812,475,607
Adjustments for:		
Unrealized foreign exchange losses (gains)	8,396,478,212	(3,044,087,635)
Interest income on service concession	(2,107,841,224)	(2,236,906,585)
Interest expense	1,796,883,078	1,567,038,735
Reversal of allowance for doubtful accounts (Note 25)	(1,116,185,994)	(43,130,239)
Derivatives gain - net (Note 40)	(384,715,411)	(56,011,571)
Depreciation and amortization (Note 11)	382,919,239	260,053,997
Interest income	(321,333,946)	(648,736,545)
Receipt of inventories from power plant contractor (Note 29)	(260,614,700)	-
Provision for retirement and other benefits - net (Notes 21 and 38)	231,125,945	276,236,218
“Day 1” loss on NPC receivable (Note 29)	189,790,628	-
Gain on sale of AFS investments (Note 29)	(46,323,392)	(7,937,724)
Provisions for doubtful accounts (Notes 25)	6,019,400	286,828,060
“Day 1” gain on deferred royalties (Note 29)	-	(39,769,241)
Operating income before working capital changes	9,353,847,822	9,126,053,077
Decrease (increase) in:		
Concession receivable	4,307,827,550	4,307,827,550
Other current assets	(715,420,791)	(292,960,969)
Trade and other receivables	271,300,196	(1,159,796,875)
Parts and supplies inventories	(160,729,905)	24,408,083
Increase (decrease) in:		
Trade and other payables	(939,074,046)	(3,142,127,173)
Royalty fee payable	(738,431,448)	(737,750,976)
Due to a related party	47,213,065	-
Net cash generated from operations	11,426,532,443	8,125,652,717
Income tax paid	(1,713,925,194)	(1,707,623,763)
Interest paid	(1,450,457,836)	(1,137,454,297)
Retirement and other post-retirement benefits paid (Note 38)	(134,153,008)	(160,000,000)
Net cash flows from operating activities (Note 43)	8,127,996,405	5,120,574,657

(Forward)



	Years Ended December 31	
	2008	2007
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of investment in subsidiaries (Note 14)	(₱5,836,311,024)	₱-
Decrease (increase) in:		
Other noncurrent assets	1,114,834,803	733,629,644
AFS investments	298,122,708	164,092,100
Exploration and evaluation assets	264,098,323	461,679,360
Amounts due from a related party (Note 37)	(96,365,150)	-
Additions to intangible assets (Note 12)	(932,254,227)	(108,813,951)
Acquisition of property and equipment (Note 11)	(340,255,615)	(158,166,483)
Interest received	211,511,548	648,736,545
Proceeds from sale of property and equipment	537,691	3,210,009
Net cash flows from (used in) investing activities	(5,316,080,943)	1,744,367,224
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments of:		
Cash dividends (Note 22)	(4,052,999,997)	(1,485,000,000)
Long-term debt	(2,138,874,502)	(9,842,606,061)
Obligations to a power plant contractor	(245,241,580)	(2,806,654,077)
Proceeds from:		
Loan availment (Note 16)	2,000,000,000	-
Issuance of preferred shares (Note 22)	-	75,000,000
Purchase of treasury stock (Note 22)	(404,219,068)	-
Net cash flows used in financing activities (Note 43)	(4,841,335,147)	(14,059,260,138)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,029,419,685)	(7,194,318,257)
EFFECT OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	5,655,565	(7,302,393)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	2,797,581,577	9,999,202,227
CASH AND CASH EQUIVALENTS AT END OF YEAR	₱773,817,457	₱2,797,581,577

See accompanying Notes to Parent Company Financial Statements.



ENERGY DEVELOPMENT (EDC) CORPORATION
(Formerly PNOC Energy Development Corporation)
A Subsidiary of Red Vulcan Holdings Corporation

NOTES TO PARENT COMPANY FINANCIAL STATEMENTS

1. Corporate Information

Energy Development (EDC) Corporation (the “Company” or “EDC”), formerly PNOC Energy Development Corporation, is a company incorporated and registered with the Philippine Securities and Exchange Commission (SEC) on March 5, 1936.

Beginning December 13, 2006, the common shares of EDC are listed and traded on the Philippine Stock Exchange (PSE). Up to November, 2007, EDC was owned and controlled by the Philippine National Oil Company (PNOC), a government-owned and controlled corporation and the PNOC EDC Retirement Fund.

On November 29, 2007, PNOC and PNOC EDC Retirement Fund sold their combined interests in EDC to First Gen Corporation (First Gen), a domestic corporation owned and controlled by First Philippine Holdings Corporation (First Holdings), also a Filipino corporation. First Gen’s interest in EDC, through its wholly owned subsidiary, Red Vulcan Holdings Corporation (Red Vulcan), consists of 6.0 billion common shares and 7.5 billion preferred shares. Control is established through First Gen’s 60% voting interest in EDC. First Holdings owns directly 66.2% of the common shares of First Gen. The ultimate parent of the Company is First Holdings, a publicly-listed entity.

The Company operates twelve geothermal projects in five geothermal service contract areas namely Leyte Geothermal Production Field, Southern Negros Geothermal Production Field, BacMan Geothermal Production Field, Mindanao Geothermal Production Field and Northern Negros Geothermal Production Field under the Geothermal Service Contracts (GSCs) entered into with the Department of Energy (DOE) pursuant to the provisions of Presidential Decree (P.D.) 1442. Geothermal steam produced is sold to the National Power Corporation (NPC) or are fed to the Company and Build-Operate-Transfer (BOT) contractor’s power plant to produce electricity. EDC sells steam and power to NPC under the Steam Sales Agreements (SSAs) and Power Purchase Agreements (PPAs), respectively. EDC also sells electricity to Iloilo Electric Cooperative 1 under the Electricity Sales Agreement. Separately, it also has drilling activities in Papua New Guinea.

On July 22, 2008, the SEC approved the change in the Company’s corporate name. Such resolution was previously approved by the Company’s Board of Directors (BOD) on June 10, 2008.

The registered office address of the Company is Merritt Road, Fort Bonifacio, Taguig City.

The parent company financial statements were reviewed and, recommended for approval by the Audit and Governance Committee on March 30, 2009. The same parent company financial statements were also approved and authorized for issuance by the BOD on March 30, 2009.



2. Basis of Preparation

The accompanying parent company financial statements have been prepared on a historical cost basis, except for derivatives and AFS investments that have been measured at fair value. The parent company financial statements are presented in Philippine peso, the Company's functional currency. All values are rounded to the nearest peso, except when otherwise indicated.

Statement of Compliance

The parent company financial statements of the Company have been prepared in compliance with Philippine Financial Reporting Standards (PFRS) issued by the Financial Reporting Standards Council and adopted by the Philippine SEC.

The Company also prepares and issues consolidated financial statements for the same period as the parent company financial statements prepared and presented in compliance with PFRS. These may be obtained from the SEC. The parent company financial statements are prepared for submission to the SEC and the Bureau of Internal Revenue (BIR).

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year, except for the adoption of the following Philippine Interpretations which became effective beginning January 1, 2008, and an amendment to an existing standard that became effective on July 1, 2008.

- Philippine Interpretation International Financial Reporting Interpretations Committee (IFRIC), "PFRS 2 - Group and Treasury Share Transactions" — This interpretation requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme by the entity even if the entity chooses or is required to buy those equity instruments (e.g., treasury shares) from another party, or the shareholder(s) of the entity provide the equity instruments needed. This interpretation has no material impact on the parent company financial statements.
- Philippine Interpretation IFRIC 14, "Philippine Accounting Standards (PAS) 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" — This interpretation provides guidance on how to assess the limit in PAS 19, "Employee Benefits" on the amount of the surplus that can be recognized as an asset, and how the pension asset or liability may be affected when there is a statutory or contractual minimum funding requirement. This interpretation has no material impact on the parent company financial statements.
- Amendments to PAS 39, "Financial Instruments: Recognition and Measurement," and PFRS 7, "Financial Instruments: Disclosures - Reclassification of Financial Assets" — The amendments to PAS 39 are effective from July 1, 2008 and permit an entity to: (1) reclassify non-derivative financial assets (other than those designated at fair value through profit or loss by the entity upon initial recognition) out of the fair value through profit or loss category if the financial asset is no longer held for the purpose of selling or repurchasing it in the near term in particular circumstances; and (2) transfer from the available-for-sale category to the loans and receivables category a financial asset that would have met the definition of loans and receivables (if the financial asset had not been designated as available-for-sale), if the entity has the intention and ability to hold that financial asset for the foreseeable future. These amendments have no impact on the parent company financial statements since the Company did not reclassify any financial assets.



3. Significant Accounting Judgments and Estimates

The preparation of the Company's parent company financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that could require material adjustments to the carrying amounts of the assets or liabilities in the future.

Judgments

In the process of applying the Company's accounting policies, management has made the following judgments, apart from those involving estimates, which has the most significant effect on the amounts recognized in the parent company financial statements:

Functional Currency. The Company's transactions are denominated or settled in various currencies such as the Philippine peso, US dollar, and Japanese yen. The Company has determined that its functional currency is the Philippine peso, the currency that most faithfully represents the economic substance of the Company's underlying transactions, events and conditions.

Service Concession Arrangements. In applying Philippine Interpretation IFRIC 12, the Company has made a judgment that its service contracts in Tongonan, Leyte; Palinpinon, Negros Oriental; Bacon-Manito in Albay and Sorsogon; and Mt. Apo in North Cotabato qualify under the financial asset model; while its service contract in Northern Negros and the expansion development of Tanawon project in the Bacon-Manito service contract area qualify under the intangible asset model (see Notes 14 and 32).

Deferred Revenue on Stored Energy. Under the Company's addendum agreements with the NPC, the Company has commitment to NPC for certain volume of stored energy that NPC may lift for a specified period, provided that the Company is able to generate such energy over and above the nominated energy for each given year in accordance with the related PPAs. The Company has made a judgment based on historical information that the probability of future liftings by NPC from the stored energy is remote and accordingly has not deferred any portion of the collected revenues. The stored energy commitments, are however disclosed in the notes to the parent company financial statements under the discussion on commitments and contingencies (see Note 41).

Classification of Financial Instruments. On initial recognition, the financial instrument, or its components parts, are classified as either a financial asset, a financial liability or an equity instrument in accordance with the substance of the contractual arrangement and the definition of a financial asset, a financial liability or an equity instrument. The substance of a financial instrument, rather than its legal form, governs its classification in the parent company balance sheet.

In addition, the Company classifies financial assets by evaluating among others, whether the asset is quoted or not in an active market. Included in the evaluation on whether a financial asset is quoted in an active market is the determination on whether quoted prices are readily and regularly available, and whether those prices represent actual and regularly occurring market transactions on an arm's-length basis.



Estimates and Assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of Receivables. The Company maintains an allowance for doubtful accounts at a level that management considers adequate to provide for potential uncollectibility of its trade and other receivables, and its receivables arising from service concession arrangements. The Company evaluates specific balances where management has information that certain amounts may not be collectible. In these cases, the Company uses judgment, based on available facts and circumstances, and based on a review of the factors that affect the collectibility of the accounts including, but not limited to, the age and status of the receivables, collection experience, past loss experience and, in the case of the receivables arising from service concession arrangements, the expected net cash inflows from the concession. The review is made by management on a continuing basis to identify accounts to be provided with allowance. These specific reserves are re-evaluated and adjusted as additional information received affects the amount estimated.

The carrying amounts of current and noncurrent trade and other receivables and receivables arising from service concession arrangements are ₱6,110.80 million and ₱34,695.43 million, respectively, as of December 31, 2008; and ₱5,000.13 million and ₱36,895.42 million, respectively as of December 31, 2007. The total amount of impairment losses recognized in 2008 and 2007 amounted to ₱6.02 million and ₱286.83 million, respectively (see Notes 6, 15, 25 and 40).

In addition to specific allowance against individually significant receivables, the Company also makes a collective impairment allowance against exposures, which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This collective allowance is based on historical default experience.

Estimating Useful Life of Property and Equipment and Intangible Asset Arising from Service Concession Arrangement. The Company estimates the useful life of property and equipment and intangible asset arising from service concession arrangement based on the period over which the asset is expected to be available for use and on the collective assessment of industry practices, internal evaluation and experience with similar arrangements. The estimated useful life is revisited periodically and updated if expectations differ materially from previous estimates. For purposes of determining the estimated useful life of the intangible asset arising from a service concession arrangement, the Company included the renewal period on the basis of the constitutional and contractual provisions and the Company's historical experience of obtaining approvals of such renewals at no significant cost.

There is no change in the estimated useful lives of property and equipment and intangible assets arising from service concession arrangement. The carrying amounts of property and equipment and intangible assets arising from a service concession arrangement are ₱1,137.81 million and ₱9,389.19 million, respectively, as of December 31, 2008; and ₱1,111.02 million and ₱8,738.84 million, respectively, as of December 31, 2007 (see Notes 11 and 12).

Estimating Net Realizable Value of Parts and Supplies Inventories. The Company carries inventories at net realizable value when such value is lower than cost due to damage, physical deterioration, obsolescence, changes in prices levels or other causes. The carrying amounts of



parts and supplies inventories carried at cost, which is lower than net realizable value, as of December 31, 2008 and 2007 amounted to ₱1,561.39 million and ₱1,140.04 million, respectively (see Note 7).

Exploration and Evaluation Assets. Exploration and evaluation costs are capitalized in accordance with PFRS 6, “*Exploration for and Evaluation of Mineral Resources.*” Capitalization of these costs is based, to a certain extent, on management’s judgment of the degree to which the expenditure may be associated with finding specific geothermal reserve. The Company determines impairment of projects based on the technical assessment of its resident scientists in various disciplines or based on management’s decision not to pursue any further commercial development of its exploration projects. At December 31, 2008 and 2007, the carrying amount of capitalized exploration and evaluation costs was ₱999.76 million and ₱1,171.92 million, respectively (see Note 13).

Retirement and Other Post-employment Benefits. The cost of defined benefit retirement plan and other post-retirement medical and life insurance benefits is determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, medical trend rate, mortality and disability rates and employee turnover rates. Due to the long term nature of these plans, such estimates are subject to significant uncertainty. The net retirement benefit liability at December 31, 2008 and 2007 was ₱1,026.39 million and ₱919.83 million, respectively. The detailed information with respect to the Company’s retirement benefits is presented in Note 38 to the parent company financial statements.

Provision for Dismantlement, Removal and Restoration Costs. In determining the amount of provisions for dismantlement, removal and restoration costs, assumptions and estimates are required in relation to the expected cost to dismantle, remove or restore sites and infrastructure when such obligation exists. The Company has made an assessment that such costs are not significant as of December 31, 2008 and 2007.

Provision for Liabilities on Regulatory Assessments. There are pending assessments from various regulatory agencies on the Company. The Company is currently involved in certain regulatory assessments. The Company’s estimate of the probable costs for the resolution of these assessments has been developed in consultation with in-house and outside counsels and is based upon the analysis of the potential outcome. It is possible, however, that future results of operations could be materially affected by changes in the estimates or in the effectiveness of strategies relating to these proceedings. As of December 31, 2008 and 2007, provision for liabilities on these regulatory assessments, included under “Trade and other payables” account, amounted to ₱678.82 million and ₱1,364.76 million, respectively (see Note 16).

Impairment of AFS Investments. The Company classifies certain financial assets as AFS and recognizes movements in their fair value in equity. When the fair value declines, management makes assumptions about the decline in value to determine whether it is an impairment that should be recognized in the parent company statement of income. No impairment losses have been recognized on AFS investments in 2008 and 2007. The total carrying amount of current and noncurrent AFS investments was ₱688.09 million and ₱1,194.00 million as of December 31, 2008 and 2007, respectively (see Note 9).



The Company recognizes impairment losses should there be an objective evidence of impairment as a result of any of the following events that occurred after initial recognition of the asset and such event has an impact on the estimated cash flows of the financial asset that can be reliably estimated:

- a. significant difficulty of the issuer or obligor;
- b. a breach of contract, such as a default or delinquency in interest or principal payments;
- c. the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- d. it is becoming probable that the borrower will enter bankruptcy or other financial reorganization;
- e. the disappearance of an active market for that financial asset because of financial difficulties; or
- f. observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including adverse changes in the payment status of borrowers in the group or national or economic conditions that correlate with defaults on the assets in the group.

In addition to the foregoing events, a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is also being considered by the Company as an objective evidence of impairment. The determination of what is "significant" and "prolonged" requires judgment. The Company considers a decline significant or prolonged whenever it reaches 20% or more and lasts longer than six months, respectively. The Company further evaluates other factors, such as volatility in share price for quoted equities and the discounted cash flows for unquoted equities in determining the amount to be impaired.

Impairment of Non-financial Assets. The Company assesses whether there are any indicators of impairment for all non-financial assets at each reporting date. These non-financial assets [intangible assets arising from service concession arrangements, property and equipment and claim for excess input value-added tax (VAT)] are tested for impairment when there are indicators that the carrying amounts may not be recoverable. Where the collection of tax claim is uncertain based on the assessment of management and the Company's legal counsel, the Company provides an allowance for impairment. When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and discounts such cash flows using the sensitivity analysis of key assumptions to calculate the present value as of the reporting date (see Notes 12 and 40).

The carrying amount of intangible assets arising from service concession arrangements as of December 31, 2008 and 2007 was ₱9,389.19 million and ₱8,738.84 million, respectively (see Note 12). The carrying amount of property and equipment as of December 31, 2008 and 2007 was ₱1,137.81 million and ₱1,111.02 million, respectively (see Note 11). The carrying amount of input VAT as of December 31, 2008 and 2007 was ₱423.00 million and ₱478.39 million, respectively (see Note 15).



Construction Revenue Recognition. The Company's revenue from construction services in relation to its service concession arrangement is recognized using the percentage-of-completion method and measured by reference to the percentage of costs incurred to date to estimated total costs for each contract.

An authority for expenditure is issued to cover the work program for the development of the concession area. When the costs incurred to date exceed the authorized amount, an assessment is conducted to determine the cause of the cost overrun. Cost overruns arising from uncontrollable factors such as oil price, wage increases and changes in technical work programs due to unforeseen geological conditions are capitalized while all other cost overruns are treated as period costs.

Deferred Tax Assets. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the assets can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized. This includes the likely timing and level of future taxable profits together with future tax planning strategies. The carrying value of recognized deferred tax assets amounted to ₱8,187.87 million and ₱6,750.70 million as of December 31, 2008 and 2007, respectively (see Note 30). There are no unrecognized deferred income tax assets as of December 31, 2008 and 2007.

Fair Values of Financial Instruments. The fair values of financial instruments that are not quoted in active markets are determined using valuation techniques. Where valuation techniques are used to determine fair values, fair values are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are reviewed before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices. To the extent practicable, models use only observable data, however areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments (see Note 40).

4. **Summary of Significant Accounting Policies**

Foreign Currency-denominated Transactions

The parent company financial statements are presented in Philippine peso, which is the Company's functional and presentation currency. Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated using the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the parent company statement of income. Nonmonetary items that are measured at historical cost in a foreign currency are translated using the exchange rate as at the date of the transaction. Nonmonetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined.

Parts and Supplies Inventories

Inventories are valued at the lower of cost and net realizable value. Cost includes invoice amount, net of trade and cash discounts. Cost is calculated using the moving-average method. Net realizable value represents the current replacement costs.



Property and Equipment

Property and equipment, except land, is stated at cost less accumulated depreciation and accumulated impairment losses. Such cost includes the cost of replacing part of the property and equipment when that cost is incurred, if the recognition criteria are met. All other repairs and maintenance costs are recognized in the parent company statement of income, as incurred. Land is carried at cost less accumulated net impairment losses, if any.

Depreciation is calculated on a straight-line basis over the economic life of the asset as follows:

Buildings and improvements	5–20 years
Exploration, machinery and equipment	2–10 years
Furniture, fixtures and equipment	3–10 years
Laboratory equipment	5–10 years
Transportation equipment	5 years

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in parent company statement of income in the year the asset is derecognized. The residual values, useful lives and methods of depreciation are reviewed, and adjusted, if appropriate, at each financial year-end.

Fixed assets are recognized based on their significant parts. Each part of an item of property and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately.

Construction in-progress is stated at cost and is not depreciated until such time that the assets are put into operational use.

Noncurrent Asset Held for Sale

An asset is classified as noncurrent asset held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale that should be expected to qualify for recognition as a completed sale within one year from the date of classification, except when there is delay of the sale caused by events or circumstances beyond the Company’s control.

Noncurrent assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell, and depreciation on such assets cease.

