



PNOC ENERGY DEVELOPMENT CORPORATION

Merritt Road, Fort Bonifacio, Taguig City, Philippines
P.O Box 2102 MCPO, Tel. No. 893-1320/893-6001 Fax No. 840-1575

May 22, 2007

ATTY. PETE M. MALABANAN
Head, Disclosures Department
Philippine Stock Exchange
Tektite Building, Ortigas Center
Pasig City

Dear Atty. Malabanan:

In compliance with the disclosure requirement of the Philippine Stock Exchange (PSE), we submit the attached Securities and Exchange Commission (SEC) Form 20-IS (Definitive).

Very truly yours,

(Original Signed)
Rowena C. Clemente
Company Information Officer, OIC

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 20-IS

**INFORMATION STATEMENT PURSUANT TO SECTION 20
OF THE SECURITIES REGULATION CODE**

1. Check the appropriate box:

Preliminary Information Statement

Definitive Information Statement

Name of Registrant as specified in its charter: **PNOC ENERGY DEVELOPMENT CORP.**

3. **PHILIPPINES**

Province, country or other jurisdiction of incorporation or organization

4. SEC Identification Number **66381**

5. BIR Tax Identification Code **000-169-125-000**

6. **Merritt Road, Fort Bonifacio** **1200**
Taguig City, Metro Manila, Philippines
Address of principal office Postal Code

7. Registrant's telephone number, including area code **(632) 893-6001**

8. **June 14, 2007, 3:00 p.m. PNOC-Energy Development Corp. Main Office, Merritt Road**
Fort Bonifacio, Taguig City, Metro Manila, Philippines
Date, time and place of the meeting of security holders

9. Approximate date on which the Information Statement is first to be sent or given to security holders **May 23, 2007**

10. In case of Proxy Solicitations:

Name of Person Filing the **PNOC ENERGY DEVELOPMENT CORP.**
represented by its President/CEO PAUL A. AQUINO

Statement/Solicitor: _____

Address and Telephone No.: **Merritt Road, Fort Bonifacio, Taguig City, Metro Manila**
(632) 893-6001
Attn: Mr. Erudito Recio (Investor Relations)

11. Securities registered pursuant to Sections 8 and 12 of the Securities Regulations Code or Sections 4 and 8 of the RSA (information on number of shares and amount of debt is applicable only to corporate registrants):

a) Authorized Capital Stock

Common shares, P1.00 par value **15,000,000,000 shares**

b) Issued and Outstanding Shares

Common shares, P1.00 par value **15,000,000,000 shares**

c) Amount of Debt Outstanding as of December 31, 2006

12. Are any or all of registrant's securities listed on a Stock Exchange?

Yes No

If yes, disclose the name of such Stock Exchange and the class of securities listed therein:

PHILIPPINE STOCK EXCHANGE - **COMMON SHARES OF STOCK**

PNOC ENERGY DEVELOPMENT CORPORATION
Annual Stockholders' Meeting
June 14, 2007

PART I: INFORMATION REQUIRED IN INFORMATION STATEMENT

A. GENERAL INFORMATION

Item 1. Date, Time and Place of Meeting of Security Holders:

The annual stockholders' meeting of **PNOC ENERGY DEVELOPMENT CORPORATION** (hereafter the "Registrant" or "Company") will be held on **June 14, 2007 at 2:00 p.m. at the Company's head office located at Merritt Road, Fort Bonifacio, Taguig City, Metro Manila, Philippines.**

The complete mailing address of the principal office of the Registrant is P.O. Box 2101 Makati City Post Office, Makati City.

The approximate date when the information statement and proxy form will be first sent to security holders will be on **May 23, 2007.**

Item 2. Dissenters' Right of Appraisal

The appraisal right will be available when the proposal to create the preferred shares is taken up. Under Section 81 of the Corporation Code, "in case any amendment to the articles of incorporation has the effect of changing or restricting the rights of any stockholder or class of shares, or of authorizing preferences in respect superior to those of outstanding shares of any class", a stockholder may exercise his appraisal right by voting against the proposed action and submit a written demand of payment of the fair market value of his shares.

Any stockholder who votes against the proposed action and who wishes to exercise such right must make a written demand, within thirty (30) days after the date of the meeting or when the vote was taken, for the payment of the fair market value of his shares. Upon payment, he must surrender his certificates of stock. No payment shall be made to any dissenting stockholder unless the Company has unrestricted retained earnings in its books to cover such payment.

Item 3. Interest of Certain Persons in or Opposition to Matters to be Acted Upon

No member of the Board of Directors or executive officer since the beginning of the last fiscal year, or nominee for election as director, or their associates, has had any substantial interest, direct or indirect, by security holdings or otherwise, in any of the matters to be acted upon in the meeting, other than election to office.

No director has informed the Company in writing or otherwise that he intends to oppose any action to be taken up at the meeting.

B. CONTROL AND COMPENSATION INFORMATION

Item 3. Voting Securities and Principal Holders Thereof

There are 15,000,000,000 outstanding unclassified common shares entitled to notice and to vote at the meeting. Each share is entitled to one (1) vote each.

The record date for the purpose of determining the stockholders entitled to notice of, and to vote at the Annual Stockholders' Meeting is **May 14, 2007**.

The election of directors for the current year will be taken up and all stockholders have the right to cumulate their votes in favor of their chosen nominees for director in accordance with Section 24 of the Corporation Code. Section 24 provides that a stockholder, may vote such number of shares registered in his name as of the record date for as many persons as there are directors to be elected or he may cumulate said shares and give one candidate as many votes as the number of directors to be elected multiplied by the number of shares shall equal, or he may distribute them on the same principle among as many candidates as he shall see fit. The total number of votes cast by such stockholder should not exceed the number of shares owned by him as shown in the books of the corporation multiplied by the whole number of directors to be elected.

Security Ownership of Certain Record and Beneficial Owners and Management

1) Persons Known to the Registrant to be Directly or Indirectly the Record or Beneficial Owner of More than 5% of Any Class of the Registrant's Voting Securities:

As of March 31, 2007, the Registrant has no knowledge of any individual or any party who beneficially owns more than 5% of its outstanding common stock except as set forth in the table below:

Type of Class	Name, address of Record Owner and Relationship with Issuer	Name of Beneficial Owner * ** & Relationship with Record Owner	Citizenship	No. of Shares Held	Percent of Class
Common	Philippine National Oil Company (PNOC) * Energy Center Merritt Road Fort Bonifacio, Taguig PNOC is the parent corporation / majority shareholder of the Company.	Republic of the Philippines (PNOC is a wholly owned corporation of the Republic of the Philippines)	Filipino	8,999,999,991	60.00%
Common	PCD Nominee Corporation (Foreign) ** PCD Nominee Corporation has no relation to the Company	The Company is not aware of any beneficial owner of shares under a PCD account holding more than 5% of the outstanding common stock. (PCD Nominee Corp. is the trustee of the shares of the beneficial owner)	Foreign	5,253,856.354	35.03%

- * Beneficial owner is the government of the Republic of the Philippines through the Philippine National Oil Company. The authority to vote the shares of PNOC is usually exercised by the Secretary of Energy, Raphael M. Perpetuo Lotilla. However, the proxy of PNOC for the meeting on June 16, 2007 has not yet been received by the Company.
- ** PCD Nominee Corporation, a wholly owned subsidiary of Philippine Central Depository, Inc. (PCD), is the registered owner of the shares in the books of the Company's transfer agent in the Philippines. The beneficial owners of such shares are PCD's participants, who hold the shares on their behalf or in behalf of their clients. PCD is a private company organized by the major institutions actively participating in the Philippines capital market to implement an automated book-entry system of handling securities transactions in the Philippines.