Investment Properties

Investment properties are measured initially at cost, including transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met; and excludes the costs of day to day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at cost less accumulated depreciation and any accumulated impairment losses.



An investment property is derecognized when either they have been disposed of or when such is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss on the retirement or disposal of an investment property is recognized in the parent company statement of income in the year of retirement or disposal.

No assets held under operating lease have been classified as investment properties.

Investments in Subsidiaries

The Company's investments in subsidiaries are carried at cost less accumulated impairment losses, if any. Under the cost method, the Company recognizes income from the investment only to the extent that the Company receives distributions from accumulated profits of the subsidiaries arising after the dates of acquisition. Distributions received in excess of such profits are regarded as a recovery of investment and are recognized as a reduction of the cost of the investment.

A subsidiary is an entity in which the Company has control.

Service Concession Arrangements

Public-to-private service concession arrangements where: (a) the grantor controls or regulates what services the Company must provide with the infrastructure, to whom it must provide them, and at what price; and (b) the grantor controls, through ownership, beneficial entitlement or otherwise, any significant residual interest in the infrastructure at the end of the term of the arrangement are accounted for under the provisions of Philippine Interpretation IFRIC 12. Infrastructures used in a public-to-private service concession arrangement for its entire useful life (whole-of-life assets) are within the scope of this interpretation if the conditions in (a) are met.

Philippine Interpretation IFRIC 12 applies to both: (a) infrastructure that the Company constructs or acquires from a third party for the purpose of the service arrangement; and (b) existing infrastructure to which the grantor gives the Company access for the purpose of the service arrangement.

Infrastructures within the scope of this interpretation are not recognized as property and equipment of the Company. Under the terms of contractual arrangements within the scope of interpretation, the Company acts as a service provider. The Company constructs or upgrades infrastructure (construction or upgrade services) used to provide a public service and operates and maintains that infrastructure (operation services) for a specified period of time.

The Company recognizes and measures revenue in accordance with PAS 11, "Construction Contracts," and PAS 18 "Revenues," for the services it performs. If the Company performs more than one service (i.e. construction or upgrade services and operation services) under a single contract or arrangement, consideration received or receivable shall be allocated by reference to the relative fair values of the services delivered, when the amounts are separately identifiable.

When the Company provides construction or upgrade services, the consideration received or receivable by the Company is recognized at its fair value. The Company accounts for revenue and costs relating to construction or upgrade services in accordance with PAS 11. Revenue from construction contract is recognized based on the percentage-of-completion method, measured by reference to the percentage of costs incurred to date to estimated total costs for each contract. The Company accounts for revenue and costs relating to operation services in accordance with PAS 18.



The Company recognizes a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services. The Company recognizes an intangible asset to the extent that it receives a right (a license) to charge users of the public service.

When the Company has contractual obligations it must fulfill as a condition of its license (a) to maintain the infrastructure to a specified level of serviceability or (b) to restore the infrastructure to a specified condition before it is handed over to the grantor at the end of the service arrangement, it recognizes and measures these contractual obligations in accordance with PAS 37, "Provisions, Contingent Liabilities and Contingent Assets," at the best estimate of the expenditure that would be required to settle the present obligation at the balance sheet date.

In accordance with PAS 23, "Borrowing Costs," borrowing costs attributable to the arrangement are recognized as an expense in the period in which they are incurred unless the Company has a contractual right to receive an intangible asset (a right to charge users of the public service). In this case, borrowing costs attributable to the arrangement are capitalized during the construction phase of the arrangement in accordance with the allowed alternative treatment under that standard.

Intangible Assets

Intangible assets pertain mainly to its right to charge users of the public service in connection with the service concession and related arrangements. This is recognized initially at the fair value of the construction services. Following initial recognition, the intangible asset is carried at cost less accumulated amortization and any accumulated impairment losses.

The intangible assets are amortized using the straight-line method over the estimated economic life which is the service concession period, and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method are reviewed at least at each reporting date. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense is recognized in parent company statement of income in the expense category consistent with the function of the intangible asset.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds, if any, and the carrying amount of the asset and are recognized in the parent company statement of income when the asset is derecognized.

Exploration and Evaluation Assets

All costs incurred in the geological and geophysical activities such as costs of topographical, geological and geophysical studies; rights of access to properties to conduct those studies; salaries and other expenses of geologists, geophysical crews, or others conducting those studies are charged to expense in the year such are incurred.

If the results of initial geological and geophysical activities reveal the presence of geothermal resource that will require further exploration and drilling, subsequent exploration and drilling costs are accumulated and deferred under the "Exploration and evaluation assets" account.



These costs include the following:

- a. costs associated with the construction of temporary facilities;
- b. costs of drilling exploratory and exploratory-type stratigraphic test wells, pending determination of whether the wells can produce proved reserves; and,
- c. costs of local administration, finance, general and security services, surface facilities and other local costs in preparing for and supporting the drilling activities, etc. incurred during the drilling of exploratory wells.

If tests conducted on the drilled exploratory wells reveal that these wells cannot produce proved reserves, the capitalized costs are charged to expense except when management decides to use the unproductive wells, for recycling or waste disposal.

Once the technical feasibility and commercial viability of the project to produce proved reserves are established, the exploration and evaluation assets shall be reclassified to either intangible asset or concession receivable at its fair value at the date of reclassification.

Impairment of Non-financial Assets

The Company assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset's recoverable amount. The recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and, its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. When the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples or other available fair value indicators.

Impairment losses of continuing operations are recognized in the parent company statement of income in those expense categories consistent with the function of the impaired asset, except for property previously revalued where the revaluation was taken to equity. In this case, the impairment is also recognized in equity to the extent of any previous revaluation.

For non-financial assets, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the Company makes an estimate of recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. In such instance, the carrying amount of the asset is increased to its recoverable amount. However, that increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the parent company statement of income unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase.



Financial Instruments

Financial instruments are recognized in the parent company balance sheet, when the Company becomes a party to the contractual provisions of the instrument. All regular way purchases and sales of financial assets are recognized on the trade date, which is the date that the Company commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace. Derivatives are also recognized on a trade date basis.

Financial instruments are recognized initially at fair value. Except for financial instruments valued at fair value through profit or loss (FVPL), the initial measurement includes transaction costs. The Company classifies its financial assets into the following categories: financial assets at FVPL, held-to-maturity (HTM) investments, AFS investments, and loans and receivables. For financial liabilities, the Company classifies them into financial liabilities at FVPL and other financial liabilities. The classification depends on the purpose for which the investments were acquired and whether they are quoted in an active market. Management determines the classification of its investments at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, dividends, gains and losses relating to a financial instrument or a component that is a financial liability, are reported as expense or income. Distributions to holders of financial instruments classified as equity are charged directly to equity, net of any related income tax benefits.

Offsetting Financial Instruments. Financial assets and financial liabilities are offset with the net amount reported in the parent company balance sheet if and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented at gross in the parent company balance sheet.

Fair Value. The fair value of financial instruments traded in active markets at the balance sheet date is based on their quoted market price or dealer price quotations without deduction for transaction costs. When current bid and asking prices are not available, the price of the most recent transaction provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction.

For all other financial instruments not traded in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include net present value techniques, comparison to similar instruments for which observable market prices exist, and other relevant valuation models.

“Day 1” Differences. Where the transaction price in a non-active market is different from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Company recognizes the difference between the transaction price and fair value (a “Day 1” difference) in the parent company statement of income unless it qualifies for recognition as some other type of asset. In cases where use is made of data which is not observable, the difference between the transaction price and model value is only recognized in the parent company statement of income when the



inputs become observable or when the instrument is derecognized. For each transaction, the Company determines the appropriate method of recognizing the “Day 1” difference amount.

Financial Assets and Financial Liabilities at FVPL. Financial assets and financial liabilities at FVPL include financial assets held for trading and financial assets designated upon initial recognition as at FVPL.

Financial assets and financial liabilities are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments held for trading are recognized parent company statement of income

Financial assets or financial liabilities may be designated at initial recognition as at FVPL if the following criteria are met: (a) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on them on a different basis; or (b) the assets are part of a group of financial assets, which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (c) the financial instrument contains an embedded derivative that would need to be separately recorded.

Where a contract contains one or more embedded derivatives, the entire hybrid contract may be designated as at FVPL, except where the embedded derivative does not significantly modify the cash flow or it is clear that separation of the embedded derivative is prohibited.

Classified under this category are the Company’s derivative assets and liabilities (see Note 40).

HTM Investments. Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as HTM when the Company has the positive intention and ability to hold to maturity. Where the Company sells other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS investments. After initial measurement, HTM investments are measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are integral parts of the effective interest rate. Gains and losses are recognized in parent company statement of income when the investments are derecognized or impaired, as well as through the amortization process.

The Company has no HTM investments as of December 31, 2008 and 2007.

Loans and Receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are carried at amortized cost using the effective interest method less any allowance for impairment. Gains and losses are recognized in parent company statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables are classified as current assets if maturity is within 12 months from the balance sheet date. Otherwise, these are classified as noncurrent assets.



Classified under loans and receivables are cash and cash equivalents, trade and other receivables, service concession receivable, due from a related party, cash collateral on Principal Collateralized Interest Reduction (PCIR) Bonds and royalty fee chargeable to NPC.

AFS Investments. AFS investments are those non-derivative financial assets that are designated as such or are not classified as financial assets designated at FVPL, HTM investments or loans and receivables. They are purchased and held indefinitely, and may be sold in response to liquidity requirements or changes in market conditions.

AFS investments are initially measured at fair value plus directly attributable transaction costs. After initial measurement, AFS investment are subsequently measured at fair value with unrealized gains and losses being recognized as a separate component of equity until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognized in parent company statement of equity is included in the parent company statement of income for the period. The Company uses the specific identification method in determining the cost of securities sold. Unquoted equity securities are carried at cost, net of impairment.

AFS investments are classified as current if they are expected to be realized within 12 months from the balance sheet date. Otherwise, these are classified as noncurrent assets.

AFS investments include quoted and unquoted investments in government securities, proprietary and equity shares (see Notes 9 and 40).

Other Financial Liabilities. Other financial liabilities, which include trade and other payables, due to related parties, long-term debt, loan payable, obligations to a power plant contractor and royalty fee payable (see Notes 16, 17, 18, 19, 20, 37 and 40) are initially recognized at fair value of the consideration received less directly attributable transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any related issue costs, discount or premium. Gains and losses are recognized in the parent company statement of income when the liabilities are derecognized, as well as through the amortization process.

Derivative Financial Instruments

Derivative instruments, including bifurcated embedded derivatives are initially recognized at fair value on the date that a derivative transaction is entered into or bifurcated, and are subsequently re-measured at fair value. Changes in fair value of derivative instruments not accounted as hedges are recognized immediately in the parent company statement of income. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The Company assesses whether embedded derivatives are required to be separated from the host contracts when the Company first becomes party to the contract. An embedded derivative is separated from the hybrid or combined contract if all the following conditions are met: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the hybrid instrument is not recognized at FVPL.



Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. The Company determines whether a modification to cash flows is significant by considering the extent to which the expected future cash flows associated with the embedded derivative, the host contract or both have changed and whether the change is significant relative to the previously expected cash flows on the contract.

Impairment of Financial Assets

The Company assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets Carried at Amortized Cost. If there is objective evidence that an impairment loss on assets carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate which is the effective interest rate computed at initial recognition. The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognized in the parent company statement of income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date. Any subsequent reversal of an impairment loss is recognized in parent company statement of income.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are derecognized when they are assessed as uncollectible.

AFS Investments. If an AFS investment is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the parent company statement of income, is transferred from equity to the parent company statement of income. Reversals in respect of equity instruments classified as AFS investments are not recognized in the parent company statement of income. Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in the parent company statement of income.

AFS Investments Carried at Cost. If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such unquoted equity instrument, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. The carrying amount of the asset is reduced through the use of an allowance account.



Derecognition of Financial Assets and Liabilities

Financial Asset. A financial asset (or where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognized when:

- the rights to receive cash flows from the asset have expired;
- the Company retains the right to receive cash flows from the asset, but has assumed as obligation to them in full without material delay to a third party under a “pass through” arrangement; or
- the Company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset but has transferred the control of the asset.

When the Company has transferred its rights to receive cash flows from an asset or has entered into a “pass-through” arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Company’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

Financial Liabilities. A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the parent company statement of income.

Cash and Cash Equivalents

Cash and cash equivalents in the parent company balance sheet comprise cash in banks and on hand and short-term deposits with an original maturity of three months or less and that are subject to insignificant risk of changes in value.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in profit or loss, net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as finance cost.



Treasury Stock

Acquisition of treasury shares by the Company is recorded at purchase cost and shown as a deduction in the equity section of the parent company balance sheet. Upon reissuance of treasury shares, the “Cost of treasury stock held” account is credited at cost. The excess of proceeds from reissuance over the cost of treasury shares is credited to the “Additional paid-in capital” account. The excess of cost of treasury shares over the proceeds from reissuance is debited to the “Additional paid-in capital” account but only to the extent of previously set-up additional paid-in capital for the same class of stock. Otherwise, this is debited against the “Retained earnings” account.

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

Company as a Lessee. Operating lease payments are recognized as expense in the parent company statement of income on a straight-line basis over the lease term.

Company as a Lessor. Leases where the Company does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same bases as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

Revenue Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable, excluding discounts, rebates, and other sales taxes or duty. The following specific recognition criteria must also be met before revenue is recognized:

Revenue from Sale of Electricity and Steam. (For service contracts qualifying under the intangible asset model and for other revenue streams for the financial asset model of service concession arrangements).

Sale of electricity is consummated whenever the electricity generated by the Company is transmitted through the transmission line designated by the buyer, for a consideration. Sale of steam is recognized when the steam generated by the Company or its by-product passes to the flowmeters installed at the interface point for conversion by the buyer into power. Revenues from sale of electricity and steam are based on sales price, net of the portion of the billings representing collection of concession receivable and related interest charges.

Construction Revenue. Construction revenue is recognized by reference to the stage of completion of the contract activity at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately.

Revenue from Drilling Services. Revenue is recognized as drilling services are rendered.



Interest Income. Revenue is recognized as interest accrues, using the effective interest rate, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

Retirement and Other Post-retirement Benefits

The Company maintains a funded, non-contributory defined benefit retirement plan. The Company also provides post retirement medical and life insurance benefits which are unfunded. The cost of providing benefits under the defined benefit plan is determined using the projected unit credit method. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded 10% of the higher of the defined benefit obligations and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plan.

Past service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested. If the benefits are already vested immediately following the introduction of, or changes to, the retirement plan, past service cost is recognized immediately. The defined benefit asset or liability comprises the present value of the defined benefit obligation less past service cost not yet recognized and less the fair value of plan assets out of which the obligations are to be settled directly. The value of any asset is restricted to the sum of any past service cost not yet recognized and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are added to the cost of the assets, until such time that the assets are substantially ready for their intended use or sale, which necessarily take a substantial period of time. Income earned on temporary investment of specific borrowings, pending the expenditure on qualifying assets, is deducted from the borrowing costs eligible for capitalization. All other borrowing costs are recognized in the parent company statement of income in the period in which they are incurred.

Taxes

Current Tax. Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authority. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted as at the balance sheet date.

Current tax relating to items recognized directly in equity is recognized in equity and not in the parent company statement of income.

Deferred Tax. Deferred tax is provided using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and



- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, carryforward unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward benefits of unused tax credits and unused tax losses can be utilized except:

- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted as at the balance sheet date.

Deferred tax relating to items recognized directly in equity is recognized in equity and not in profit or loss.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Value-Added Tax. Revenues, expenses and assets are recognized, net of the amount of VAT except:

- where the VAT incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the VAT is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables that are stated with the amount of VAT included.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the parent company balance sheet.



Contingencies

Contingent liabilities are not recognized in the parent company financial statements. These are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the parent company financial statements but disclosed when an inflow of resources is probable.

Events after the Balance Sheet Date

Post-year-end events that provide additional information about the Company's position at the balance sheet date (adjusting events) are reflected in the parent company financial statements. Post-year-end events that are not adjusting events are disclosed in the notes to the parent company financial statements, when material.

Future Changes in Accounting Policies

The Company will adopt the following standards and interpretations enumerated below when these become effective and, as they are applicable. Except as otherwise indicated, the Company does not expect the adoption of these new and amended PFRS and Philippine Interpretations to have significant impact on its parent company financial statements.

Effective in 2009

- PFRS 1, "First-time Adoption of Philippine Financial Reporting Standards - Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate"

The amended PFRS 1 allows an entity, in its separate financial statements, to determine the cost of investments in subsidiaries, jointly controlled entities or associates (in its opening PFRS financial statements) as one of the following amounts: (a) cost determined in accordance with PAS 27; (b) at the fair value of the investment at the date of transition to PFRS, determined in accordance with PAS 39; or (c) previous carrying amount (as determined under generally accepted accounting principles) of the investment at the date of transition to PFRS.

- PFRS 2, "Share-based Payment - Vesting Condition and Cancellations"

PFRS 2 has been revised to clarify the definition of a vesting condition and prescribes the treatment for an award that is effectively cancelled. It defines a vesting condition as a condition that includes an explicit or implicit requirement to provide services. It further requires non-vesting conditions to be treated in a similar fashion to market conditions. Failure to satisfy a non-vesting condition that is within the control of either the entity or the counterparty is accounted for as cancellation. However, failure to satisfy a non-vesting condition that is beyond the control of either party does not give rise to a cancellation.

- PFRS 8, "Operating Segments"

PFRS 8 will replace PAS 14, "Segment Reporting," and adopts a full management approach to identifying, measuring and disclosing the results of an entity's operating segments. The information reported would be that which management uses internally for evaluating the performance of operating segments and allocating resources to those segments. Such information may be different from that reported in the balance sheet and statement of income and the Company will provide explanations and reconciliations of the differences. This



standard is only applicable to an entity that has debt or equity instruments that are traded in a public market or that files (or is in the process of filing) its financial statements with a securities commission or similar party.

- Amendments to PAS 1, “Presentation of Financial Statements”

These amendments introduce a new statement of comprehensive income that combines all items of income and expenses recognized in the profit or loss together with “other comprehensive income”. Entities may choose to present all items in one statement, or to present two linked statements, a separate statement of income and a statement of comprehensive income. These amendments also prescribe additional requirements in the presentation of the balance sheet and owner’s equity as well as additional disclosures to be included in the financial statements.

- PAS 23, “Borrowing Costs”

PAS 23 has been revised to require capitalization of borrowing costs when such costs relate to a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

- Amendments to PAS 27, “Consolidated and Separate Financial Statements - Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate”

These amendments prescribe changes in respect of the holding companies’ separate financial statements including (a) the deletion of ‘cost method’, making the distinction between pre- and post-acquisition profits no longer required; and (b) in cases of reorganizations where a new parent is inserted above an existing parent of the group (subject to meeting specific requirements), the cost of the subsidiary is the previous carrying amount of its share of equity items in the subsidiary rather than its fair value. All dividends will be recognized in profit or loss. However, the payment of such dividends requires the entity to consider whether there is an indicator of impairment.

- Amendment to PAS 32, “Financial Instruments: Presentation and PAS 1 Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation”

These amendments specify, among others, that puttable financial instruments will be classified as equity if they have all of the following specified features: (a) the instrument entitles the holder to require the entity to repurchase or redeem the instrument (either on an ongoing basis or on liquidation) for a pro rata share of the entity’s net assets; (b) the instrument is in the most subordinate class of instruments, with no priority over other claims to the assets of the entity on liquidation; (c) all instruments in the subordinate class have identical features; (d) the instrument does not include any contractual obligation to pay cash or financial assets other than the holder’s right to a pro rata share of the entity’s net assets; and (e) the total expected cash flows attributable to the instrument over its life are based substantially on the profit or loss, a change in recognized net assets, or a change in the fair value of the recognized and unrecognized net assets of the entity over the life of the instrument.



- Philippine Interpretation IFRIC 13, “Customer Loyalty Programmes,” effective for annual periods beginning on or after July 1, 2008

IFRIC 13 requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted and therefore part of the fair value of the consideration received is allocated to the award credits and deferred over the period that the award credits are fulfilled.

- Philippine Interpretation IFRIC 16, “Hedges of a Net Investment in a Foreign Operation”

IFRIC 16 provides guidance on identifying foreign currency risks that qualify for hedge accounting in the hedge of net investment; where within the group the hedging instrument can be held in the hedge of a net investment; and how an entity should determine the amount of foreign currency gains or losses, relating to both the net investment and the hedging instrument, to be recycled on disposal of the net investment.