2) Security Ownership of Management (as of March 31, 2007):

Title of class	Name of Beneficial Owner	Amount of Shares	Nature of Ownership	Citizenship	Percent of Class
Directors					
Common	Antonio M. Cailao	50,001	Direct	Filipino	0.000%
Common	Paul A. Aquino	100,001 100,000	Direct Indirect	Filipino	0.001%
Common	Benjamin F. Tugonon	50,001	Direct	Filipino	0.000%
Common	Danilo Luis M. Mariano	30,001	Direct	Filipino	0.000%
Common	Ernesto S. Amatong	10,001	Direct	Filipino	0.000%
Common	Benito Jose Q. Bengzon	10,001	Direct	Filipino	0.000%
Common	Nicasio P. Rodriguez, Jr.	10,001	Direct	Filipino	0.000%
Common	Ralph A. Salazar	140,001	Direct	Filipino	0.001%
Common	Asuncion J. Espina	200,001	Direct	Filipino	0.001%

Title of Class	Name of Beneficial Owner	Amount of Shares	Nature of Ownership	Citizenship	Percent of Class
Key Executive Officers					
Common	Ester R. Guerzon	50,001	Direct	Filipino	0.000%
Common	Agnes C. De Jesus	200,001	Direct	Filipino	0.001%
Common	Marcelino M. Tongco	330,001	Direct	Filipino	0.002%
Common	Manuel S. Ogena	600,001	Direct	Filipino	0.004%
Common	Danilo C. Catigtig	150,001	Direct	Filipino	0.001%
Common	Fenina O. T. Rodriguez	500,001	Direct	Filipino	0.003%
Common	Michael A. Medado	10,001	Direct	Filipino	0.000%
Common	Roberto V. San Jose	0	-	Filipino	0.000%
Common	Ana Maria A. Katigbak-Lim	0	-	Filipino	0.000%

Aggregate ownership of directors and officers as a group unnamed

As of March 31, 2007, the total number of shares owned by the Directors and key executive officers is 2,540,016 or 0.017%.

(3) Voting Trust Holder of 5% or more

The Company knows of no persons holding more than 5% of common shares under a voting trust or similar agreement.

(4) Changes in control

No change in control of the Registrant has occurred since the previous fiscal year.

(5) Certain Relationships and Related Transactions

There is no material transaction or proposed transaction to which the Company was or is to be a party, in which any of its directors or executive officers, or any nominee for election as a director, or any individual owning, directly or indirectly, significant voting power of the Company, or any close family members of such individuals, had or is to have a direct or indirect material interest.

Item 5. Directors and Executive Officers

The following are the directors and executive officers of the Company, each having a term of one (1) year and to serve as such until their successors are elected and qualified, and their respective positions, ages and business experience in the past five years:

Directors

Antonio M. Cailao, 59

Mr. Cailao, Filipino, the Company's Chairman of the Board, was elected on November 23, 2006. He was previously a Senior Executive Vice President of the United Coconut Planters Bank from September 2003 to December 2005. Mr. Cailao has also worked overseas in senior management positions for leading global financial institutions for over two decades. As a business franchise builder, he has developed and managed business plans and strategies for in-country, intra-country and regional clients in Latin America and Asia. He has an undergraduate degree, and a postgraduate degree in Business Administration, from the University of the Philippines.

Paul A. Aquino, 64

Mr. Aquino, Filipino, the Company's President and CEO since February 2004, is an electrical engineer by profession and has a master's degree in business administration. He has been a Director of the Company since 2001. He previously served as president to various companies, including Dynamic Computer Services, Corinthian Securities and Management Dynamics. Mr. Aquino was also a consultant for Sycip, Gorres & Velayo from 1967 to 1969. He also serves as an Honorary Consul of the Republic of Malta.

Benjamin F. Tugonon, 73

Atty. Tugonon, Filipino, is a lawyer and has been in active law practice since 1960. He has been a Director since June 18, 2001. Atty. Tugonon served as City Councilor of Ormoc City from 1964 to 1967, 1980 to 1986 and 1988 to 1992 and was elected Vice Mayor for Ormoc City for two consecutive terms from 1992 to 1998. He is active in various legal, social and cooperative organizations, and has attended numerous seminars and trainings on national government functions.