Improvements to PFRSs. In May 2008, the International Accounting Standards Board issued its first omnibus of amendments to certain standards, primarily with a view to removing inconsistencies and clarifying wording. There are separate transitional provisions for each standard.

- PAS 1, “Presentation of Financial Statements”

Assets and liabilities classified as held for trading are not automatically classified as current in the balance sheet.

- PAS 16, “Property, Plant and Equipment”

The amendment replaces the term “net selling price” with “fair value less costs to sell,” to be consistent with PFRS 5, “Noncurrent Assets Held for Sale and Discontinued Operations and PAS 36, Impairment of Asset.”

Items of property, plant and equipment held for rental that are routinely sold in the ordinary course of business after rental, are transferred to inventory when rental ceases and they are held for sale. Proceeds of such sales are subsequently shown as revenue. Cash payments on initial recognition of such items, the cash receipts from rents and subsequent sales are all shown as cash flows from operating activities.

- PAS 19, “Employee Benefits”

Revises the definition of “past service costs” to include reductions in benefits related to past services “negative past service costs” and to exclude reductions in benefits related to future services that arise from plan amendments. Amendments to plans that result in a reduction in benefits related to future services are accounted for as a curtailment.

Revises the definition of “return on plan assets” to exclude plan administration costs if they have already been included in the actuarial assumptions used to measure the defined benefit obligation.



Revises the definition of “short-term” and “other long-term” employee benefits to focus on the point in time at which the liability is due to be settled.

Deletes the reference to the recognition of contingent liabilities to ensure consistency with PAS 37, “Provisions, Contingent Liabilities and Contingent Assets.”

- PAS 20, “Accounting for Government Grants and Disclosures of Government Assistance”

Loans granted with no or low interest rates will not be exempt from the requirement to impute interest. The difference between the amount received and the discounted amount is accounted for as a government grant.

- PAS 23, “Borrowing Costs”

Revises the definition of borrowing costs to consolidate the types of items that are considered components of “borrowing costs,” i.e., components of the interest expense calculated using the effective interest method.

- PAS 28, “Investment in Associates”

If an associate is accounted for at fair value in accordance with PAS 39, only the requirement of PAS 28 to disclose the nature and extent of any significant restrictions on the ability of the associate to transfer funds to the entity in the form of cash or repayment of loans will apply.

An investment in an associate is a single asset for the purpose of conducting the impairment test. Therefore, any impairment test is not separately allocated to the goodwill included in the investment balance.

- PAS 29, “Financial Reporting in Hyperinflationary Economies”

The improvement to PAS 29 revises the reference to the exception that assets and liabilities should be measured at historical cost, such that it notes property, plant and equipment as being an example, rather than implying that it is a definitive list.

- PAS 31, “Interest in Joint Ventures”

If a joint venture is accounted for at fair value, in accordance with PAS 39, only the requirements of PAS 31 to disclose the commitments of the venturer and the joint venture, as well as summary financial information about the assets, liabilities, income and expense will apply.

- PAS 36, “Impairment of Assets”

When discounted cash flows are used to estimate “fair value less cost to sell,” additional disclosure is required about the discount rate, consistent with disclosures required when the discounted cash flows are used to estimate “value in use”.



- PAS 38, “Intangible Assets”

Expenditure on advertising and promotional activities is recognized as an expense when the Company either has the right to access the goods or has received the services. Advertising and promotional activities now specifically include mail order catalogues.

It also deletes references to “there being rarely”, if ever, persuasive evidence to support an amortization method for finite life intangible assets that results in a lower amount of accumulated amortization than under the straight-line method, thereby effectively allowing the use of the unit-of-production method.

- PAS 39, “Financial Instruments: Recognition and Measurement”

Changes in circumstances relating to derivatives - specifically derivatives designated or de-designated as hedging instruments after initial recognition - are not reclassifications.

When financial assets are reclassified as a result of an insurance company changing its accounting policy in accordance with paragraph 45 of PFRS 4, “Insurance Contracts,” this is a change in circumstance, not a reclassification.

It further removes the reference to a “segment” when determining whether an instrument qualifies as a hedge.

It also requires the use of revised effective interest rate (rather than the original effective interest rate) when re-measuring a debt instrument on the cessation of fair value hedge accounting.

- PAS 40, “Investment Properties”

Improvement on PAS 40 revises the scope (and the scope of PAS 16) to include property that is being constructed or developed for future use as an investment property. Where an entity is unable to determine the fair value of an investment property under construction, but expects to be able to determine its fair value on completion, the investment under construction will be measured at cost until such time as fair value can be determined or construction is complete.

- PAS 41, “Agriculture”

The improvement to PAS 41 removes:

- a. the reference to the use of a pre-tax discount rate to determine fair value, thereby allowing use of either a pre-tax or post-tax discount rate depending on the valuation methodology used; and
- b. the prohibition to take into account cash flows resulting from any additional transformations when estimating fair value. Instead, cash flows that are expected to be generated in the “most relevant market” are taken into account.



Effective in 2010

- Revised PFRS 3, “Business Combinations” and PAS 27, “Consolidated and Separate Financial Statements”

The revised PFRS 3 introduces a number of changes in the accounting for business combinations that will impact the amount of goodwill recognized, the reported results in the period that an acquisition occurs, and future reported results. The revised PAS 27 requires, among others, that (a) change in ownership interests of a subsidiary (that do not result in loss of control) will be accounted for as an equity transaction and will have no impact on goodwill nor will it give rise to a gain or loss; (b) losses incurred by the subsidiary will be allocated between the controlling and non-controlling interests (previously referred to as “minority interests”); even if the losses exceed the non-controlling equity investment in the subsidiary; and (c) on loss of control of a subsidiary, any retained interest will be remeasured to fair value and this will impact the gain or loss recognized on disposal. The changes introduced by the revised PFRS 3 must be applied prospectively and will affect future acquisitions and transactions with non-controlling interests. Revised PAS 27 must be applied retrospectively subject to certain exceptions.

- Amendment to PAS 39, “Financial Instruments: Recognition and Measurement - Eligible Hedged Items”

The amendment to PAS 39 will be effective on July 1, 2009, which addresses only the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situations. The amendment clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item.

- PFRS 5, “Noncurrent Assets Held for Sale and Discontinued Operations”

When a subsidiary is held for sale, all of its assets and liabilities will be classified as held for sale under PFRS 5, even when the entity retains a non-controlling interest in the subsidiary after the sale.

Effective in 2012

- Philippine Interpretation IFRIC 15, “Agreement for Construction of Real Estate”

This interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. This interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under PAS 11, “Construction Contracts”, or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and reward of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion.



5. Cash and Cash Equivalents

	2008	2007
Cash on hand and in banks	₱9,644,200	₱16,353,040
Cash equivalents	764,173,257	2,781,228,537
	₱773,817,457	₱2,797,581,577

Cash in banks earn interest at the respective bank deposit rates. Cash equivalents consist of money market placements which are made for varying periods of up to three months depending on the immediate cash requirements of the Company. Total interest earned net of final tax amounted to ₱209.74 million in 2008 and ₱303.81 million in 2007.

6. Trade and Other Receivables

	2008	2007
Trade (see Note 15)	₱4,650,490,516	₱4,674,443,525
Others:		
Claims receivable	293,146,429	7,577,854
Non-trade accounts receivable	232,317,043	517,499,843
Loans and notes receivables	60,350,973	54,453,890
Employee receivables	30,096,534	26,393,358
Advances to employees	26,724,217	22,531,712
Total other receivables	642,635,196	628,456,657
	5,293,125,712	5,302,900,182
Less allowance for doubtful accounts	2,182,181	377,218,598
	₱5,290,943,531	₱4,925,681,584

Trade receivables are noninterest-bearing and are generally collectible in 30 days.

The rollforward analysis of allowance for doubtful accounts, which pertains to trade receivables, is presented below:

	2008	2007
Balance at beginning of year	₱377,218,598	₱1,641,726,228
Recoveries (see Notes 25 and 28)	(377,218,598)	(17,273,164)
Provisions for doubtful accounts (see Notes 25 and 28)	2,182,181	285,482,600
Reclassification to other noncurrent assets (see Note 15)	-	(950,145,606)
Write-off	-	(582,571,460)
Balance at end of year	₱2,182,181	₱377,218,598

The recoveries shown in the table above came from the implementation of the arbitral decision that was arrived at in March 2008 by a third-party arbiter, details of which are disclosed in Notes 15 and 28 to the parent company financial statements.



7. Parts and Supplies Inventories

	2008	2007
Drilling tubular products and equipment spares	P559,877,157	P497,928,721
Power plant spares	369,183,232	110,717,107
Pump, production/steam gathering system, steam turbine, valves and valve spares	195,984,369	175,536,519
Chemical, chemical products, gases and catalyst	84,651,321	83,394,594
Heavy equipment spares	74,592,591	83,477,931
Electrical, cable, wire product and compressor spares	41,414,462	53,259,044
Measuring instruments, indicators and tools, safety equipment and supplies	34,023,490	33,791,322
Automotive, mechanical, bearing, seals, v-belt, gasket, tires and batteries	31,713,381	29,441,624
Construction and hardware supplies, stationeries and office supplies, hoses, communication and other spares and supplies	3,290,577	2,852,740
Total	1,394,730,580	1,070,399,602
In-transit	151,054,481	64,567,422
Materials and supplies for disposal	15,603,606	5,077,038
	P1,561,388,667	P1,140,044,062

Inventories in-transit include items not yet received but ownership or title to the goods have already passed to the Company.

The inventories are carried at cost, which is lower than net realizable value as of December 31, 2008 and 2007. The amount of inventory charged to expense amounted to P1,127.18 million in 2008 and P682.03 million in 2007 (see Notes 24 and 25).

8. Other Current Assets

	2008	2007
Advances to contractors (see Note 37)	P268,678,263	P23,037,464
Prepaid expenses	206,109,836	125,589,232
Royalty fee chargeable to NPC (see Note 15)	122,018,657	-
Cash collateral on PCIR Bonds (see Notes 15 and 20)	3,519,226	-
Tax credit certificates	-	386,956,078
	P600,325,982	P535,582,774

In 2008, advances to contractors include a 20% advance payment amounting to P198.00 million for the purchase of a new drilling rig expected to be delivered to the Company in November 2009.

Prepaid expenses comprise mainly of creditable withholding tax certificates issued by NPC and Lihir Gold Ltd. for the drilling services in Lihir, Papua New Guinea.



Royalty fees chargeable to NPC are unpaid royalty fees of Palinpinon I due to the DOE and the Local Government Units (LGUs), which NPC reimburses the Company upon its presentation of official receipts of the actual payments. This arrangement will be effective until the privatization of NPC's Palinpinon power plants scheduled in 2009. In 2008, this account was reclassified from "Other noncurrent assets" account to "Other current assets" account since this is expected to be reimbursed from NPC in 2009 (see Note 15).

9. AFS Investments

	2008	2007
Current AFS investments -		
Quoted government debt securities	₱674,494,128	₱1,177,589,987
Noncurrent AFS investments:		
Quoted equity securities (see Note 15)	₱13,522,688	₱16,336,106
Unquoted equity securities (see Note 15)	74,550	74,550
	₱13,597,238	₱16,410,656

The current AFS investments consist of government debt securities, specifically Republic of the Philippines (ROP) bonds with maturities between 2013 to 2016 and 2009 to 2024 in 2008 and 2007, respectively. Such bonds were acquired at a discount and bear interest between 7.25% to 9.00% in 2008 and 2007.

The noncurrent AFS investments amounting to ₱13.60 million and ₱16.41 million as of December 31, 2008 and 2007, respectively, are included under "Other Noncurrent Assets - others" account in the parent company balance sheets (see Note 15).

The movements of gains or losses related to the foregoing investments are presented as a separate component of equity on AFS investments with details as follows:

	2008	2007
Net accumulated unrealized gain on AFS investments at beginning of year	₱368,549,253	₱131,462,811
Changes in fair value recognized in equity	(291,399,507)	245,024,166
Net unrealized gain removed from equity and recognized in profit or loss (see Note 29)	(46,323,392)	(7,937,724)
Net accumulated unrealized gain on AFS investments at end of year	₱30,826,354	₱368,549,253

Changes in equity refer to unrealized gains and losses recognized during the period brought about by the temporary increase or decrease in the fair value of the equity instruments. The net gain derecognized in equity and recognized in parent company statement of income pertains to the disposal of equity securities during the year.

The Company records unrealized gain and loss on AFS investments directly in equity, presented under the "Accumulated unrealized gain on AFS investments" account. If the investment is sold or assessed to be impaired, the cumulative losses or gains recognized in equity is transferred to the parent company statement of income.



10. **Noncurrent Assets Held for Sale**

	2008	2007
Land	₱1,669,587,000	₱1,672,516,100
Buildings, improvements and equipment	128,000,000	-
	₱1,797,587,000	₱1,672,516,100

This account consists of the 29,291 square meter land and buildings together with the improvements and immovable equipment owned by the Company in Fort Bonifacio previously presented under property and equipment and investment property accounts.

The properties were classified as noncurrent assets held for sale in accordance with the Company's Board Resolution No. 115 series of 2007 dated November 13, 2007, whereby the Company shall sell these properties to PNOC. Management expects such transaction to be concluded in 2009 upon issuance by the Office of the Government Corporate Counsel of an opinion covering the land swap among EDC, DOE and Bases Conversion Development Authority.

There are no liabilities directly associated with the noncurrent assets held for sale.



11. Property and Equipment

2008									
	Buildings and Improvement	Exploration, Machinery and Equipment	Transportation Equipment	Furniture, Fixtures and Equipment	Laboratory Equipment	Land	Construction in-Progress	Major Spares and Others	Total
Cost:									
Balance - January 1	P348,605,868	P1,167,410,125	P50,851,751	P171,502,531	P49,244,740	P328,306,933	P175,633,662	P27,737,419	P2,319,293,029
Additions	2,747,823	22,908,653	3,168,464	22,518,294	6,613,656	1,705,540	264,803,610	15,789,575	340,255,615
Retirements/Write-Off	(792,413)	(1,183,153)	(87,290)	(8,602,616)	(1,171,802)	(144,550)	-	(33,571)	(12,015,395)
Reclassifications (see Note 10)	(276,486,487)	5,380,600	(969,999)	16,982,821	4,213,557	2,929,100	(108,449,699)	(22,405,029)	(378,805,136)
Balance - December 31	74,074,791	1,194,516,225	52,962,926	202,401,030	58,900,151	332,797,023	331,987,573	21,088,394	2,268,728,113
Accumulated depreciation:									
Balance - January 1	208,680,286	786,560,321	41,934,765	130,694,118	40,403,183	-	-	-	1,208,272,673
Depreciation	220,861	73,467,111	4,708,345	18,183,160	4,441,799	-	-	-	101,021,276
Retirements/Write-Off	(611,841)	(1,136,659)	(87,289)	(8,470,136)	(1,171,779)	-	-	-	(11,477,704)
Reclassifications (see Note 10)	(166,031,920)	(4,421,102)	(502,748)	2,308,520	1,744,713	-	-	-	(166,902,537)
Balance - December 31	42,257,386	854,469,671	46,053,073	142,715,662	45,417,916	-	-	-	1,130,913,708
Net book value	P31,817,405	P340,046,554	P6,909,853	P59,685,368	P13,482,235	P332,797,023	P331,987,573	P21,088,394	P1,137,814,405
2007									
	Buildings and Improvement	Exploration, Machinery and Equipment	Transportation Equipment	Furniture, Fixtures and Equipment	Laboratory Equipment	Land	Construction in-Progress	Major Spares and Others	Total
Cost:									
Balance - January 1	P348,605,868	P1,158,038,095	P49,324,273	P162,660,784	P46,070,652	P1,727,641,708	P50,735,205	P31,503,835	P3,574,580,420
Additions	-	-	-	-	-	235,471	149,324,599	8,606,413	158,166,483
Retirements/Write-Off	-	(614,210)	(2,508,632)	(6,789,335)	(409,104)	-	-	(2,866,469)	(13,187,750)
Reclassifications/Adjustments	-	9,986,240	4,036,110	15,631,082	3,583,192	(1,399,570,246)	(24,426,142)	(9,506,360)	(1,400,266,124)
Balance - December 31	348,605,868	1,167,410,125	50,851,751	171,502,531	49,244,740	328,306,933	175,633,662	27,737,419	2,319,293,029
Accumulated depreciation:									
Balance - January 1	188,626,885	705,696,155	39,087,595	135,287,405	36,662,701	-	-	-	1,105,360,741
Depreciation	20,053,401	52,395,147	5,122,900	14,066,308	3,268,554	-	-	-	94,906,310
Retirements/Write-Off	-	(615,794)	(2,275,730)	(6,677,119)	(409,098)	-	-	-	(9,977,741)
Reclassifications (see Note 10)	-	29,084,813	-	(11,982,476)	881,026	-	-	-	17,983,363
Balance - December 31	208,680,286	786,560,321	41,934,765	130,694,118	40,403,183	-	-	-	1,208,272,673
Net book value	P139,925,582	P380,849,804	P8,916,986	P40,808,413	P8,841,557	P328,306,933	P175,633,662	P27,737,419	P1,111,020,356



The net book value of assets retired/written off amounted to ₱0.54 million and ₱3.21 million, net of accumulated depreciation of ₱11.48 million and ₱9.98 million as of December 31, 2008 and 2007, respectively.

Management believes that, based on the assessment performed, none of the Company's property and equipment are impaired.

Details of depreciation and amortization charges are shown below:

	2008	2007
Property and equipment	₱101,021,276	₱94,906,311
Intangible assets (see Note 12)	281,897,963	164,294,068
Investment property	-	853,618
	₱382,919,239	₱260,053,997

12. Intangible Assets

	2008	2007
Cost:		
Balance at the beginning of year	₱8,903,130,895	₱8,794,316,944
Additions (see Notes 13 and 32)	932,254,227	108,813,951
Balance at the end of year	9,835,385,122	8,903,130,895
Accumulated amortization:		
Balance at the beginning of year	(164,294,068)	-
Amortization (see Note 11)	(281,897,963)	(164,294,068)
Balance at the end of year	(446,192,031)	(164,294,068)
Carrying amount	₱9,389,193,091	₱8,738,836,827

Amortization expense charged to operations amounted to ₱281.90 million in 2008 and ₱164.29 million in 2007.

Additions to intangible assets arising from service concessions during 2008 pertain to the construction of the Tanawon Geothermal Project (₱250.91 million) and the start of the steam field expansion development of Northern Negros Geothermal Project's (NNGP) buffer zone (₱681.34 million).

The intangible asset of the NNGP is being amortized over the term of the related GSC (see Notes 4 and 32). The remaining amortization period of NNGP is 30 years as of December 31, 2008. With respect to the Tanawon Project, the reckoning date shall be from project completion date through 2031 consistent with the terms of the final extension of the service contract for Bacon-Manito area.

Management believes that based on the assessment performed, the intangible assets are not impaired.



The recoverable amount of the NNGP, which is considered as a cash generating unit, has been determined based on a value-in-use calculation using the expected cash flow projections.

The five-year cash flow projections of the Company used for impairment testing were based on the budget approved by the Company's BOD on December 16, 2008. The projected cash flows considered published forecast of inflation and exchange rates. The Company uses the Perpetuity Growth Model to determine the terminal value, which accounts for the value of free cash flows that continue in perpetuity beyond the five-year-period projection, growing at an assumed constant rate. The assumed growth rate was 5%, which does not exceed the average real gross domestic growth rate of 5.66% and the average annual demand growth of 6% for the Visayas power industry market where the unit operates. The pre-tax discount rate used was 9.9% based on NNGP's weighted average cost of capital.

Based on the foregoing, the recoverable amount of NNGP is higher than its carrying amount of ₱9.14 billion.

NNGP, which is on temporary shutdown since June 2008, is expected to resume operation in the second quarter of 2009.

13. Exploration and Evaluation Assets

	2008	2007
Balance at beginning of year	₱1,171,922,174	₱1,614,922,295
Additions	561,873,053	84,962,253
Transfers to financial assets/intangible asset	(734,037,968)	(527,962,374)
Balance at end of year	₱999,757,259	₱1,171,922,174

Deferred exploration and evaluation costs are all intangible and pertain to the following project areas:

	2008	2007
Cabalian, Southern Leyte	₱567,811,104	₱558,363,775
Mindanao	276,639,012	76,080,913
Ilocos Norte	63,967,545	48,427,707
Dauin, Southern Negros	48,648,779	-
Bacman-Rangas/Kayabon	35,582,535	-
Northern Negros	-	445,872,148
Bacman-Tanawon	-	37,315,026
Other areas	7,108,284	5,862,605
	₱999,757,259	₱1,171,922,174

In 2008, the exploration projects in Northern Negros and Bacman-Tanawon are carried at zero balance since the accumulated costs have been transferred and reclassified to "Intangible Assets" account (see Note 12) consistent with the Company's accounting policy for development projects.