Danilo-Luis M. Mariano, 54

Mr. Mariano, Filipino, has been a Director since June 17, 2002. He obtained his Journalism degree from the University of the Philippines and attended a journalism fellowship program at the

University of Michigan, Ann Arbor from 1983 to 1984. He was columnist and editor-in-chief of various major news publications, including The Philippine Daily Inquirer, The Manila Times, The Philippine Post and Today. He was the editor-in-chief and senior manager for ABS-CBN Interactive.

Ernesto S. Amatong, 77

Mr. Amatong, Filipino, has been a Director since October 23, 2002. He also served as director for PNOC Coal Corporation from 2001 to June 2002. He is a lawyer by profession and obtained his graduate degree from Georgetown University in Washington DC. Attorney Amatong served at Dipolog City's Andres Bonifacio College as instructor (1954 to 1960), Dean of the College of Law (1968 to 72), President (1968 to 90) and is currently Chairman of the Board of the college. His public service includes two terms as Congressman (1987 to 1995), as well as memberships in various congressional committees.

Benito Q. Bengzon, 71

Mr. Bengzon, Filipino, has been a Director since April 27, 2003. He is a lawyer and obtained his bachelor of laws and postgraduate studies in Business Administration from the Ateneo de Manila University. He has previously worked with various offices which include the PNOC and its Subsidiaries, the Department of Agriculture, Government Service Insurance System (GSIS), the Department of Environment and Natural Resources (DENR), the Bureau of Fisheries, the Medical City, Hyatt Hotel and Manila Hotel. He is currently President of Mt. Abo-Abo Development Corporation, Chairman of Crew Minerals Philippines, Central Palawan Mining and Industrial Corporation and is an active member of various NGOs.

Nicasio P. Rodriguez, Jr., 67

Mr. Rodriguez, Filipino, has been a Director of the Company since March 17, 2003. He graduated from the Philippine Military Academy and has a post graduate degree in National Resource Management from the Naval Post Graduate School in the United States and a Business Management degree from the Asian Institute of Management ("AIM"). Mr. Rodriguez was Postmaster General and CEO of the Philippine Postal Corporation from 1998 to 2003 and served as the Commanding General of the Philippine Air Force from 1993 to 1995.

Ralph A. Salazar, 42

Mr. Salazar, Filipino, has been a Director since November 22, 2004. He is a civil engineer by profession. He is the President of the Tacloban RAS Construction Corporation, the Vice President of Leyte Concrete Aggregates Corp. and the General Manager of RAS Construction. He is also the District Chairman of the Lakas-NUCD-UMDP Party in the 3rd District of Leyte.

Asuncion Jimenez Espina, 70

Ms. Espina, Filipino, has been a Director of the Company since February 15, 2005. She is an accountant by profession and graduated *magna cum laude* from Philippine Women's University in 1960. Ms. Espina was a CPA reviewer and instructor. She was employed at the Central Bank of the Philippines from 1968 to 1992.

Key Executive Officers

Ester R. Guerzon, 60 — Vice President for Corporate Services

Ms. Guerzon, Filipino, has been with the Company since 1978 and has held her current position since April 4, 2005. She was appointed Vice President for Logistics and Administration in October 2003. Previously, she served as Manager of the Company's Property Management Department and Operations Services Division (1993 to 2003) and has held various positions in the human resources department, including in the areas of employment compensation, benefits and labor relations and in the administrative services department both at the Company and Petron Corporation. She is a Political Science graduate, *magna cum laude*, from the University of Santo Tomas and has masters degrees in Political Science from the University of Santo Tomas and Business Administration from the Ateneo Graduate School. Ms. Guerzon is a 1996 graduate of the Management Development Program with Distinction from AIM.

Agnes C. de Jesus, 53 — Vice President for Environmental and External Relations

Ms. de Jesus, Filipino, joined the Company in 1980 and has held her current position since April 4, 2005. She has had extensive experience in environmental and watershed management, government relations, policy formulation, community development and conflict resolution for energy projects. She was the environmental editor of *Geothermics (International Journal on Geothermal Research and its Applications)* from 1996 to 2004. She was also a member of the Board of Consultants of the Kenya Geothermal Program from 1993 to the present and is an accredited Environmental Assessment Expert of the DENR from 1997 to the present. Ms. de Jesus was the head of the Company's Environmental Management Division prior to her current position. Ms. de Jesus obtained bachelors and masters degrees in Botany from the University of the Philippines in Diliman and completed the Management Development Program of AIM.