14. Investments in Subsidiaries

The Company's investments in the following subsidiaries are carried at cost. No impairment loss was recognized in 2008.

Incorporation of First Luzon Geothermal Energy Corporation (FL Geothermal)

The Company invested ₱0.25 million in FL Geothermal, a wholly owned subsidiary of the Company. FL Geothermal is a special purpose company incorporated on April 9, 2008 to participate in the bid for another local power plant. The bid was won by and awarded to another local entity. Thereafter, there has been no business activity yet as far as FL Geothermal is concerned.

Acquisition of First Gen Hydro Power Corporation (FG Hydro)

On October 16, 2008, the Company, First Gen and FG Hydro entered into a Share Purchase and Investment Agreement (SPIA), whereby EDC shall own 60% of the outstanding equity of FG Hydro, then a wholly owned subsidiary of First Gen. The acquisition by EDC was through a combination of primary issuance by FG Hydro of up to 17% interest and sale of secondary shares by First Gen of up to 43% interest in FG Hydro. FG Hydro and EDC are subsidiaries of First Gen and therefore under common control of First Gen. FG Hydro operates the 112MW Pantabangan-Masiway hydroelectric power plants located in Nueva Ecija, Philippines.

Consistent with the SPIA, on October 20, 2008, FG Hydro issued 101,281,942 shares of its common stocks to EDC for a total subscription price of ₱1,648.03 million. Thereafter, on November 17, 2008, EDC acquired 249,287,223 common shares held by First Gen for US\$85.22 million (₱4,114.59 million). Total direct cost related to the transaction amounted to ₱73.44 million. The total cost of the acquisition of FG Hydro amounted to ₱5,836.06 million. The acquisition was funded through internally generated cash flows.

15. Other Noncurrent Assets

	2008	2007
Long-term receivables	₱2,780,884,962	₱2,981,776,511
Input VAT	423,004,135	478,391,948
Special deposits and funds	37,171,098	36,785,822
Prepaid expenses	22,359,991	764,352,330
Royalty fee chargeable to NPC (see Note 8)	-	464,520,286
Investment property	-	5,121,709
Cash collateral on PCIR Bonds (see Notes 8 and 20)	-	3,066,807
Others (see Note 9)	63,589,801	25,062,861
	3,327,009,987	4,759,078,274
Less allowance for doubtful accounts	1,961,023,573	2,907,331,961
	₱1,365,986,414	₱1,851,746,313



Long-term receivables

The composition of long-term receivables is as follows:

	2008	2007
Claims for VAT refund	₱1,894,719,994	₱1,894,719,994
NPC accounts and other receivables	886,164,968	1,087,056,517
	₱2,780,884,962	₱2,981,776,511

Claims for VAT Refund

The BIR related claims pertain to the Company's claims for refund of input VAT on BOT fees amounting to ₱1,894.72 million which was initially denied at the BIR regional level on July 2, 2002. Subsequently, on September 2, 2002, the Company filed a letter for reconsideration with the Revenue District Office (RDO) 50. RDO 50 endorsed the request for reconsideration to the BIR Head Office legal department and the review of the claims is still on-going.

NPC accounts and other receivables

As discussed in Note 28, on April 24, 2008, an arbitral settlement award was concluded with NPC liable to the Company for ₱2,894.93 million covering the long-standing issue related to the SSAs and PPAs of EDC with NPC. A payment schedule as agreed upon among the parties call for NPC's settlement of the arbitral award over three years at zero interest. Consistent with the provisions of PAS 39, the net amount of receivables was presented at fair value, discounted using 7.99% to 8.11%. As of the award date, the difference between the nominal value and fair value of ₱189.79 million was recognized as a "Day 1" loss and presented under the "Miscellaneous-net" account in the 2008 parent company statement of income. Subsequent to the initial recognition, the receivable is accreted to its maturity value based on its effective interest rate. The accretion recognized in 2008 amounted to ₱108.11 million and is included under "Interest income" account in the 2008 parent company statement of income.

The movement of the NPC receivables covered by the arbitration is as follows:

	2008
Arbitration settlement award	₱2,894,930,272
Collection during the year	(1,000,000,000)
	1,894,930,272
"Day 1" loss recognized	(189,790,628)
Accretion	108,113,195
	(81,677,433)
Balance as of December 31, 2008	1,813,252,839
Current portion of receivables (see Note 6)	993,391,450
Noncurrent portion of receivables	₱819,861,389



Special deposits and funds

The special deposits and funds mainly consisted of the ₱11.73 million sinking fund required by the Department of Finance and ₱4.72 million escrow account in favor of terminated employees.

Allowance for doubtful accounts

The allowance for doubtful accounts for current and noncurrent trade receivables is established based on a regular review of the age and status of the accounts relative to historical collections, changes in customer payment terms and other factors that may affect collectibility. Except for accounts covered by special agreements with NPC (see Note 28), allowance for doubtful accounts covered all the full amounts of accounts outstanding over one year or accounts subject to contractual interpretation-dispute.

For other receivables, it was also established that accounts outstanding for less than one year are fully recoverable while accounts outstanding over one year shall be provided with 100% provision based on the Company's assessment of individually significant balances. Provision for individually non-significant balances was made on a portfolio or group basis after performing the regular review of the age and status of the individual accounts and portfolio/group of accounts relative to historical collections, changes in payment terms and other factors that may affect collectibility.

The rollforward analysis of the allowance for doubtful accounts pertaining to long-term receivables is presented below.

	2008			
	NPC	VAT Refund	Others	Total
Balance at beginning of year	₱950,145,607	₱1,894,719,994	₱62,466,360	₱2,907,331,961
Recoveries (see Notes 25 and 28)	(738,967,396)	-	-	(738,967,396)
Write-off of uncollectible accounts	(211,178,211)	-	-	(211,178,211)
Provision for doubtful accounts (see Note 25)	3,500,052	-	337,167	3,837,219
Balance at end of year	₱3,500,052	₱1,894,719,994	₱62,803,527	₱1,961,023,573
Specific impairment	₱3,500,052	₱1,894,719,994	₱-	₱1,898,220,046
Collective impairment	-	-	62,803,527	62,803,527
Total	₱3,500,052	₱1,894,719,994	₱62,803,527	₱1,961,023,573

	2007			
	NPC	VAT Refund	Others	Total
Balance at beginning of year	₱1,641,726,228	₱1,894,719,994	₱61,120,900	₱3,597,567,122
Write-off of uncollectible accounts	(665,723,546)	-	-	(665,723,546)
Recoveries (see Notes 25 and 28)	(25,857,075)	-	-	(25,857,075)
Provision for doubtful accounts (see Note 25)	-	-	1,345,460	1,345,460
Balance at end of year	₱950,145,607	₱1,894,719,994	₱62,466,360	₱2,907,331,961
Specific impairment	₱950,145,607	₱1,894,719,994	₱-	₱2,844,865,601
Collective impairment	-	-	62,466,360	62,466,360
Total	₱950,145,607	₱1,894,719,994	₱62,466,360	₱2,907,331,961



As discussed in Notes 8 and 28, the write-off and recoveries in 2008 were the result of the arbitral settlement award related to receivables from NPC. Long-outstanding receivables from NPC that are not recoverable as a result of the arbitration were written off.

16. Trade and Other Payables

	2008	2007
Accounts payable - trade (see Note 3)	₱2,156,184,775	₱3,392,254,842
Accrued interest and guarantee fees (see Note 20)	347,876,055	139,924,021
Accrued premium on range bonus forwards (see Note 40)	175,116,194	-
Withholding and other taxes payable	34,877,590	56,557,449
SSS and other contributions payable	6,526,176	38,921,376
Deferred credits	9,730,829	6,297,836
Other current liabilities	8,649,387	3,826,743
	₱2,738,961,006	₱3,637,782,267

Accounts payable - trade are noninterest-bearing and are normally settled on a 30-day payment term.

The accrued interest represents interest accrual on outstanding loans reckoning from the last payment date up to the balance sheet date. Guarantee fees are accrual of amounts due to the Philippine Government reckoning from the last payment date up to the balance sheet date. Details of the guarantee fees are discussed in Note 20 to the parent company financial statements.

The ₱175.12 million accrued premium on range bonus forwards represents the total premium due to counterparty every time the spot rate of the Japanese Yen was traded outside the predetermined ranges defined in the two range bonus forward contracts that cover the yen-dollar foreign exchange risk of the JPY8.0 billion out of the JPY12.0 billion Miyazawa 1 loan.

As of December 31, 2008, the Company had ₱2.67 billion unused credit facilities from various local banks which may be available for future operating activities.

17. Loan Payable

Loan payable consists of an unsecured short-term borrowing obtained from a local bank for the Company's working capital requirements. The loan matures within 12 months from availment date. Interest rate is calculated based on three months Philippine Dealing System Treasury Reference Rate 2 (PDSTFR2) plus spread of 6.75%.



18. Royalty Fee Payable

	2008	2007
Due to DOE (see Note 33)	₱1,575,483,582	₱1,477,653,457
Due to LGUs (see Note 33)	112,798,885	256,273,707
Total	1,688,282,467	1,733,927,164
Current portion	(1,688,282,467)	(456,273,707)
Long-term portion	₱-	₱1,277,653,457

A rollforward analysis of the recognized “Day 1” gain and accretion on the deferred royalty fee due to the DOE is shown below:

	2008	2007
Balance at beginning of year	₱225,590,774	₱397,267,332
Additions (see Note 29)	-	39,769,241
Accretion (see Note 26)	(225,590,774)	(211,445,799)
Balance at end of year	₱-	₱225,590,774

As discussed in Note 32, by virtue of P.D. 1442, the Company entered into seven service contracts with the DOE, which grants the Company the right to explore, develop, and utilize the country’s geothermal resources subject to sharing of net proceeds with the Philippine Government. The Company pays royalty fees to the DOE and LGUs under the agreements.

Royalty fees due to the DOE are payable based on a pre-agreed payment schedule and are non-interest bearing (see Note 33). In accordance with PAS 39, a “Day 1” gain was recognized for the difference between the nominal/maturity value and present value of the royalty fee payable, which was discounted using 12.38% to 12.72% in 2007 and 11.75% to 12.26% in 2006. “Day 1” gain recognized amounted to nil in 2008, ₱39.77 million in 2007 and ₱95.70 million in 2006, for the difference between the maturity value and present value of additional royalty fee recorded in each of the year. The amount of “Day 1” gain is included in the “Miscellaneous - net” account in the parent company statements of income. Subsequent to initial recognition, royalty fee payable is accreted to its maturity value based on its effective interest rate determined at day one.

Royalty fees due to the LGUs are payable within sixty days after the end of each quarter to DOE, which in turn remits the said payments to the Department of Budget and Management (DBM). The DBM releases on a quarterly basis the preceding year’s royalty fees due to the LGUs within five days after the end of each quarter. This procedure is in accordance with Article 390 of the Implementing Rules and Regulations of the Local Government Code of 1991.

Accretion recognized in 2008 and 2007 amounted to ₱225.59 million and ₱211.45 million, respectively. This is included under “Interest expense” account in the parent company statements of income (see Note 26).



19. Obligations to a Power Plant Contractor

This account pertains to the remaining obligation to the power plant contractor, Marubeni-Oxbow Consortium in connection with the construction of the geothermal power plants in Mindanao which are due for transfer to the Company in June 2009.

The details are as follows:

	Minimum Payments		Present Value of Minimum Payments	
	2008	2007	2008	2007
Amounts payable to a power plant contractor:				
Within one year	₱115,151,291	₱265,744,529	₱112,187,446	₱246,719,220
Second to fifth years, inclusive	–	100,347,856	–	96,287,392
Future finance charges	(2,963,845)	(23,085,773)	–	–
Present value of obligations	112,187,446	343,006,612	112,187,446	343,006,612
Amount due for settlement within 12 months (shown under current liabilities)	(112,187,446)	(246,719,220)	(112,187,446)	(246,719,220)
Amount due for settlement after 12 months	₱–	₱96,287,392	₱–	₱96,287,392

20. Long-term Debt

The Company's foreign-currency denominated long-term loans were translated into Philippine pesos based on the prevailing foreign exchange rates as at balance sheet date (USD1=JPY90.942: USD1=PHP47.520 on December 31, 2008 and USD1=JPY113.688: USD1=PHP41.411 on December 31, 2007).

The details of the Company's long-term debt are as follows:

Creditor/Project	Maturities	Interest Rate	2008	2007
International Bank for Reconstruction and Development (IBRD)				
<i>2969 PH Bacon-Manito Geothermal Power Plant</i>				
▪ USD41 million	1994 to 2008	½ of 1% over cost of qualified borrowings	₱–	₱213,917,487
<i>3164 PH Energy Sector Loan</i>				
▪ USD118 million	1995 to 2010	½ of 1% over cost of qualified borrowings	1,012,590,991	1,327,865,958
<i>3702 PH Geothermal Exploration Project</i>				
▪ USD64 million	1999 to 2013	½ of 1% over cost of qualified borrowings	1,261,094,917	1,194,375,196
<i>3747 PH Geothermal Exploration Project</i>				
▪ USD114 million	1999 to 2014	½ of 1% over cost of qualified	1,449,918,621	1,353,629,819
▪ JPY12.4 billion	1999 to 2014	qualified borrowings/3.5%	1,177,667,697	971,506,792

(Forward)



Creditor/Project	Maturities	Interest Rate	2008	2007
Overseas Economic Cooperation Fund (OECF)				
<i>8th Yen Tongonan I Geothermal Power Plant (share in OECF-NPC loan)</i>				
▪ JPY5.8 billion	1990 to 2010	3.0%	223,345,012	259,486,510
▪ JPY1.5 billion (Restructured)		3.2%	131,647,242	117,990,135
<i>9th Yen Palimpinon I Geothermal Power Plant</i>				
▪ JPY8.5 billion	1991 to 2011	3.0%	542,686,512	529,623,002
<i>15th Yen Palimpinon I Geothermal Power Plant</i>				
▪ JPY4.0 billion	1999 to 2019	5.7%	851,549,400	650,141,912
<i>18th Yen Palimpinon II Geothermal Power Plant</i>				
▪ JPY77.4 million	2003 to 2023	5.5%	28,597,891	21,310,198
<i>19th Yen Mt. Labo Geothermal Project</i>				
▪ JPY320 million	2004 to 2024	4.9%	130,540,515	96,686,098
<i>21st Yen NNGP</i>				
▪ JPY14.5 billion, of which JPY5.9 billion was drawn in 2007	2007 to 2027	2.7%/2.3%	4,916,323,601	3,612,377,416
National Government				
<i>PCIR Bonds</i>				
▪ USD328 thousand	1992 to 2017	Year 1 - 4 ¼% 2 - 5 ¼% 3 - 5 ¾% 4-5 - 6 ¼% 6-25 - 6 ½%	-	13,579,092
Miyazawa I				
▪ JPY5.2 billion	June 1, 2009	Tranche A=3.78%	₱2,714,273,054	₱1,889,975,187
▪ JPY6.8 billion		Tranche B=1.60% + LIBOR	3,549,771,370	2,471,931,240
Miyazawa II				
▪ JPY22.0 billion	June 26, 2010	2.37%	11,327,043,915	7,738,708,293
Land Bank of the Philippines				
▪ PHP1.5 billion	June 29, 2008	Average 91-day T-Bill + 2%	-	378,409,091
Total			29,317,050,738	22,841,513,426
Current portion			(8,217,253,830)	(2,031,565,879)
Long-term portion			₱21,099,796,908	₱20,809,947,547

The long-term debt is presented net of unamortized transaction costs. A rollforward analysis of unamortized transactions costs follows:

	2008	2007
Balance at beginning of year	₱283,924,584	₱539,995,801
Amortization	(120,834,470)	(218,138,637)
Foreign exchange loss (gain) - net	11,838,826	(37,932,580)
Balance at end of year	₱174,928,940	₱283,924,584

Amortization of transaction costs during the year is included under "Interest expense" account in the parent company statements of income.

The Company entered into long-term loan arrangements with domestic and international financial institutions for its various development projects and working capital requirements. PNOC, then the parent company of EDC, is the primary borrower of the loans from IBRD with sub-lending



arrangements with EDC. NPC is the primary borrower of certain loans from OECF with sub-lending arrangements with EDC. For the other loans, EDC is the direct borrower with the obligations guaranteed by the Philippine Government. The Company pays a guarantee fee of 1.00% per annum to the Philippine Government based on the outstanding balance of the guaranteed loans. Starting January 1, 2008, the guarantee fee increased to 2% per annum. Beginning January 2011, the guarantee fee shall be increased by 0.25% per annum up to a maximum of 3.00% per annum.

The loan covenants covering the obligation to the IBRD include, among others, maintenance of certain level of current, debt-to-equity and debt-service ratios. As of December 31, 2008, the Company is in compliance with the loan requirements.

Except for the PCIR Bonds, the loans of the Company are unsecured. The PCIR Bonds represent converted outstanding International Bank of Japan loans equivalent to US\$327,910 under a Memorandum of Agreement dated November 16, 1992. The PCIR Bonds bear interest rate of 6.5% per annum, payable semi-annually with bullet principal payment in 2017. A cash collateral amounting to US\$74,057 (₱3.52 million), presented under “Other current assets” account in 2008 and “Other noncurrent assets” account in 2007, was deposited with the Bangko Sentral ng Pilipinas (BSP) as part of the agreement and will be returned to the Company without interest upon full settlement of the bonds (see Notes 8 and 15). The PCIR Bonds were fully settled in December 2008 and the related cash collateral has yet to be returned by the BSP.

21. Other Long-Term Liabilities

This account consists of accrued vacation and sick leave entitlement of active employees. The accruals pertain to the unused vacation and sick leaves at the end of the calendar year up to the maximum allowed leave credits for accrual. Vacation and sick leave credits exceeding the maximum allowed for accrual are forfeited.

22. Equity

Capital Stock

As required under the Philippine Constitution, the Company is subject to the nationality requirement that at least sixty percent (60%) of its capital stock must be owned by Filipino citizens since it is engaged in the exploration and exploitation of the country’s energy resources. The Company is compliant with the said nationality requirement.

The common shares are majority held by Filipinos, with Red Vulcan holding 6 billion shares or an equivalent of 40% interest.

The ownership of the Company’s preferred shares is limited to Filipino citizens. The preferred shares have voting rights and subject to 8% cumulative interest. Red Vulcan holds the entire 7.5 billion preferred shares equivalent to 20% voting interest in EDC. The combined interest of Red Vulcan entitles it to 60% voting interest and 40% economic interest in EDC.



As of December 31, 2008, there are 635 common stockholders and one (1) preferred shareholder of the Company.

The movements of common and preferred shares are as follows:

	Number of Shares	
	2008	2007
Common stock - ₱1 par value		
Authorized and issued	15,000,000,000	15,000,000,000
Outstanding:		
Balance at beginning of year	15,000,000,000	15,000,000,000
Common shares held in treasury	(93,000,000)	–
Balance at end of year	14,907,000,000	15,000,000,000
Preferred stock - ₱0.01 par value		
Authorized, issued and outstanding:		
Balance at beginning of year	7,500,000,000	–
Issuances	–	7,500,000,000
Balance at end of year	7,500,000,000	7,500,000,000

Cost of Treasury Shares Held

On March 25, 2008, the BOD of the Company approved a share buyback program involving up to ₱4.0 billion worth of the Company's common shares, representing approximately four percent (4%) of the Company's market capitalization as of the date of approval. The buyback program will be carried out within a two-year period which commenced on March 26, 2008 and ending on March 25, 2010.

The Company intends to implement a proposed executive/employee stock option ownership plan through options, grants, purchases, or such other equivalent methods. On January 23, 2009, the BOD of the Parent Company approved the Executive/Employee Stock Ownership Plan and the related rules, specifically on stock grant. The plan is an integral part of the Parent Company's rewards program for its employees and it is intended to provide an opportunity for the participants to have real and personal direct interest in the Company. There are no stock awards granted as of March 30, 2009.

As of December 31, 2008, a total of 93,000,000 common shares amounting to ₱404.22 million have been acquired by the Company.

Retained Earnings

a. Dividend declarations

On February 19, 2008, the BOD of the Company approved the following cash dividends in favor of all stockholders of record as of March 5, 2008, which were paid on March 17, 2008:

- cash dividend of ₱0.0004 a share on the preferred shares totaling ₱3.00 million
- regular cash dividend of ₱0.125 a share on the common shares totaling ₱1,875.00 million
- special cash dividend of ₱0.145 a share on the common shares totaling ₱2,175.00 million



On April 17, 2007, the Company declared a cash dividend of ₱0.099 a share or a total of ₱1,485.00 million to all stockholders of record as of May 15, 2007, which was paid on June 5, 2007.

On September 19, 2006, the Company declared a 20% stock dividend to PNOC, the then sole shareholder of the Company, which was distributed on October 9, 2006.

b. Reversal of appropriations

On December 16, 2008, the BOD of the Company approved the reversal of previously appropriated retained earnings totaling ₱1,653.32 million, which was earmarked to undertake exploration activities and, acquisition and refurbishment of exploration equipment. The intended activities and acquisitions have been completed in 2008.

c. Adjustment on appraisal increase

In 2008, the Company adjusted the related deferred tax liabilities on appraisal increase on property and equipment recorded upon adoption of PFRS on January 1, 2005. The appraised values of property and equipment were recognized as fair value deemed cost consistent with the provisions of PFRS 1.

23. Purchased Services and Utilities

	2008	2007
Professional and technical services	₱684,647,336	₱387,199,262
BOT fees (see Note 35)	393,981,872	2,105,680,050
Purchased services	247,672,243	166,636,601
Rig mobilization charges	76,685,866	85,527,042
Hauling and handling costs	75,159,487	40,958,297
Contractual employee costs	19,254,749	28,278,317
Purchased utilities	17,619,911	219,335,104
Others	8,912,246	4,381,485
	₱1,523,933,710	₱3,037,996,158

24. Operations and Maintenance Expenses

	2008	2007 (see Note 43)
Repairs and maintenance	₱1,773,106,790	₱1,026,987,972
Personnel costs	1,388,397,780	1,232,874,326
Materials and supplies issued (see Note 7)	969,116,159	569,879,759
Royalty fees	590,120,392	499,577,821
Rental, insurance and taxes	271,786,514	584,220,983
Business and related expenses	137,230,571	86,377,159
Proceeds from insurance claims	(205,157,285)	(63,656,268)
Grantor assessment adjustment	-	(866,399,332)
	₱4,924,600,921	₱3,069,862,420



Proceeds from insurance claims are shown as a separate line item under the operations and maintenance expenses. The Company charges to expense outright any cost incurred relating to restoring or rehabilitating facilities or land improvements damaged by typhoons or by other factors, insurance proceeds from the insurance claims upon receipt are subsequently recognized as proceeds from insurance claims.

In 2007, the grantor assessment adjustment was the result of the re-computation of the recoverable costs done in conjunction with the DOE to give effect to the amended provisions set forth in the GSCs, which allows recovery of the translation effects of the Company's foreign loans and financing costs. The amended provisions and the royalty adjustments were agreed with the DOE in July 2007.

25. General and Administrative Expenses

	2008	2007 (Note 43)
Personnel costs	₱910,598,551	₱903,179,645
Purchased services and utilities (see Note 37)	522,852,337	345,802,058
Rental, insurance and taxes (see Note 37)	338,126,951	577,573,077
Business and related expenses	213,571,452	121,934,614
Materials and supplies issued (see Note 7)	158,068,102	112,145,705
Repairs and maintenance	54,692,168	31,413,518
Depreciation (see Note 11)	18,727,670	39,944,943
Provisions for doubtful accounts (see Notes 6 and 15)	6,019,400	286,828,060
Credit adjustment on allowance for doubtful accounts (see Notes 6, 15 and 28)	(1,116,185,994)	(43,130,239)
	₱1,106,470,637	₱2,375,691,381

26. Interest Expense

	2008	2007 (Note 43)
Interest on long-term loans	₱1,416,039,385	₱1,137,502,428
Interest accretion of day 1 gain (see Note 18)	225,590,774	211,445,799
Amortization of transaction costs on loans	120,834,470	218,138,637
Interest on short-term loan	34,535,508	51,798
	₱1,797,000,137	₱1,567,138,662
Amounts included in the cost of qualifying assets	(117,059)	(99,927)
	₱1,796,883,078	₱1,567,038,735

This account pertains to interest charges on long-term and short-term loans, including accretion of "Day 1" gain. The amounts included in the cost of qualifying assets represent the capitalized interest on loans obtained for NNGP. The capitalized interest is included under "Exploration and evaluation costs" account in the parent company balance sheets.



27. Foreign Exchange Gains (Losses)

	2008	2007
Foreign exchange gains (losses) on long-term loans	(P8,828,854,167)	P4,239,574,615
Foreign exchange losses on other accounts	(139,573,680)	(339,228,391)
Net	(P8,968,427,847)	P3,900,346,224

This account pertains to foreign exchange gains adjustments realized on repayment of loans and restatement of outstanding balances of foreign currency-denominated loans, short-term placements and cash in banks. Following are the exchange rates used to restate outstanding balances at yearend:

Currency	Equivalent to US\$1.00	
	December 31, 2008	December 31, 2007
Japanese Yen	90.942	113.688
Philippine Peso	47.520	41.411

28. Revenue from Arbitration Award

On April 24, 2008, the Company and NPC signed a Joint Manifestation and Undertaking (JMU) to abide by the arbitral decision on March 25, 2008. The arbitral decision covered the long-standing issue related to the SSAs and PPAs of EDC and NPC.

In the execution of the arbitral decision, both the Company and NPC agreed that the amount of P2,894.93 million shall be paid by NPC to the Company, without further interest, in accordance with the following schedule:

Tranche	Settlement Amount	Payment Term	Actual Date of Settlement
First	P500.00 million	30 days from submission of JMU to the Office of the Voluntary Arbitrator	July 15, 2008
Second	500.00 million	60 days from submission of JMU to the Office of the Voluntary Arbitrator	July 15, 2008
Third	1,000.00 million	January 2009	February 2, 2009
Fourth	894.93 million	January 2010	Not applicable

Full payment of the foregoing amounts shall constitute full and complete settlement of all the claims each party has against the other as detailed in the November 5, 2007 arbitration agreement.



As a result of the foregoing transaction in 2008, the Company recognized an income of ₱2,894.93 million recorded as revenue from arbitration award of ₱2,067.34 million and a reversal of allowance for doubtful accounts of ₱827.59 million previously recorded related to the portion collected as part of the settlement. In addition, allowance for doubtful accounts of ₱288.60 million was reversed following the resolution of some of certain issues covered by the arbitration. The reduction of the allowance for doubtful accounts resulted in the recognition of the credit adjustments on allowance for doubtful accounts totaling ₱1,116.19 million classified under “General and administrative expenses” account (see Note 25).

29. Miscellaneous Income (Charges)

	2008	2007
Power plant materials inventory turned over by contractor	₱260,614,700	₱-
“Day 1” loss (see Note 15)	(189,790,628)	-
Gain on sale of AFS investments (see Note 9)	46,323,392	7,937,724
Waste disposal fees	16,525,517	17,893,896
Gain (loss) on retirement of parts and supplies inventory	(2,012,309)	5,683,609
“Day 1” gain (see Note 18)	-	39,769,241
Others	27,350,026	(275,697,407)
	₱159,010,698	(₱204,412,937)

The Company recognized a “Day 1” loss of ₱189.79 million representing the difference between the present values of the third and fourth tranches of the scheduled collection of the arbitration award and the maturity values (see Notes 15 and 28).

30. Income Tax

	2008	2007
Deferred tax assets	₱8,187,873,115	₱6,750,699,755
Deferred tax liabilities	(4,777,480,777)	(3,697,907,168)
Net	₱3,410,392,338	₱3,052,792,587

The deferred tax assets consist mainly of the undepreciated balance of foreign exchange losses on payment and realignment of the payable to contractors capitalized under BIR reporting, unrealized foreign exchange losses on foreign loans and allowance for doubtful accounts. The account is net of deferred tax liabilities on allowed accelerated deductions for tax purposes of expenses related to steam operations based on the GSCs and P.D. 1442, appraisal increase on Company’s properties and prior year’s revenues from uncollected contested nominated energy.



The components of the Company's deferred income tax assets and liabilities follow:

Deferred Tax Assets

	Foreign Exchange Losses (Gains) BOT Power Plants	Unrealized Foreign Exchange Losses (Gains)	Allowance For Doubtful Accounts	IFRIC 12 Adjustments	Others	Total
At January 1, 2008	₱4,346,549,575	₱215,335,039	₱1,149,431,133	₱436,335,882	₱603,048,126	₱6,750,699,755
Charged to income for the year	(342,721,181)	2,335,799,856	(560,607,889)	61,244,725	(56,542,151)	1,437,173,360
At December 31, 2008	₱4,003,828,394	₱2,551,134,895	₱588,823,244	₱497,580,607	₱546,505,975	₱8,187,873,115
At January 1, 2007	₱4,673,833,358	₱1,229,264,289	₱1,064,246,930	₱509,705,776	₱570,146,497	₱8,047,196,850
Charged to income for the year	(327,283,783)	(1,013,929,250)	85,184,203	(70,683,170)	32,901,629	(1,293,810,371)
Reclassification (see Note 43)	-	-	-	(2,686,724)	-	(2,686,724)
At December 31, 2007	₱4,346,549,575	₱215,335,039	₱1,149,431,133	₱436,335,882	₱603,048,126	₱6,750,699,755

Deferred Tax Liabilities

	Deductible Expenses under P.D. 1442	Others	Total
At January 1, 2008	(₱3,659,182,751)	(₱38,724,417)	(₱3,697,907,168)
Charged to retained earnings (see Note 22)	-	(449,433,875)	(449,433,875)
Charged to income for the year	(22,175,897)	(607,963,837)	(630,139,734)
At December 31, 2008	(₱3,681,358,648)	(₱1,096,122,129)	(₱4,777,480,777)
At January 1, 2007	(₱3,085,955,501)	(₱41,287,282)	(₱3,127,242,783)
Charged to income for the year	(575,913,974)	2,562,865	(573,351,109)
Reclassification (see Note 43)	2,686,724	-	2,686,724
At December 31, 2007	(₱3,659,182,751)	(₱38,724,417)	(₱3,697,907,168)

	Deferred Tax Assets	Deferred Tax Liabilities	Net Deferred Tax Assets
At January 1, 2008	₱6,750,699,755	(₱3,697,907,168)	₱3,052,792,587
Charged to retained earnings (see Note 22)	-	(449,433,875)	(449,433,875)
Charged to income for the year	1,437,173,360	(630,139,734)	807,033,626
At December 31, 2008	₱8,187,873,115	(₱4,777,480,777)	₱3,410,392,338
At January 1, 2007	₱8,047,196,850	(₱3,127,242,783)	₱4,919,954,067
Charged to income for the year	(1,293,810,371)	(573,351,109)	(1,867,161,480)
Reclassification (see Note 43)	(2,686,724)	2,686,724	-
At December 31, 2007	₱6,750,699,755	(₱3,697,907,168)	₱3,052,792,587



The components of provision for income tax expense are as follows:

	2008	2007
Current tax	₱2,142,539,458	₱2,293,832,941
Deferred tax	(807,033,626)	1,867,161,480
	₱1,335,505,832	₱4,160,994,421

A numerical reconciliation between tax expense and the product of accounting income multiplied by the tax rate of 35.00% is as follows:

	2008	2007
Accounting income	₱2,587,645,987	₱12,812,475,607
Income tax expense at statutory tax rate	₱905,676,095	₱4,484,366,462
Effect of change in tax rate	492,973,349	(274,795,065)
Tax effect of non-deductible interest expense	37,233,986	53,375,602
Non-deductible provisions	1,602,816	-
Non-deductible foreign contractor's tax - excess	403,557	4,389,682
Additional expenses (50%) on Adopt-A-School Act of 1998	(913,963)	-
Non-taxable foreign exchange gains in ROP bonds	(27,612,838)	-
Interest income - net of final tax	(73,857,170)	(106,342,260)
Provision for income tax	₱1,335,505,832	₱4,160,994,421

Under Republic Act No. 9337, which amended certain provisions of Tax Return Act of 1997, the new Regular Corporate Income Tax rate shall be 30% effective January 1, 2009.

On December 18, 2008, the BIR issued Revenue Regulations (RR) No. 16-2008 which implemented the provisions of Section 34(L) of the Tax Code of 1997, as amended by Section 3 of Republic Act No. 9504, which allows individuals and corporations to adopt the Optional Standard Deduction (OSD) in computing their taxable income.

Under RR 16-2008, individuals and corporations may claim OSD equivalent to 40% of gross income, excluding passive income subjected to final tax, in lieu of the itemized deductions. A corporate taxpayer who elected to avail of the OSD shall signify such in the income tax return. Otherwise, it shall be considered as having availed of the itemized deductions allowed under Section 34 of the National Internal Revenue Code. Election is done on an annual basis.

In 2008, the Company computed its income tax based on itemized deductions.



31. Personnel Costs

	2008	2007
Salaries and other benefits	₱2,313,481,409	₱2,158,560,842
Retirement benefit costs (see Note 38)	240,719,196	189,749,707
Social security costs	43,707,750	42,316,907
	₱2,597,908,355	₱2,390,627,456

32. Description of the Service Concession and Related Arrangements

All geothermal resources in public and/or private lands in the Philippines, whether found in, on or under the surface of dry lands, creeks, rivers, lakes, or other submerged lands within the waters of the Philippines, belong to the State, inalienable and imprescriptible, and their exploration, development and exploitation are governed under P.D. No. 1442 (P.D. 1442, An Act to promote the exploration and development of geothermal resources). Under P.D. 1442, the Government may enter into service contracts for the exploration, development and exploitation of geothermal resources.

Pursuant to P.D. 1442, the Company has entered into the following service contracts with the Government of the Republic of the Philippines (Government, represented by the DOE) for the exploration, development and production of geothermal fluid for commercial utilization:

- a. Tongonan, Leyte, dated May 14, 1981
- b. Southern Negros, dated October 16, 1981
- c. Bacman, Sorsogon, dated October 16, 1981
- d. Mt. Apo, Kidapawan, Cotabato, dated March 24, 1992
- e. Mt. Labo, Camarines Norte and Sur, dated March 19, 1994
- f. Northern Negros, dated March 24, 1994
- g. Mt. Cabalian, Southern Leyte, dated January 13, 1997

The exploration period under the service contracts shall be five years from the effective date, renewable for another two years, if the Company has not been in default in its exploration, financial and other work commitments and obligations and has provided a work program for the extension period acceptable to the Government. Where geothermal resource in commercial quantity is discovered during the exploration period, the service contracts shall remain in force for the remainder of the exploration period or any extension thereof and for an additional period of 25 years thereafter, provided that, if the Company has not been in default in its obligations under the contracts, the Government may grant an additional extension of 15 to 20 years.

The Company shall acquire for the geothermal operations materials, equipment, plants and other installations as are required and necessary to carry out the geothermal operations. All materials, equipment, plants and other installations erected or placed on the contract areas of a movable nature by the Company shall remain the property of the Company unless not removed therefrom within one year after the expiration and/or termination of the related service contract in which case, ownership shall be vested in the Government.



The service contracts provide that, among other privileges, the Company shall have the right to enter into agreements for the disposition of the geothermal resources produced from the contract areas, subject to the approval of the Government.

Pursuant to such right, the Company has entered into agreements for the sale of the geothermal resources produced from the service contract areas principally with the NPC, a government-owned and controlled corporation. These agreements are for 25 years and may be renegotiated by either party after five years from the date of commercial operations.

Pursuant to such right also, the Company has also entered into agreements with NPC for the development, construction and operation of a geothermal power plant by the Company in its geothermal service contract areas and the sale to NPC of the electrical energy generated from such geothermal power plants. These agreements are for 25 years of commercial operations and may be extended upon the request of the Company by notice of not less than 12 months prior to the end of the contract period, the terms and conditions of any such extension to be agreed upon by the parties.

The Company's agreements with NPC for the sale of the geothermal resources produced from the service contract areas and the sale of the electrical energy generated from the geothermal power plants contain certain provisions relating to pricing control in the form of a cap in the Company's internal rate of return for specific contracts; as well as for payment by NPC of minimum guaranteed monthly remuneration and nominated capacity.

For the Northern Negros service contract, the Company does not have agreements with NPC for the sale of the geothermal resources and electrical energy produced from the service contract area. The Company instead enters into contracts with distribution utilities, electric cooperatives and other third party buyers of electricity for the sale of the electrical energy generated from the service contract.

The Company has made a judgment that these service concessions and related arrangements qualify for accounting under Philippine Interpretation IFRIC 12. Accordingly, the Company has recognized the consideration received or receivable in exchange for its infrastructure construction services or its acquisition of infrastructure to be used in the arrangements as either a financial asset to the extent that the Company has an unconditional contractual right to receive cash or other financial asset for its construction services from or at the direction of the grantor, or an intangible asset for the right to charge users of the public service.

Revenue and profits recognized in 2008 and 2007, on exchanging construction services for a financial or an intangible asset amounted to ₱932.25 million and ₱108.81 million, respectively; and ₱128.59 million and ₱7.68 million, respectively.

The disclosures have been provided in aggregate since management believes that the service concession arrangements are similar in nature.



33. Service Contracts

As discussed in Note 32, by virtue of P.D. 1442, the Company entered into seven service contracts with the DOE granting the Company the right to explore, develop, and utilize the country's geothermal resource subject to sharing of net proceeds with the government. The net proceeds is what remains after deducting from the gross proceeds the allowable recoverable costs, which include development, production and operating costs.

The allowable recoverable costs shall not exceed 90% of the gross proceeds. The Company pays 60% of the net proceeds as government share and retains the remaining 40%.

The 60% government share is comprised of royalty fees and income taxes. The royalty fees are shared by the Government through DOE (60%) and the LGU (40%).

The Company secured an approval from the DOE to defer remittance of the royalty portion of the Government share at ₱180 million per year. A portion of said payment was applied to the amortization of the deferred royalty fees as of December 31, 1998, and the balance to 1999 and future obligations. On March 23, 2004, the Company and DOE agreed to increase the royalty payment plan to ₱200 million per year starting 2004. A portion of the revised payment shall be applied to the amortization of the deferred royalty fees as of December 31, 2003 and the balance to 2004 and future obligations for existing Company operating projects. However, remittances to the LGUs of their share in royalty fees are made as they fall due pursuant to the Local Government Code.

Total outstanding royalty fees due to DOE and to LGUs are shown in Note 18 to the parent company financial statements.

The DOE approved the application of the Company for the 20-year extension of the Tongonan, Palinpinon and Bacon-Manito GSC. The extension is embodied in the fourth amendment to the GSCs dated October 30, 2003. The amendment extended the Tongonan GSC from May 15, 2011 to May 16, 2031, while the Palinpinon and Bacon-Manito GSCs are extended from October 16, 2011 to October 17, 2031.

34. Geothermal Resources Sales Contract

The geothermal energy currently produced by the Company's geothermal projects is supplied to the power plants owned and operated by NPC pursuant to the following terms of the steam sales contracts:

Tongonan-I

Under the steam sales contract entered in June 1984 for Tongonan I, NPC agrees to pay the Company a base price per kilowatt-hour of net generation, subject to inflation adjustments and based on a guaranteed take-or-pay rate at 75% plant factor for a period of 25 years. NPC opted to extend this agreement until the sale of the power plant slated for bidding in mid-2009.



Palinpinon-I

The steam sales contract for Palinpinon I provides, among others, that NPC shall pay the Company a base price per kilowatt-hour of gross generation, subject to inflation adjustments and based on a guaranteed take-or-pay rate at 75% plant factor. The contract is for a period of 20 years, which commenced on December 25, 1988. NPC opted to extend this agreement until the sale of the power plant slated for bidding in mid-2009.

Palinpinon-II

In June 1996, the Company and NPC signed a steam sales contract for Palinpinon II's four modular plants - Nasuji, Okoy, Sogongon I and Sogongon II. Under the terms and conditions, NPC agrees to pay the Company a base price per kilowatt-hour of gross generation, subject to inflation adjustments and based on a guaranteed take-or-pay rate commencing from the established commercial operation period, using the following plant factors: 50% for the first year, 65% for the second year and 75% for the third and subsequent years. The contract is for a period of 25 years for each module, which commenced on December 13, 1993 for Nasuji; November 28, 1994 for Okoy; January 28, 1995 for Sogongon I and March 23, 1995 for Sogongon II.

Bacon-Manito-I

The steam sales contract for the Bacon-Manito (Bacman) geothermal resources entered in November 1988 provides, among others, that NPC shall pay the Company a base price per kilowatt-hour of gross generation, subject to inflation adjustments and based on a guaranteed take-or-pay rate at 75% plant factor. The contract is for a period of 25 years, which commenced in May 1993.