Marcelino M. Tongco, 52 — Vice President for Operations

Mr. Tongco, Filipino, has been with the Company since 1979 and has held his current position since April 4, 2005. He previously served as General Manager of Operations, Manager for Engineering and Construction from 1988 to 1991 and Manager for Project Development from 1991 to 1994. He graduated with a Bachelors of Science in Civil Engineering from the University of Santo Tomas and has pursued masters studies in Civil Engineering at the University of the Philippines in Diliman. Mr. Tongco also completed the Management Development Program of AIM in 1997 and obtained a Master's Certificate in Project Management from George Washington University in 1997.

Manuel S. Ogena, 50 — Vice President for Technical Services

Mr. Ogena, Filipino, joined the Company in 1979 and has held his current position as Vice President for the Technical Services Sector since December 2005. He joined the Company as a Geologist and was appointed Supervisor under the Geoscientific department in 1985. He became Department Manager in 1994 in the Exploration Department and then the Geoscientific Department in 2003. Mr. Ogena has been a member of the board of directors of the International Geothermal Association since May 2006. He graduated with a BS Geology degree from the University of the Philippines in Diliman and an MS Mechanical Engineering degree from the University of Auckland in New Zealand. He is also a graduate of the Management Development

Program of AIM and earned his Masters Certificate in Project Management from George

appointed as Director of PNOC – Shipping and Transport Corporation Board from 1998-1999. A Chemical Engineer, he graduated from Mapua Institute of Technology in 1974. He obtained MBA units at the Ateneo Graduate School of Business in 1983 and completed the Management Development Program of AIM in 1996.

Francis M. Dolor, 54 — Senior Manager, Planning and Control Division

Mr. Dolor, Filipino, has been with the Company since 1980 and has held his current position since February 2005. He was previously Manager for the Power and Energy Services Department from August 2003 to January 2005. He also served as Project and Business Development Manager from March 1996 to July 2003. He graduated from the University of the Philippines in Diliman with a B.S. in Mechanical Engineering. Mr. Dolor also completed the Management Development Program of AIM in 1996. He obtained a Master's Certificate in Project Management from George Washington University in 1995.

Michael A. Medado, 52 — Senior Manager, Human Resources & Legal Division

Attorney Medado, Filipino, has been with the Company since May 1993. He was appointed as the Company's General Counsel and Corporate Secretary in September 2001. He was appointed Senior Manager of the Company's Human Resources and Legal Division in April 2005. Prior to his employment in the Company, he had extensive experience in taxation, corporate and labor law in the PNOC Group of companies. A graduate of the University of the Philippines College of Law, he has been a lawyer since 1979.

Elvira L. Punsalan, 47 — Senior Manager, Supply, Procurement and Materials Management Division

Ms. Punsalan, Filipino, joined the PNOC Energy Development Corporation in October 1994 and has held her current position since August 2006. Prior to this assignment, she held the position of Accounting Manager from June 1996 to July 2006. Prior to her employment in the Company, she held various positions in corporate accounting and administrative systems in PNOC and Petron Corporation. A certified public accountant, she graduated with a B.S. degree in Commerce with a major in Accounting, and graduated *summa cum laude* at Far Eastern University. She has completed the Management Development Program of the AIM in 1994 and completed the foundation courses for the Master in Business Administration at De La Salle University.