Bacon-Manito-II

Bacman II's steam sales contract with NPC was signed in June 1996 for its two 20-MW capacity modular plants - Cawayan and Botong. The terms and conditions under the contract contain, among others, NPC's commitment to pay the Company a base price per kilowatt-hour of gross generation, subject to inflation adjustments and based on a guaranteed take-or-pay rate, commencing from the established commercial operation period, using the following plant factors: 50% for the first year, 65% for the second year and 75% for the third and subsequent years. The contract is for a period of 25 years, which commenced in March 1994 for Cawayan and December 1997 for Botong.

35. **BOT Contracts**

Pursuant to Republic Act Number 7718 dated May 5, 1994 (Amended BOT Law), the Company entered into Energy Conversion Agreements (ECA) with various international geothermal power producers for the construction and operation of power plants in Leyte and Mindanao to convert the geothermal steam to be supplied by the Company to electricity. Under these contracts, the BOT Contractor shall deliver electricity to NPC on behalf of the Company.

Leyte

Under the ECA with the BOT Contractors, namely: California Energy for a) 125 MW Power Plant - Upper Mahiao Agreement; b) 231 MW Power Plant - Malitbog Agreement; and c) 180 MW Power Plant - Mahanagdong Agreement and with Ormat Inc. for the Leyte Optimization Project BOT Agreement, the Company shall pay the BOT Contractors monthly energy fees to be



computed based on actual energy delivered and capacity fees, which include capital and fixed operating cost recovery fees and service fees, to be computed on a per kilowatt nominated capacity basis.

Except for the capital cost recovery portions, the fees are subject to inflation adjustments. The contracts are for a period of ten years, which commenced in July 1996 for the Upper Mahiao Agreement, July 1997 for the Malitbog and Mahanagdong Agreements and September 1997 for the Optimization Agreement. The ownership of the Upper Mahiao Power Plant was transferred to the Company on June 25, 2006; Malitbog and Mahanagdong Power Plants were transferred on July 25, 2007; and the Optimization Power Plants on September 25, 2007.

Mindanao

Under the terms and conditions of the ECA with Oxbow Power Corporation and Marubeni Corporation, the Company shall pay the BOT Contractor monthly energy efficiency fees and capacity fees, which include capital and fixed operating cost recovery fees and service fees, to be computed on a per kilowatt nominated capacity basis and excess energy fees which are payment for the share of BOT Contractor for the revenues from surplus energy generation on top of the nominated energy. Except for energy efficiency payments and capital cost recovery portion of capacity fees, the fees are subject to inflation adjustments. The contract is for a period of ten years, which commenced in March 1997 for Mindanao I (47 MW) and June 1999 for Mindanao II (48.25 MW). An Amendment to the Mindanao I ECA was signed on November 17, 2006 extending the contract period to June 2009 with corresponding restructuring of BOT fees.

The fair value of these BOT contracts are included as part of the fair value of the construction services accounted for under Philippine Interpretation IFRIC 12 as discussed in Note 32 to the parent company financial statements.

36. Power Purchase Agreements

The electricity produced by the Company is sold to NPC, pursuant to the following PPAs:

Leyte-Cebu, Leyte-Luzon

The PPA provides, among others, that NPC shall pay the Company a base price per kilowatt-hour of electricity delivered subject to inflation adjustments. The PPA stipulates a contracted annual energy of 1,370 GWH for Leyte-Cebu and 3,000 GWH for Leyte-Luzon throughout the cooperation period. It also stipulates a nominated energy of not lower than 90% of the contracted annual energy.

On November 12, 1999, NPC agreed to accept from the Company a combined average annual nominated energy of 4,455 GWH for the period July 25, 1999 to July 25, 2000 for both Leyte-Cebu and Leyte-Luzon PPA. The annual nominated energy starting July 25, 2000 and onwards was contested by NPC, which is one of the issues of the arbitration with NPC (see Notes 15 and 28). The contracts are for a period of 25 years commencing in July 1996 for Leyte-Cebu and July 1997 for Leyte-Luzon.



47 MW Mindanao I

The PPA provides, among others, that NPC shall pay the Company a base price per kilowatt-hour of electricity delivered subject to inflation adjustments. The PPA stipulates a minimum offtake energy of 330 GWH for the first year and 390 GWH per year for the succeeding years. The contract is for a period of 25 years, which commenced in March 1997.

48.25 MW Mindanao II

The PPA provides, among others, that NPC shall pay the Company a base price per kilowatt-hour of electricity delivered subject to inflation adjustments. The PPA stipulates a minimum offtake energy of 398 GWH per year. The contract is for a period of 25 years, which commenced in June 1999.

37. Related Party Transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

The following are transactions that the Company had with related parties in 2008. No related party transactions transpired in 2007.

a. First Balfour, Inc. (First Balfour)

Following the usual bidding process in 2008, the Company awarded to First Balfour a procurement contract for various civil, structural, mechanical and piping works for the Leyte Geothermal Production Field. The contract amount is ₱360.0 million. The Company paid ₱54.0 million in 2008 as 15% advance payment for the steam augmentation project in Leyte.

Advance payment made was recorded under “Other current assets” account in the 2008 parent company balance sheet (see Note 8).

First Balfour is a wholly owned subsidiary of First Holdings, which is the ultimate parent company of EDC.

b. First Gen

First Gen provides financial consultancy, business development and other related services to the Company under a consultancy agreement beginning September 1, 2008. Such agreement is for a period of three years up to August 31, 2011. Under the terms of the agreement, billings for consultancy services shall be ₱8.70 million per month plus applicable taxes. Total consultancy services billed by First Gen amounted to ₱45.85 million. The outstanding balance as of December 31, 2008 included in the “Due to a related party” account amounted to ₱45.85 million.



c. FG Hydro

On November 24, 2008, the Company granted a cash advance to FG Hydro amounting to US\$3.24 million to fund its capital expenditure requirements as approved by the Company's BOD. Such cash advance bears an interest of 5.29% and payable upon demand. As of December 31, 2008, the Company had outstanding receivable from FG Hydro of ₱95.48 million inclusive of interest.

Following are the amounts of transactions and outstanding balances as of and for the year ended December 31, 2008:

Related Party	Nature of Transaction	Transaction During the Period	Amount Due from a Related Party	Amount Due to a Related Party
FG Hydro	Grant of interest-bearing advances	₱95,475,959	₱95,475,959	₱-
First Gen	Consultancy fee	45,854,118	-	47,213,065
	Directors liability insurance	1,358,947		

There were no guarantees provided or received for any related party. The Company has not recognized any impairment loss on the receivable from a related party as of December 31, 2008.

d. Remuneration of Key Management Personnel

The remuneration of the directors and other members of key management personnel by benefit type follows:

	2008	2007
Short-term employee benefits	₱79,192,591	₱39,626,921
Post-employment benefits (see Note 38)	82,218,181	76,699,639
	₱161,410,772	₱116,326,560

38. Retirement and Other Post-Retirement Benefit Plans

The Company maintains a funded, non-contributory, defined benefit retirement plan. The plan covers all permanent employees and is administered by a trustee bank. The Company also provides post-retirement medical and life insurance benefits which are unfunded.

The following tables summarize the components of net retirement expense recognized in the parent company statements of income and the funded status and amounts recognized in the parent company balance sheets:

	2008	2007
Current service cost	₱165,734,850	₱137,976,928
Interest cost on benefit obligation	188,497,828	154,587,224
Expected return on plan assets	(113,828,988)	(102,814,445)
Net actuarial loss recognized in the year	315,506	-
Net retirement expense (see Note 31)	₱240,719,196	₱189,749,707



	2008	2007
Actual return on plan assets	₱65,258,618	₱45,943,657
Present value of defined benefit obligations	₱3,179,147,273	₱2,692,826,116
Fair value of plan assets	(1,792,770,559)	(1,626,128,399)
	1,386,376,714	1,066,697,717
Unrecognized actuarial losses	(359,982,232)	(146,869,423)
Retirement liability	₱1,026,394,482	₱919,828,294

Changes in the present value of the defined benefit obligation are as follows:

	2008	2007
Defined benefit obligation at beginning of year	₱2,692,826,116	₱2,187,879,669
Interest cost	188,497,828	154,587,224
Current service cost	165,734,850	137,976,928
Benefits paid	(32,769,466)	(48,593,043)
Actuarial losses on obligation	164,857,945	260,975,338
Defined benefit obligation at end of year	₱3,179,147,273	₱2,692,826,116

Changes in the fair value of plan assets are as follows:

	2008	2007
Fair value of plan assets at beginning of year	₱1,626,128,399	₱1,468,777,785
Expected return	113,828,988	102,814,445
Contributions by employer	134,153,008	160,000,000
Benefits paid	(32,769,466)	(48,593,043)
Actuarial losses	(48,570,370)	(56,870,788)
Fair value of plan assets at end of year	₱1,792,770,559	₱1,626,128,399

The Company expects to contribute ₱173.00 million to its defined benefit retirement plan in 2009. The major categories of plan assets as a percentage of the fair value of total plan assets are as follows:

	2008	2007
Fixed income	93.83%	88.23%
Equities	6.17%	10.05%
Real properties	-	0.51%
Others	-	1.21%
	100.00%	100.00%

The principal actuarial assumptions used in determining retirement and post-retirement medical and life insurance benefit obligations are as follows:

	2008	2007
Discount rate	9.76%	7.00%
Expected rate of return on assets	7.00%	7.00%
Future salary increase rate	10.00%	6.00%
Medical trend rate	7.00%	3.00%



The assumption on the discount rate is based on the long-term government bond rates approximating the expected working life of the employees as published by the Philippine Dealing Exchange Corporation. The assumption on the expected rate of return on plan assets is based on the asset allocation while the expected rate of salary increases is around 3.00%–4.00% more than the projected inflation rate of about 6.00%–7.00%.

Amounts for the current and previous four periods are as follows:

	2008	2007	2006	2005	2004
Defined benefit obligation	(₱3,179,147,273)	(₱2,692,826,116)	(₱2,187,879,669)	(₱1,791,112,900)	(₱1,758,346,900)
Plan assets	1,792,770,559	1,626,128,399	1,468,777,785	1,222,617,700	1,594,938,200
Deficit	(₱1,386,376,714)	(₱1,066,697,717)	(₱719,101,884)	(₱568,495,200)	(₱163,408,700)

The experience adjustments on plan liabilities amounted to ₱62.11 million in 2008 and ₱143.64 million in 2007.

A one percentage point change in the assumed rate of increase in medical costs would have the following effects:

	Increase	Decrease
2008		
Effect on the aggregate current service cost and interest cost	23.35%	18.70%
Effect on the defined benefit obligation	20.67%	16.90%
2007		
Effect on the aggregate current service cost and interest cost	15.91%	13.47 %
Effect on the defined benefit obligation	13.22%	11.47 %

39. Supplementary Disclosures of Geothermal Reserves

In September 2008, the Company has contracted GeothermEX, Inc. (GeothermEX) to provide an independent review of the updated geothermal energy reserves estimation made by the Company's Reservoir Engineering Department for five geothermal fields: Bacon-Manito (Luzon), Mindanao (Mindanao), Palinpinon (Southern Negros) and Greater Tongonan (Leyte) and Northern Negros.

Five available methods of estimating geothermal reserves were considered as regards to their applicability to the Company's fields: empirical methods, volumetric reserve estimation, decline curve analysis, lumped-parameter modeling and numerical simulation of the reservoir. It was concluded that, of these methods, only volumetric reserve estimation and numerical simulation are generally useful to the Company in estimating reserves. The Company has conducted numerical simulation to most of its fields. A detailed review of such simulation study, for Mindanao field, showed it to be reasonable. It is pointed out that while numerical simulation is more sophisticated than volumetric reserve estimation, the latter can be readily conducted in a probabilistic way, while the former cannot.



GeothermEX, in their report released in October 2008, used the same volumetric reserve estimation method used by the Company for the various geothermal fields patterned after the United States Geological Survey but differ only in the heat recovery factor. GeothermEX concluded that the Company's estimation is conservative due to the low heat recovery factor values of 0.20 to 0.30. On the other hand, GeothermEX estimates of reserves in these field locations are 60% higher than those of the Company.

Proved geothermal reserves refer to reserves which can be produced with known certainty and delineated in known production limits as confirmed by drilling and production history.

Probable reserves refer to those that could be proven by normal step-out drilling as well as those that could be extracted by improved recovery techniques like acidizing.

Possible reserves refer to those reserves that are currently unextractable because of resource and technology problems but may be found to be commercial in the future.

The following table shows a comparison of estimated geothermal energy reserves from the Company and GeothermEX:

Estimated Geothermal Energy Reserves

Field	Mean Reserves Company Estimates (MWe)	Mean Reserves GeothermEX Estimates (MWe)
Greater Tongonan (Leyte)	686	772
Mindanao	154	456
Bacon-Manito (Luzon)	270	415
Palinpinon (Negros Oriental)	217	411
Northern Negros	47	103
Total	1,374	2,157

Source: GeothermEX Report, October 2008

40. **Financial Risk Management Objectives and Policies**

The Company's financial instruments consist mainly of cash and cash equivalents, AFS investments, and long-term debt. The main purpose of these financial instruments is to finance the Company's operations and accordingly manage its exposure to financial risks. The Company has various financial assets and liabilities such as trade receivables, concession receivables, trade payables and other liabilities, which arise directly from operations.

Overview of the Company's Risk Management

The Company has an Enterprise Wide Risk Management (EWRM) process in place covering all areas of its organization. EWRM is a process, approved by the Company's BOD, and is applied in strategy setting and across the enterprise, designed to identify potential events that may affect the Company and manage risks to be within its risk appetite and to provide reasonable assurance with



respect to the achievement of Company objectives. In addition, EWRM is a holistic approach to the protection of assets, revenues, liabilities, personnel and reputation against predictable and unpredictable losses to achieve maximum efficiency at minimum costs.

The implementation of the Company's EWRM Program provides the following benefits and advantages:

- a. Provides balance in the management of risks.
- b. Identifies and manages the key exposures of the Company proactively.
- c. Establishes the accountability of the proper risk owner(s) in the management of the risks.
- d. Ensures that efforts are well-coordinated so that the Company does not manage risks in silo.
- e. Monitors the effectiveness of the mitigation strategies.
- f. Ensures compliance with the policies and processes that are established to manage risks.
- g. Provides a systematic approach to the management of risks in terms of fortuitous events or accidental losses happening, as well as the attainment of incremental economic benefits that can be derived from the effective management of the Company's risks.
- h. Aims to protect corporate assets and profits by identifying and preventing risks before they occur.
- i. It is designed to avoid losses which can impair the operations or financial position of the company in case of the occurrence of fortuitous events.
- j. Reduces the reliance on increasingly expensive insurance protection. Insurance may provide the financial relief in case of loss. However, certain risks are not insurable, while some though insurable, may be too costly and uneconomical to insure.

Risk Management Oversight Structure

The Risk Management Oversight Structure of the Company has been created based on the current organization set-up. The salient points regarding the said oversight structure are as follows:

- The Risk Management Committee (RMC) is a sub-committee of the BOD to whom it reports directly. The RMC plays a vital oversight role in the implementation of the Company's EWRM Program and is also an important liaison to the BOD. The RMC shall assist the BOD of the Company in its oversight responsibility of managing risks involving physical, financial, operational, labor, legal, security, environmental and other risks of the corporation.
- The Risk Management Executive Committee (RMEC) is comprised of the President, who is the Chairman of the RMEC, the Vice President (VP) for Operations, VP for Corporate Services, VP for Environmental & External Relations, VP for Technical Services and VP for Power Generation. The RMEC shall ensure the effective and efficient implementation of the Company's EWRM Program and provides appropriate actions, solutions and recommendations in line with the requirements of the RMC.
- The Risk Management Group (RMG) is composed of the Property Management Department, the over-all coordinator of the RMG, and the Risk Management Units (RMU), i.e. the different divisions/departments and project sites of the Company. Each RMU is represented in the Company's EWRM Program through their respective Risk Management Coordinators. One of the senior managers of the supply chain sector is the head of RMG. The RMG shall develop, implement and manage the Risk Management Program of the Company in



accordance with the risk management policies and standards set by the Company. The RMG, as the technical working group, shall also assist the RMEC and the RMC attain and perform their missions and functions.

Risk Management Process

The Company's Risk Management Process is the general guideline that the Company follows in the implementation of its EWRM Program. This involves the following:

- a. Identification of the risk exposures;
- b. Formulation of the customized definitions of all risks;
- c. Validation of the customized risk;
- d. Facilitation of the initial prioritization of the risks and the risk voting to identify top risks;
- e. Determination of the risk owners of the top risks;
- f. Validation of the existence of the top risks;
- g. Endorsement of top risks to the REMC for approval;
- h. Determination of the risk drivers of the top risks including the development of risk management strategies and assessment of EDC's risk management capability;
- i. Secure approval of the RMEC for the proposed strategies;
- j. Develop action plans for the approved risk management strategies;
- k. Implementation of the risk management strategies; and
- l. Continuous monitoring of the risk management performance.

Risk Measurement

Another major step in the Company's Risk Management Process is the Risk Measurement where quantitative or qualitative impact of the risk is determined.

Risk Measurement is the process used to quantitatively or qualitatively determine the consequences (including financial impact) of possible outcome or events over a given time horizon under alternative scenarios. The risk measurement process provides information for more informed decision-making.

Risk Management Strategy

The Company uses the risk management option model in its Risk Management Strategy formulation. This model involves whether to accept or reject the risk identified based on the risk management process. When the risk is accepted, the Company chooses the following alternatives: retain, reduce, exploit, modify time and wait and see. When the risk is rejected, the Company may opt to avoid or transfer the risk.

Financial Risk Management Policy

The main risks arising from the Company's financial instruments are credit and credit concentration risk, interest rate risk, liquidity risk, and foreign currency risk. The Company's policies for managing the aforementioned risks are summarized hereinafter.

Credit Risk and Credit Concentration

The Company's geothermal and power generation business trades with only one major customer, NPC, a government-owned-and-controlled corporation. Any failure on the part of NPC to pay its obligations to the Company would significantly affect the Company's business operations. As a practice, the Company monitors closely its collection from NPC and charges interest on delayed payments following the provision of its respective SSAs and PPAs. Receivable balances are



monitored on an ongoing basis to ensure that the Company's exposure to bad debts is not significant. The maximum exposure of trade receivable is equal to the carrying amount.

With respect to credit risk arising from other financial assets of the Company, which comprise of cash and cash equivalents excluding cash on hand, other receivables, AFS investments, derivative assets, concession receivable, cash collateral on PCIR Bonds, due from related parties and deferred royalty fee, the Company's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

	2008	2007
Loans and receivables:		
Cash and cash equivalents	₱769,817,417	₱2,793,993,755
Trade receivables - net	4,648,308,335	4,297,224,927
Non-trade receivables	232,317,043	517,499,843
Loans and notes receivables	60,350,973	54,453,890
Employee receivables	30,096,534	26,393,358
Advances to employees	26,724,217	22,531,712
Long-term receivables - net	819,861,389	74,444,550
Concession receivable	34,695,434,198	36,895,420,525
Cash collateral on PCIR Bonds	3,519,226	3,066,807
Royalty fee chargeable to NPC	122,018,657	464,520,286
Due from a related party	95,475,959	-
AFS investments:		
Debt investments	674,494,128	1,177,589,987
Equity investments	13,597,238	16,410,656
Financial asset at FVPL:		
Range bonus forwards	614,081,623	-
	₱42,806,096,937	₱46,343,550,296

The Company trades only with recognized, creditworthy third parties and/or transacts only with institutions and/or banks which have demonstrated financial soundness and which have passed the financial evaluation and accreditation of the Company.