Gino P. de la Cruz, 51 — Resident Manager, Northern Negros Geothermal Production Field (NNGPF)

Mr. De la Cruz, Filipino, has been with the Company since October 1978 and has held his current position since May 2005. He previously served as Resident Manager for BGPF from October 2002 to April 2005. He rose from the ranks and has held field maintenance and production managerial positions in BGPF and SNGPF, respectively. He graduated with a B.S. in Mechanical Engineering from Silliman University in Dumaguete City in 1978 and obtained his MBA from St. Paul College also in Dumaguete City in 2000. He is a graduate of the Management Development Program of AIM in 1998 and attended the Plant Operations and Maintenance Management Training in Japan in 2006.

Ellsworth R. Lucero, 48 — Resident Manager, Mindanao Geothermal Production Field (MGPF)

Mr. Lucero, Filipino, has been with the Company since July 1983 and has held his current position since July 2003. He previously served as Field Production Manager for BGPF from June 1994 until his promotion as Resident Manager at MGPF. He graduated with a B.S. in Mechanical Engineering from Cebu Institute of Technology in Cebu City in 1979. He is also a graduate of the Management Development Program of Asian Institute of Management in 1995. Prior to his employment with the Company, he had worked as Power Plant Junior Manager at the Atlas Consolidated Mining & Development Corporation from 1979 to 1982.

Dwight A. Maxino, 48 — Resident Manager, Southern Negros Geothermal Production Field (SNGPF)

Mr. Maxino, Filipino, has been with the Company since February 1980 and has held his current position since January 2006. He previously served as Resident Manager for Leyte Geothermal Production Field (LGPF) from July 2004 to April 2005 and as Field Production Manager for the same project from January 1989 to June 2004. He graduated with a B.S. in Mechanical Engineering from Cebu Institute of Technology in Cebu City in 1979. He obtained his Diploma in Geothermal Technology at the University of Auckland in New Zealand in 1981 and a graduate of the Management Development Program of AIM in 1992.

Manuel C. Paete, 50 — Resident Manager, Leyte Geothermal Production Field (LGPF)

Mr. Paete, Filipino, has been with the Company since March 1980 and has held his current position since August 2005. Prior to his promotion as Resident Manager, he was Field Production Manager for LGPF since July 2004. He has held various positions that dealt with functions covering geothermal reservoir engineering, well test and measurement and FCRS operations in LGPF. He graduated with a B.S. in Mechanical Engineering from the Leyte Institute of Technology in Tacloban City in 1978. He obtained his Diploma in Geothermal Technology at the United Nations University in Iceland in 1983. Prior to his employment in the Company, he had worked as an Engineering Analyst at the Consult Asia Management in Metro Manila for a year.

Liberato S. Virata, 47 — Resident Manager, Bacman Geothermal Production Field (BGPF)

Mr. Virata, Filipino, has been with the Company since April 1982 and has held his current position since May 2005. Likewise, he held the field maintenance and production managerial positions since April 1990 in LGPF and BGPF, respectively. He graduated with a B.S. in Mechanical Engineering from Mapua Institute of Technology in Manila in 1981. He also completed the Management Development Program of AIM in 1996, the Diploma Course of Maintenance Management System in Japan in 2002, as well as the Refinery Operators Course in Sydney, Australia in 1988.

Mario L. Taguines, 52 — Senior Manager, Engineering, Procurement & Design Division (EPDD)

Mr. Taguines, Filipino, has been with the Company since December 1979 and has held his current position since April 2005. Prior to moving to Field Operations, he has held division and department managerial positions in the Engineering and Construction of EDC since June 1997.

He graduated with a B.S. in Mechanical Engineering from Holy Angel College in Angeles City in 1976. He also completed the Management Development Program of AIM in 1997. He also completed his Diploma in Geothermal Technology at the University of Auckland in New Zealand in 1987. Prior to his employment in the Company, he had worked as Mechanical Engineer with Ecco-Asia from 1978 to 1979. He also taught mechanical engineering courses at Holy Angel College from 1977 to 1978.