The table below shows the Company's aging analysis of past due but not impaired receivables as of December 31, 2008 and 2007:

	2008						Total
	Neither Past Due nor Impaired	Past Due but Not Impaired				Past Due and Impaired	
		Less than 30 Days	31 Days to 1 Year	Over 1 Year up to 3 Years	Over 3 Years		
<i>(In Thousand Pesos)</i>							
Loans and receivables:							
Cash and cash equivalents	₱769,817	₱-	₱-	₱-	₱-	₱-	₱769,817
Trade receivables	4,641,432	-	6,876	-	-	2,182	4,650,490
Non-trade receivables	222,012	4,974	5,274	-	57	-	232,317
Loans and notes receivables	51,814	221	7,474	551	291	-	60,351
Employee receivables	30,005	-	82	10	-	-	30,097

(Forward)



2008							
	Neither Past Due nor Impaired	Past Due but Not Impaired				Past Due and Impaired	Total
		Less than 30 Days	31 Days to 1 Year	Over 1 Year up to 3 Years	Over 3 Years		
<i>(In Thousand Pesos)</i>							
Advances to employees	₱14,925	₱5,550	₱5,860	₱389	₱-	₱-	₱26,724
Long-term receivables	819,861	-	-	-	-	66,304	886,165
Concession receivable	34,695,434	-	-	-	-	-	34,695,434
Cash collateral on PCIR Bonds	3,519	-	-	-	-	-	3,519
Royalty fee chargeable to NPC	122,019	-	-	-	-	-	122,019
Due from a related party	95,476	-	-	-	-	-	95,476
AFS investments:							
Debt investments	674,494	-	-	-	-	-	674,494
Equity investments	13,597	-	-	-	-	-	13,597
Financial asset at FVPL:							
Range bonus forwards	614,082	-	-	-	-	-	614,082
Total	₱42,768,487	₱10,745	₱25,566	₱950	₱348	₱68,486	₱42,874,582

2007							
	Neither Past Due Nor Impaired	Past Due but Not Impaired				Past Due and Impaired	Total
		Less than 30 Days	31 Days to 1 Year	Over 1 Year up to 3 Years	Over 3 Years		
<i>(In Thousand Pesos)</i>							
Loans and receivables:							
Cash and cash equivalents	₱2,793,994	₱-	₱-	₱-	₱-	₱-	₱2,793,994
Trade receivables	4,228,325	45,380	23,520	-	-	377,219	4,674,444
Non-trade receivables	95,524	-	421,976	-	-	-	517,500
Loans and notes receivables	51,831	-	2,205	376	41	-	54,453
Employee receivables	25,593	-	-	800	-	-	26,393
Advances to employees	19,596	-	2,640	296	-	-	22,532
Long-term receivables	-	-	-	31,000	43,445	1,012,612	1,087,057
Concession receivable	36,895,421	-	-	-	-	-	36,895,421
Cash collateral on PCIR Bonds	3,067	-	-	-	-	-	3,067
Royalty fee chargeable to NPC	464,520	-	-	-	-	-	464,520
AFS investments:							
Debt investments	1,177,590	-	-	-	-	-	1,177,590
Equity investments	16,411	-	-	-	-	-	16,411
Total	₱45,771,872	₱45,380	₱450,341	₱32,472	₱43,486	₱1,389,831	₱47,733,382

Credit Quality of Neither Past Due nor Impaired Financial Assets

Financial assets are classified as high grade if the counterparties are not expected to default in settling their obligations. Thus, the credit risk exposure is minimal. These counterparties normally include customers, banks and related parties who pay on or before due date. Financial assets are classified as a standard grade if the counterparties settle their obligation with the Company with tolerable delays. Low grade accounts are accounts, which have probability of impairment based on historical trend. These accounts show propensity to default in payment despite regular follow-up actions and extended payment terms.



As of December 31, 2008, financial assets categorized as neither past due nor impaired are viewed by management as high grade considering the collectability of the receivables and the credit history of the counterparties.

Foreign Currency Risk

The Company's exposure to foreign currency risk resulted from the financial assets and liabilities that are denominated in U.S. dollar and Japanese yen. This primarily arise from future payments of foreign loans, BOT lease obligation and other commercial transactions and the Company's investment in ROP Bonds.

The Company's exposure to foreign currency risk to some degree is mitigated by some provisions in the Company's GSCs, SSAs and PPAs. The service contracts allow full cost recovery while the sales contracts include billing adjustments covering the movements in Philippine peso and the US dollar rates, US Price and Consumer Indices, and other inflation factors.

To mitigate further the effects of foreign currency risk, the Company will prepay, refinance or hedge its foreign currency denominated loans, whenever deemed feasible. During 2008, the Company entered into derivative contracts with various counterparties to minimize the foreign currency risk from its Miyazawa 1 loan.

The Company's foreign currency-denominated financial assets and liabilities (translated into Philippine peso) as of December 31, 2008 are as follows:

	2008			2007		
	Original Currency		Peso Equivalent ¹	Original Currency		Peso Equivalent ²
	Yen	US Dollar		Yen	US Dollar	
Financial Assets						
Loans and receivables:						
Cash equivalents	–	14,769,052	701,825,372	–	2,757,445	114,188,538
Cash on hand and in banks	386,027	241,864	11,876,109	6,458,189	65,265	5,055,106
Trade and other receivables	–	2,442,801	116,081,918	–	1,151,599	49,294,872
Cash collateral on PCIR Bonds	–	74,058	3,519,226	–	74,058	3,066,807
AFS investments:						
Government debt securities	–	14,193,900	674,494,128	–	28,436,647	1,177,589,987
Financial asset at FVPL:						
Derivative assets	–	12,922,593	614,081,623	–	–	–
Total financial assets	386,027	44,644,268	2,121,878,376	6,458,189	32,485,014	1,349,195,310
Current Financial Liabilities						
Liabilities at amortized cost:						
Trade and other payables	390,442,807	9,456,709	614,247,441	–	1,817,746	75,274,681
Current portion of interest-bearing financial liabilities	13,856,808,675	20,552,540	8,217,253,830	1,868,893,372	23,481,930	1,653,156,788
Current portion of obligation to a power plant contractor	–	2,360,847	112,187,446	–	5,957,818	246,719,220
Financial liability at FVPL:						
Derivative liabilities	–	1,110,992	54,250,018	–	–	–
Total current financial liabilities	14,247,251,482	33,481,088	8,997,938,735	1,868,893,372	31,257,494	1,975,150,689



	2008			2007		
	Original Currency		Peso Equivalent ¹	Original Currency		Peso Equivalent ²
	Yen	US Dollar		Yen	US Dollar	
Noncurrent Financial Liabilities						
Liabilities at amortized cost:						
Interest-bearing financial liabilities - net of current portion	35,123,058,752	57,806,141	21,099,796,908	48,535,148,611	75,606,900	20,809,947,547
Obligations to a power plant contractor - net of current portion	-	-	-	-	2,325,165	96,287,392
Total noncurrent financial liabilities	35,123,058,752	57,806,141	21,099,796,908	48,535,148,611	77,932,065	20,906,234,939
Total financial liabilities	49,370,310,234	91,287,229	30,097,735,643	50,404,041,983	109,189,559	22,881,385,628

¹USD1=JPY90.942 and USD1= P47.520

²USD1=JPY113.688 and USD1= P41.411

The following tables demonstrate the sensitivity to a reasonably possible change in the U.S. dollar and Japanese yen exchange rates, with all other variables held constant, of the Company's profit before tax as at December 31, 2008 and 2007 (arising from revaluation of monetary assets and liabilities and derivative instruments).

2008		
	Foreign Currency Appreciates (Depreciates) By	Effect on Profit Before Tax
USD	5% or PHP2.376 (5% or PHP2.376)	(P108,093,964) 41,535,990
JPY	5% or PHP0.02488 (5% or PHP0.02750)	(1,061,867,588) 1,204,896,251
2007		
	Foreign Currency Appreciates (Depreciates) By	Effect on Profit Before Tax
USD	5% or PHP2.071 (5% or PHP2.071)	(P158,855,113) 158,855,113
JPY	5% or PHP0.01735 (5% or PHP0.01917)	(874,398,079) 966,121,681

Equity Price Risk

Equity price risk is the risk that the fair value of traded equity instruments decrease as the result of the changes in the levels of equity indices and the value of the individual stocks.

As of December 31, 2008 and 2007, the Company's exposure to equity price risk is minimal since quoted AFS investments in equity securities are immaterial.

Interest Rate Risk

The Company's exposure to the risk of changes in market interest rates relates primarily to the Company's long-term debt obligations with floating interest rates and AFS investments.

The interest rates of some of the Company's long-term borrowings, AFS debt investments and finance leases (to which the Company is a lessee) are fixed at the inception of the loan agreement and/or lease.



The Company regularly evaluates its interest rate risk by taking into account the cost of qualified borrowings being charged by its creditors. Prepayment, refinancing or hedging the risks are undertaken when deemed feasible and advantageous to the Company.

The following tables demonstrate the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Company's profit before tax and equity as of December 31, 2008 and 2007. The effect also includes impact of change in interest rate on derivatives.

2008			
	Increase/Decrease in Basis Points	Effect on Profit Before Tax	Effect on Equity
PHP	+100	₱5,027,101	₱-
	-100	(3,654,973)	-
USD	+100	(49,671,451)	(26,692,263)
	-100	30,682,513	29,948,351
JPY	+100	(41,161,399)	-
	-100	38,502,825	-

2007			
	Increase/Decrease in Basis Points	Effect on Profit Before Tax	Effect on Equity
PHP	+100	(₱1,845,392)	₱-
	-100	1,845,392	-
USD	+100	(38,735,880)	(39,037,640)
	-100	38,735,880	39,037,640
JPY	+100	(24,769,080)	-
	-100	24,769,080	-

Interest Rate Risk Table

Set out below is the scheduled interest payments from the Company's long-term debt.

	Interest Rates	Within 1 Year	2-3 Years	4-5 Years	More than 5 Years	Total
2008 Fixed Rate						
Long-term debt:						
	OECF 3% - 5.7%	₱80,125,182	₱72,791,485	₱12,616,304	₱30,880,143	₱196,413,114
	JEXIM ^(a) 3747 3.5%	39,312,925	31,753,377	-	-	71,066,302
	JBIC ^(b) 21 st yen 2.3% & 2.7%	130,228,204	239,046,620	210,803,299	674,642,893	1,254,721,016
	Miyazawa I 2.62% & 3.78%	98,019,103	-	-	-	98,019,103
	Miyazawa II 2.37%	272,449,143	136,224,572	-	-	408,673,715
2008 Floating Rate						
Long-term debt:						
	IBRD 7.07%	243,635,506	158,627,319	-	-	402,262,825
2007 Fixed Rate						
Long-term debt:						
	OECF 3% - 5.7%	₱68,166,832	₱99,590,277	₱62,390,773	₱99,945,342	₱330,093,224
	JEXIM ^(a) 3747 3.5%	32,908,255	49,539,731	28,496,765	7,590,775	118,535,526
	JBIC ^(b) 21 st yen 2.3% & 2.7%	96,021,646	176,587,145	156,898,959	541,169,536	970,677,286
	Miyazawa I 2.62% & 3.78%	137,644,691	68,452,839	-	-	206,097,530
	Miyazawa II 2.37%	189,922,044	284,883,066	-	-	474,805,110
2007 Floating Rate						
Long-term debt:						
	IBRD 6.09%	239,231,613	278,604,341	127,173,198	28,645,948	673,655,100

(a) The Export - Import Bank of Japan

(b) Japan Bank for International Cooperation



Liquidity Risk

The Company's objective is to maintain a balance between continuity of funding and sourcing flexibility through the use of available financial instruments. The Company manages its liquidity profile to meet its working and capital expenditure requirements and service debt obligations. As part of the liquidity risk management program, the Company regularly evaluates and considers the maturity of both its financial investments and financial assets (e.g. trade receivables, other financial assets) and resorts to short-term borrowings whenever its available cash or matured placements is not enough to meet its daily working capital requirements. To ensure immediate availability of short-term borrowings, the company maintains credit lines with banks on a continuing basis.

Liquidity risk arises primarily when the Company has difficulty collecting its receivables from its major customer, NPC. Other instances that contribute to its exposure to liquidity risk are when the Company finances long-term projects with internal cash generation and when there is a credit crunch especially at times when the Company has temporary funding gaps.

The table below summarizes the maturity analysis of the Company's financial liabilities at December 31, 2008 based on contractual undiscounted payments:

	2008						Total
	On Demand	Less than 3 Months	3 to 6 Months	6 to 12 Months	1 to 5 Years	More than 5 Years	
<i>(In Thousand Pesos)</i>							
Liabilities at amortized cost:							
Accounts payable - trade	₱-	₱1,477,367	₱-	₱-	₱-	₱-	₱1,477,367
Accrued interest and guarantee fees	-	347,876	-	-	-	-	347,876
Accrued premium on range bonus forwards	-	-	175,116	-	-	-	175,116
Other current liabilities	-	8,649	-	-	-	-	8,649
Loan payable	-	34,500	33,750	2,066,750	-	-	2,135,000
Due to a related party	-	47,213	-	-	-	-	47,213
Royalty fee payable	-	1,688,282	-	-	-	-	1,688,282
Obligations to a power plant contractor	-	61,011	54,140	-	-	-	115,151
Long-term debt	-	532,144	7,315,727	1,453,711	18,595,758	4,025,796	31,923,136
Financial liability at FVPL:							
Derivative liabilities	-	-	54,250	-	-	-	54,250
Total	₱-	₱4,197,042	₱7,632,983	₱3,520,461	₱18,595,758	₱4,025,796	₱37,972,040

	2007						Total
	On Demand	Less than 3 Months	3 to 6 Months	6 to 12 Months	1 to 5 Years	More than 5 Years	
<i>(In Thousand Pesos)</i>							
Liabilities at amortized cost:							
Accounts payable - trade	₱-	₱1,422,651	₱604,431	₱411	₱-	₱-	₱2,027,493
Accrued interest and guarantee fees	-	139,924	-	-	-	-	139,924
Other current liabilities	-	3,827	-	-	-	-	3,827
Royalty fee payable	-	306,274	50,000	100,000	1,503,244	-	1,959,518
Obligations to a power plant contractor	-	66,436	66,436	132,872	100,348	-	366,092
Long-term debt	-	264,201	1,425,032	1,305,986	19,906,853	3,113,768	26,015,840
Total	₱-	₱2,203,313	₱2,145,899	₱1,539,269	₱21,510,445	₱3,113,768	₱30,512,694



Financial Assets and Financial Liabilities

Set out below is a comparison of carrying amounts and fair values of the Company's financial instruments as of December 31, 2008 and 2007.

	2008		2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets				
Loans and receivables:				
Cash and cash equivalents	₱773,817,457	₱773,817,457	₱2,797,581,577	₱2,797,581,577
Trade receivables - net	4,648,308,335	4,648,308,335	4,297,224,927	4,297,224,927
Non-trade receivables	232,317,043	232,317,043	517,499,843	517,499,843
Loans and notes receivables	60,350,973	60,350,973	54,453,890	54,453,890
Employee receivables	30,096,534	30,096,534	26,393,358	26,393,358
Advances to employees	26,724,217	26,724,217	22,531,712	22,531,712
Long-term receivables - net	819,861,389	838,203,873	74,444,550	70,097,825
Concession receivable	34,695,434,198	30,995,036,175	36,895,420,525	33,836,177,796
Cash collateral on PCIR Bonds	3,519,226	3,519,226	3,066,807	3,066,807
Royalty fee chargeable to NPC	122,018,657	122,018,657	464,520,286	464,520,286
Due from related parties	95,475,959	95,475,959	-	-
AFS investments:				
Debt investments	674,494,128	674,494,128	1,177,589,987	1,177,589,987
Equity investments	13,597,238	13,597,238	16,410,656	16,410,656
Financial assets at FVPL:				
Derivative assets	614,081,623	614,081,623	-	-
	₱42,810,096,977	₱39,128,041,438	₱46,347,138,118	₱43,283,548,664
Financial Liabilities				
Liabilities at amortized cost:				
Accounts payable - trade	₱1,477,366,593	₱1,477,366,593	₱2,027,492,672	₱2,027,492,672
Accrued interest and guarantee fees	347,876,055	347,876,055	139,924,021	139,924,021
Accrued premium on range bonus forwards	175,116,194	175,116,194	-	-
Other current liabilities	8,649,387	8,649,387	3,826,743	3,826,743
Loan payable	2,000,000,000	2,000,000,000	-	-
Due to related party	47,213,065	47,213,065	-	-
Royalty fee payable	1,688,282,467	1,688,282,467	1,733,927,164	2,083,225,515
Obligations to a power plant contractor	112,187,446	111,720,404	343,006,612	332,043,695
Long-term debt	29,317,050,738	30,897,737,515	22,841,513,426	21,231,466,800
Financial liabilities at FVPL:				
Derivative liabilities	54,250,018	54,250,018	-	-
	₱35,227,991,963	₱36,808,211,698	₱27,089,690,638	₱25,817,979,446

The methods and assumptions used by the Company in estimating the fair value of financial instruments are:

Cash and Cash Equivalents. Carrying amounts approximate fair values due to its short-term nature.

Trade and Other Receivables, Due to/from a Related Party, Cash Collateral on PCIR Bonds, Royalt Fee Payable to NPC, Trade and Other Payables and Loan Payable. These are instruments with relatively short maturity ranging 1 to 3 months. Carrying amounts approximate fair values.



Long-term Receivables. The fair value of long-term receivables was computed by discounting the expected cash flow using the applicable rate of 6.08% to 6.59% and 5.59% to 5.71% in 2008 and 2007, respectively.

Concession Receivable. The fair value of concession receivables is computed by discounting the expected free cash flows using the applicable rates as of balance sheet dates ranging from 5.26% to 15.03% and 4.01% to 9.21% in 2008 and 2007, respectively.

AFS Investments. Fair values of debt securities are based on quoted market prices. For equity investments that are not quoted, the investments are carried at cost less allowance for impairment losses due to the unpredictable nature of future cash flows and the lack of suitable methods of arriving at a reliable fair value.

Derivative Assets and Liabilities. Fair values are determined by reference to market values for similar instruments as provided by counterparty banks.

Long-term Debt and Royalty Fee Payable. Fair values for long-term debt are estimated using the discounted cash flow methodology using the Company's current incremental borrowing rates ranging from 0.49% to 1.61% in 2008. Fair value of royalty fee payable approximates the carrying value in 2008 while in 2007 its fair value was determined using discount rates ranging from 5.84% to 6.48%.

Obligations to a Power Plant Contractor. The fair value of obligations to a power plant contractor represents the present value of the expected future cash flows of the liability using the applicable rates at balance sheet date ranging from 0.86% to 1.65% and 4.35% to 4.92% in 2008 and 2007, respectively.

The Company classifies its financial instruments in the following categories.

2008						
	Loans and Receivables	AFS	Financial Assets at FVPL	Liabilities at Amortized Cost	Financial Liabilities at FVPL	Total
<i>(In Thousands)</i>						
Financial Assets						
Cash and cash equivalents	₱773,817	₱-	₱-	₱-	₱-	₱773,817
Trade receivables - net	4,648,308	-	-	-	-	4,648,308
Non-trade receivables	232,317	-	-	-	-	232,317
Loans and notes receivables	60,351	-	-	-	-	60,351
Employee receivables	30,097	-	-	-	-	30,097
Advances to employees	26,724	-	-	-	-	26,724
Long-term receivables - net	819,861	-	-	-	-	819,861
Concession receivable	34,695,434	-	-	-	-	34,695,434
Cash collateral on PCIR Bonds	3,519	-	-	-	-	3,519
Royalty fee chargeable to NPC	122,019	-	-	-	-	122,019
Due from a related party	95,476	-	-	-	-	95,476
AFS - debt investments	-	674,494	-	-	-	674,494
AFS - equity investments	-	13,597	-	-	-	13,597
Derivative financial asset	-	-	614,082	-	-	614,082
Financial Liabilities						
Accounts payable - trade	-	-	-	1,477,367	-	1,477,367
Accrued interest and guarantee fees	-	-	-	347,876	-	347,876
Accrued premium on range bonus forwards	-	-	-	175,116	-	175,116

(Forward)



2008						
	Loans and Receivables	AFS	Financial Assets at FVPL	Liabilities at Amortized Cost	Financial Liabilities at FVPL	Total
<i>(In Thousands)</i>						
Other current liabilities	₱-	₱-	₱-	₱8,649	₱-	₱8,649
Loan payable	-	-	-	2,000,000	-	2,000,000
Due to a related party	-	-	-	47,213	-	47,213
Royalty fee payable	-	-	-	1,688,282	-	1,688,282
Obligations to a power plant contractor	-	-	-	112,187	-	112,187
Long-term debt	-	-	-	29,317,051	-	29,317,051
Derivative financial liabilities	-	-	-	-	54,250	54,250
Total	₱41,507,923	₱688,091	₱614,082	₱35,173,741	₱54,250	₱78,038,087

2007						
	Loans and Receivables	AFS	Financial Assets at FVPL	Liabilities at Amortized Cost	Financial Liabilities at FVPL	Total
<i>(In Thousands)</i>						
Financial Assets						
Cash and cash equivalents	₱2,797,582	₱-	₱-	₱-	₱-	₱2,797,582
Trade receivables	4,297,225	-	-	-	-	4,297,225
Non-trade receivables	517,500	-	-	-	-	517,500
Loans and notes receivables	54,454	-	-	-	-	54,454
Employee receivables	26,393	-	-	-	-	26,393
Advances to employees	22,532	-	-	-	-	22,532
Long-term receivables	74,445	-	-	-	-	74,445
Concession receivable	36,895,421	-	-	-	-	36,895,421
Cash collateral on PCIR Bonds	3,067	-	-	-	-	3,067
Royalty fee chargeable to NPC	464,520	-	-	-	-	464,520
AFS - debt investments	-	1,177,590	-	-	-	1,177,590
AFS - equity investments	-	16,411	-	-	-	16,411
Financial Liabilities						
Accounts payable - trade	-	-	-	2,027,493	-	2,027,493
Accrued interest and guarantee fees	-	-	-	139,924	-	139,924
Other current liabilities	-	-	-	3,827	-	3,827
Royalty fee payable	-	-	-	1,733,927	-	1,733,927
Obligations to a power plant contractor	-	-	-	343,007	-	343,007
Long-term debt	-	-	-	22,841,513	-	22,841,513
Total	₱45,153,139	₱1,194,001	₱-	₱27,089,691	₱-	₱73,436,831

The table below demonstrates the income, expense, gains or losses of the Company's financial instruments for the years ended December 31, 2008 and 2007:

	2008		2007	
	Effect in Profit or Loss Increase (Decrease)	Effect in Equity Increase (Decrease)	Effect in Profit or Loss Increase (Decrease)	Effect in Equity Increase (Decrease)
Loans and receivables:				
Interest income on cash in bank	₱1,917,865	₱-	₱1,006,736	₱-
Interest income on cash equivalents	207,821,886	-	302,802,941	-
Interest income on trade receivables	108,113,195	-	-	-

(Forward)



	2008		2007	
	Effect in Profit or Loss Increase (Decrease)	Effect in Equity Increase (Decrease)	Effect in Profit or Loss Increase (Decrease)	Effect in Equity Increase (Decrease)
Interest income on due from a related party	₱261,069	₱-	₱-	₱-
Interest income on concession receivables	2,107,841,224	-	2,236,906,585	-
Interest income on other receivables	1,995,342	-	673,975	-
Interest income on employees receivable	381,892	-	-	-
“Day 1” loss on NPC receivable	(189,790,628)	-	-	-
AFS investments:				
Equity investments:				
Net gain (loss) recognized in equity	-	(2,813,418)	-	4,263,827
Debt investments:				
Gain on sale of AFS investments	46,323,392	-	7,937,724	-
Net gain removed from equity	-	(46,323,392)	-	(7,937,724)
Net gain (loss) recognized in equity	-	(288,586,089)	-	240,760,339
Interest income on ROP Bonds	842,697	-	-	-
Financial assets at FVPL:				
Realized gain	-	-	56,011,571	-
Realized loss	(175,116,193)	-	-	-
Unrealized loss on fair value changes	(54,250,018)	-	-	-
Unrealized gain on fair value changes	614,081,623	-	-	-
Financial liabilities at amortized cost:				
Interest expense on long-term loans	(1,415,922,326)	-	(1,137,402,501)	-
Interest accretion of “Day 1” gain on royalty payable	(225,590,774)	-	(211,445,798)	-
Interest expense on loan payable	(34,535,508)	-	(51,799)	-
Amortization of transaction costs on loans	(120,834,470)	-	(218,138,637)	-
“Day 1” gain on royalty fee payable	-	-	39,769,241	-
	₱873,540,268	(₱337,722,899)	₱1,078,070,038	₱237,086,442



Capital Management

The primary objective of the Company's capital management is to ensure that it maintains a healthy capital ratio in order to comply with its financial loan covenants and support its business operations.

The Company manages and makes adjustment to its capital structure as it deems necessary. To maintain or adjust its capital structure, the Company may increase the levels of capital contributions from its creditors and owners/shareholders through debt and new shares issuance, respectively.

The Company monitors capital using the debt ratio, which is long-term liabilities divided by long-term liabilities plus equity. The Company's policy is to keep the debt ratio not more than 70:30. The Company's long-term liabilities include both the current and long-term portions of obligations to a power plant contractor and long-term debt. Equity includes capital stock attributable to common and preferred shares, unrealized gains reserve and retained earnings.

Table below shows the Company's debt ratio as at December 31, 2008 and 2007.

	2008	2007
Long-term liabilities	₱29,429,238,184	₱23,184,520,038
Equity	30,861,044,922	34,853,280,606
Debt ratio	48.8%	39.9%

Derivative Financial Instruments

The Company's freestanding derivative financial instruments are accounted for as financial instruments at FVPL. The table below shows the fair value of derivative financial instruments, reported as current assets or liabilities, together with their notional amounts as of December 31, 2008. The notional amount is the basis upon which changes in the value of derivatives are measured. The Company has no outstanding derivatives as of December 31, 2007.

	Derivative Assets	Derivative Liabilities	Notional Amount
Freestanding Derivatives:			
Range bonus forwards	₱614,018,623	₱-	JPY 8 Billion
Currency forwards	-	54,250,018	USD 100 Million
Total Derivatives	₱614,018,623	₱54,250,018	

Freestanding Derivatives. The Company entered into derivative transactions to hedge the foreign currency exposure arising from its foreign currency denominated loan contracts, particularly the maturing Miyazawa 1 loan. As of December 31, 2008, the Company has positions in the following types of freestanding derivatives to protect itself against foreign currency risk arising from the changes in the exchange rate of the peso in relation to the foreign currency:



Foreign Currency Forward Contract. Foreign currency forward contracts are contractual agreements to buy or sell a foreign currency at an agreed rate on a future date. These are contracts that are customized and transacted with a bank or financial institution.

In 2008, the Company entered into nine foreign currency forward contracts with various counterparty banks maturing on May 28, 2009. The Company's outstanding deliverable buy Dollar and sell Peso forward exchange contracts as of December 31, 2008 have an aggregate notional amount of \$100.00 million. The weighted average forward rate of the outstanding forward exchange rates is ₱48.71 to US\$1. As of December 31, 2008, the unrealized mark-to-market loss recognized from these contracts amounted to ₱54.25 million.

Range Bonus Forward Contract. A Range Bonus forward contract is an agreement that provides protection against unfavorable exchange rate movement by setting an agreed rate at which the Company can exchange one currency for another. At the same time, it provides that for each day during the fixing period that the spot rate is outside the predetermined range, the Company will accrue a premium based on a specified formula, which is payable at maturity.

The following table shows the relevant data with the corresponding unrealized gain pertaining to the two range bonus forward contracts entered into by the Company for the Miyazawa 1 loan, which will mature in June 2009:

Notional Amount	JPY 5 Billion	JPY 3 Billion
Trade date	April 30, 2008	May 2, 2008
Expiry date	May 26, 2009	May 26, 2009
Delivery date	May 28, 2009	May 28, 2009
Agreed rate	110	110
Premium formula (where n = number of days when the spot rate is outside the predetermined range during the fixing period and N = fixing period)	USD47,846,890 x 13.40% x n/N	USD28,571,428.57 x 13.06% x n/N
Predetermined range	JPY96-JPY106	JPY97-JPY107
Fixing period (in days)	260	258
Unrealized marked to market gain	₱384,658,412	₱229,423,211

As of December 31, 2008, the total accrued premium payable for the JPY5 billion and JPY3 billion range bonus forward amounted to ₱116.01 million and ₱59.11 million, respectively, based on the total number of days, of 99 and 86 days, that the spot rate is outside the predetermined ranges. The said amounts are included under trade and other payables in the 2008 parent company balance sheet.

Embedded Derivatives. The Company has financial and non-financial contracts with derivatives embedded in them. These embedded derivatives have the effect that some of the cash flows of the financial and non-financial contracts vary in a similar way to a freestanding derivative.



Prepayment Options. Embedded prepayment (call) options were bifurcated from the USD90 million ING syndicated loan which matured in February 2007 and USD75 million Standard Chartered term loan which was scheduled to mature in August 2009. In 2007, the embedded prepayment option on the USD75 million Standard Chartered loan was exercised by the Company.

Fair Value Changes of Derivatives

The tables below summarize the net movement in fair values of the Company's derivatives as of December 31, 2008.

Net Derivative Assets	2008	2007
Balance at beginning of year	₱-	₱344,000,987
Net changes in fair value during the year	559,831,605	56,011,571
Settled during the year	-	(400,012,558)
Balance at end of year	₱559,831,605	₱-
Presented as:		
Derivative assets	₱614,081,623	₱-
Derivative liabilities	54,250,018	-

The net changes in fair value of the Company's derivative during the year were taken into "Derivatives gain - net" account in the parent company statements of income, net of accrued premium range bonus forwards.

41. **Commitments and Contingencies**

Stored Energy

On various dates, the Company entered into Addendum Agreements to the PPA for the Unified Leyte and GRSC for BacMan 2 projects, where any excess generation above the nominated energy or take-or-pay volume will be credited against payments made by NPC for the periods it was not able to take electricity or steam, where applicable. As of December 31, 2008, the commitments for stored energy are as follows in gigawatt-hours:

Plant	Stored energy (in gigawatt-hours)
Unified Leyte	4,326.6
BacMan 2 - Cawayan	437.9

Lease Commitments

Company as a Lessee. Future minimum lease payments under the operating leases are as follows:

	Amount
Within one year	₱10,260,761
After one year but not more than five years	989,151
Total	₱11,249,912



The Company's lease commitments pertained to drilling rig and various office and warehouse rentals.

Under the terms and conditions governing the rig lease agreement with PNOC Exploration Corporation, the Company shall use the Kremco 750T drilling rig for the Lihir Island Drilling Project with an operating rental rate of USD 1,680/day. The agreement took effect last March 1, 2008 and shall terminate on the rig release time of the last well.

Company as a Lessor. The Company leases to PNOC Exploration Corporation the lot occupied by Buildings 1 & 2 as well as the office spaces of Building 2 located at Energy Center, Merritt Road, Fort Bonifacio, Taguig City at a total annual rental of ₱2.70 million. The contract is renewable annually.

Purchase Commitments

Total purchase commitments for capital items as of December 31, 2008 and 2007 year amounted to ₱904.3 million and ₱27.36 million, respectively.

Legal Claims

The Company is contingently liable for lawsuits or claims filed by third parties, including labor related cases, which are pending decision by the courts, the outcomes of which are not presently determinable. In the opinion of management and its legal counsel, the eventual total liability from these lawsuits or claims, if any, will not have a material effect on the parent company financial statements.

42. Events after the Balance Sheet Date

Proceeds of Loan from International Finance Corporation (IFC)

The Company entered into a loan agreement with IFC, a shareholder of the Company, on November 27, 2008 for US\$100.0 million or its peso equivalent. On January 7, 2009, the Company received the proceeds of the loan amounting to ₱4,048.75 million, net of ₱51.25 million front-end fee. The loan is payable in 24 equal semi-annual installments after a three-year grace period at an interest rate of 7.4% per annum for the first five years subject to re-pricing for another five to 10 years.

Amendment of the Share Buy-back Program

On January 23, 2009, the BOD approved an amendment to the Company's share buy-back program, to include, not only the previously stated objective of acquiring shares to implement the proposed executive/employee stock ownership plan, but also for the purpose of enhancing shareholder value whenever the stock is trading at a price discount to its true valuation.

The share buy-back program will be implemented through grants, options, purchases or other equivalent methods.

The maximum amount approved for the buy-back program remains at ₱4.0 billion, which may be carried out over a two-year period from March 26, 2008 to March 25, 2010 at the discretion of management. As of December 31, 2008, the total number of treasury shares was 93,000,000 (see Note 22).



Executive/Employee Stock Ownership Plan

On January 23, 2009, the BOD of the Parent Company approved the Executive/Employee Stock Ownership Plan and the related rules, specifically on stock grant. The plan is an integral part of the Parent Company's rewards program for its employees and it is intended to provide an opportunity for the participants to have real and personal direct interest in the Company. There are no stock awards granted as of March 30, 2009.

Republic Act No. 9513 (RA 9513)

On January 30, 2009, RA 9513, "An Act Promoting the Development, Utilization and Commercialization of Renewable Energy Resources and for Other Purposes," which shall be known as the "Renewable Energy Act of 2008" (the Act), became effective.

RA 9513 aims to accelerate the exploration and development of renewable energy resources as well as to increase the utilization of renewable energy by institutionalizing the development of national and local capabilities in the use of renewable energy systems, and promoting its efficient and cost-effective commercial application by providing fiscal and non-fiscal incentives.

The law also encourages the development and utilization of renewable energy resources as effective tools to prevent or reduce harmful emissions and thereby balancing the goals of economic growth and development with the protection of health and the environment. The Act also intends to establish the necessary infrastructure to carry out the mandates specified in the law and other relevant existing laws.

The Act provides a seven-year income tax holiday and tax exemptions for the carbon credits generated from renewable energy sources. A 10% corporate income tax, as against the regular 30%, is also provided once the income tax holiday expires; energy self-sufficiency to 60% by 2010 from 56.6% in 2005, by tapping resources like solar, wind, hydropower, ocean and biomass energy; renewable energy facilities will also be given a 1.5% realty tax cap on original cost of equipment and facilities to produce renewable energy.

The law also prioritizes the purchase, grid connection and transmission of electricity generated by companies from renewable energy sources and power generated from renewable energy sources will be value added tax-exempt.

Within six (6) months from the effectivity of the Act, the DOE shall, in consultation with the Senate and House of Representatives Committee on Energy, relevant government agencies and renewable energy stakeholders, promulgate the Implementing Rules and Regulations of the Act.

The Company is evaluating the significant impact that the Act may have on the Company's future operations and financial results.

Hedging Transaction

On March 17, 2009, as part of currency risk management, the Company entered into a foreign exchange contract to hedge the remaining JPY 4 billion of the JPY12 billion Miyazawa loan due on June 1, 2009. The strike rate is JPY 98.60 per USD.



Dividend Declaration

On March 30, 2009, the BOD approved the following cash dividends in favor of all stockholders of record as of April 16, 2009 and payable on May 11, 2009:

- Cash dividend of ₱0.0008 per share on the preferred shares totaling ₱6.00 million.
- Regular cash dividend of ₱0.125 per share on the common shares totaling ₱1,863.38 million.

43. Reclassification of Certain 2007 Accounts Presentation

The 2007 amounts were restated to conform to the 2008 parent company financial statement presentation. The affected accounts and the corresponding amounts in the parent company financial statements are described below:

a. 2007 Parent Company Statement of Income

- 1) Reclassification of the breakdown of operations and maintenance expenses (see Note 24) and general and administrative expenses (see Note 25) to align with the 2008 presentation.
- 2) Reclassification of the breakdown of interest expenses (see Note 26) to align with the 2008 presentation.
- 3) Reclassification of deferred tax asset on IFRIC 12 adjustments from deductible expenses per P.D. 1442 in 2007 (see Note 30) to align with the 2008 presentation.

b. 2007 Parent Company Statement of Cash Flows

Account Name	Explanation	Effect on 2007
1) Net cash flows from operating activities	Presented in this section are the payments of royalty, retirement and other post-retirement benefit plan previously reported in the “net cash flows from (used in) financing activities” and the settlement/adjustment of disputed noncurrent receivables taken up in “net cash flows from (used in) investing activities.”	(₱1,163,584,500)
2) Net cash flows from (used in) investing activities	Reclassification to “net cash flows from operating activities.”	363,600,044
3) Net cash flows from (used in) financing activities	Reclassification to “net cash flows from operating activities.”	807,286,849
4) Unrealized foreign exchange gain (loss) on cash and cash equivalents	Reclassification from “net cash flows from operating activities” to reflect the foreign exchange fluctuations on foreign currency deposits.	(7,302,393)
Total		₱-



44. **Electric Power Industry Reform Act (EPIRA)**

Republic Act No. 9136, otherwise known as the EPIRA, and the covering Implementing Rules and Regulations (IRR) provide for significant changes in the power sector, which include among others: the functional unbundling of the generation, transmission, distribution and supply sectors; the privatization of the generating plants and other disposable assets of NPC, including its contracts with Independent Power Producers (IPP); the unbundling of electricity rates; the creation of a WESM; and the implementation of open and nondiscriminatory access to transmission and distribution systems.

The law also requires public listing of not less than 15% of common shares of distribution companies within five years from the effectivity date of the EPIRA. It provides cross ownership restrictions between transmission and generation companies and between transmission and distribution companies and a cap of 50% of its demand that a distribution utility is allowed to source from an associated company engaged in generation, except for contracts entered into prior to the effectivity of the EPIRA.

There are also certain sections of the EPIRA, specifically relating to generation companies, which provide for a cap on the concentration of ownership to only 30% of the installed capacity of a grid and/or 25% of the national installed generating capacity.

Over the last two years, the implementation of reforms in the power industry mandated by the EPIRA attained significant momentum.

The privatization of the NPC generating assets has accelerated with the sale of its hydropower and coal-fired facilities.

The 25-year concession agreement for the National Transmission Corporation (TransCo), which was previously spun-off from NPC, has been bid out, with a private consortium emerging as the winner. The agreement allows the concessionaire to operate, maintain and expand the transmission facilities of TransCo.

On June 26, 2006, the commercial operation of the WESM in the Luzon Grid commenced. During the first year of operation, total registered peak demand reached 6,552 MW with total registered capacity at 11,396 MW. To date, the monthly transaction volumes for both the spot and bilateral contract quantities recorded a high of 3,725.54 GWh. The WESM has now 23 direct participants, 14 indirect participants, 9 applicants and 2 intending participants. Trial operations in the Visayas Grid are ongoing, with the commercial launch awaiting the approval of the DOE.

Retail competition and open access have yet to be implemented since the preconditions of privatizing at least 70% of NPC's generating assets and at least 70% of NPC-IPP contracts have not been met so far.

The ERC has continued to issue regulations implementing the EPIRA, among which are the Rules for Setting Distribution Wheeling Rates for Privately-Owned Distribution Utilities Entering Performance-Based Regulation, Competition Rules, Rules for Registration of Wholesale Aggregators, Guidelines for the Issuance of Licenses to Retail Electricity Suppliers and Distribution Service and Open Access Rules.



The ERC is presently considering a petition by several industry participants, among which are Meralco, Visayas Electric Co. and the Philippine Independent Power Producers Association, to allow a transitional (interim) and voluntary form of open access. If approved by the ERC, the interim open access regime will allow qualified generation companies and registered electricity suppliers, i.e. those not exceeding the EPIRA-prescribed market limits, to contract directly with eligible end-users for the supply of electricity. Only NPC and PSALM are in breach of the market limits as of the filing of the petition in May 2008.

Following are the proposed amendments to the EPIRA that, if enacted, may have material adverse effect on the Company's business, financial condition and performance.

In the Philippine Senate, the Committee on Energy sponsored the approval on second reading of Senate Bill No. 2121. The bill is now in the period of committee amendments. Proposed amendments to the EPIRA include, among others:

- Lowering the privatization level precondition to retail open access from 70% to 50% for both the NPC generating assets and NPC-IPP contracts, while allowing ERC to declare retail open access even before the 50% level is met with participation being limited to generation companies that comply with the 30%-25% installed generating capacity limits. This may affect the Company's competitiveness of its expansion projects vis-à-vis NPC, which would still control sizeable generating capacity sufficient to dominate the market at the time of implementation should there be a delay as the privatization program progresses.
- Recognizing the regulatory authority of the Philippine Economic Zone Authority (PEZA) over distribution utilities in PEZA-administered economic zones.
- Prescribing additional limitation on bilateral contracts between related parties in that such contracts shall not exceed 20% of the installed generating capacity of a grid. This proposed restriction may prevent generation facilities acquired or developed by the Company or First Gen to enter into off-take agreements with Meralco, the largest distribution utility in Luzon island and the Philippines.
- Disallowing the recovery of stranded debts and contract costs of distribution utilities.
- Subjecting pass-through charges or adjustments to public hearing.

In the House of Representatives, the Committee on Energy has submitted for plenary approval House Bill No. 3124 proposing the following amendments to the EPIRA, among others:

- Accelerating the implementation of retail competition and open access by lowering the prerequisite level of privatization of NPC's generating assets and IPP contracts from 70% to 50%, and recognizing the authority of PEZA to immediately declare retail open access in economic zones. As in the Senate proposal, this could adversely affect the Company's competitiveness vis-à-vis NPC.



The Company cannot provide any assurance whether any or all of these proposed amendments will be enacted in their current form or at all or when any amendment to the EPIRA will be enacted. Proposed amendments to the EPIRA, including those discussed above, as well as other legislation or regulation could have material adverse impact on the Company's business, financial condition and performance.

Based on the Company's assessment, it is in the process of complying with the provisions of the EPIRA and its IRR.