Francisco A. Palafox, 54 — Senior Manager, Power and Sales Division

Mr. Palafox, Filipino, has been with the Company since February 1981 and has held his current position since December 2005. Prior to moving to Field Operations, he was the Senior Manager and Department Manager under the Purchasing and Traffic Division in 2003 and 1993, respectively. In 1991, he was the Materials and Control Manager. He held the position of Resident Manager of the Bacman Geothermal Production Field in 1986 to 1991. He graduated with a B.S. in Civil Engineering from University of Santo Tomas in Manila in 1975. He is also a graduate of the Management Development Program of AIM in 1994. He also earned credits in the MBA program at the Ateneo Graduate School of Business in Makati City from 1976 to 1978.

Significant Employees

No single person or employee is expected to make a significant contribution to the Company's business since the Company considers the collective efforts of all its employees as instrumental to the success of the Company.

Nominees for Directors

The foregoing directors have been renominated for the current year.

In addition, the nominations of the following persons for independent director have been approved by the Company's Nomination Committee:

Carmelo Maria Luza Bautista is currently a Partner at Argosy Partners, Inc., a Financial Advisory Group involved in various investment banking activities. Concurrently, he is also an Executive Director of First Metro Investment Corporation, the Investment Banking subsidiary of the Metrobank Group of Companies. He was formerly president and chief executive officer of the Philippine Bank of Communications from June 2005 to November 2006, president of ABN AMRO Bank (Philippines), Inc. in 2002 to May 2005 and country manager of ABN AMRO Bank NV in 1998 to May 2005. Mr. Bautista also served as vice president / head of corporate banking group of Citibank NA Philippine Branch in 1995 to 1998 and vice president of BPI Capital in 1995. He spent a total of 16 years in various capacities in Citibank Singapore Regional Office and the Manila Branch. He was also a director of the European Chamber of Commerce of the Philippines in 2000 to 2003 and vice chairman of the Overseas Bankers Association of the Philippines. Mr. Bautista has a degree in economics from the Ateneo de Manila University and obtained his Masters in Business Management at the Asian Institute of Management.

Edgardo A. Bautista, is currently Executive Director, Head of Infrastructure of Avenue Asia Investments Management, LLC (Philippine Representative Office). He is also a director of San Fernando Electric Company. He was formerly vice chairman of Mirant Corporation from January to July 2006 and its president from January 1997 to December 2005. Prior to that, Mr. Bautista was president and CEO of Hopewell Energy Philippines Corporation and Hopewell Power

Corporation. He was also engaged in various capacities in a number of companies including Westinghouse Electric International, Inc., General Electric (Philippine) Inc., Mobil Oil Philippines, Philippine Refining Corporation, Jardine Davies and First Philippine Holdings Corporation. Mr. Bautista is a certified fellow of the Institute of Corporate Directors.

Vicente S. Perez Jr. is currently chairman of Merritt Partners, a boutique energy advisory firm focused on Asia, and founder of Alternergy Partners, a renewable power company for emerging countries in Asia. He is an independent director of Nido Petroleum (ASX), SM Investments (PSE), ST Telemedia (a Temasek company), and Northwind Power (the first commercial windfarm in Southeast Asia), as well as a member of the national council of World Wildlife Fund-US and the board of advisors of the Yale Center for Environment Law and Policy. Mr. Perez served as Secretary of Energy of the Republic of the Philippines from June 2001 to March 2005 and Undersecretary for Industry at the Department of Trade and Industry in early 2001. Previous to his government service, Mr. Perez was formerly Managing Director of Lazard Freres in New York and Singapore from 1988 to 1997 and thereafter founded Next Century Partners, a private equity firm. He is 49 years old.

Eric O. Recto is currently CEO of Eastern Telecommunications Philippines, Inc. (ETPI) and Connectivity Unlimited Resources Enterprise, Inc. (CURE) as well director and president of ISM Communications Corporation, and vice chairman of PhilWeb Corporation. He is also a director of Philippine National Bank. He was formerly Undersecretary of Department of Finance for the Philippine Government in charge of handling both the International Finance Group and the Privatization Office. Before his work with the government, he was Chief Financial Officer of Alaska Milk Corporation and prior to that, Belle Corporation. Mr. Recto has a degree in Industrial Engineering from the University of the Philippines as well as an MBA from the Johnson School, Cornell University.

Gabriel R. Singson Jr. is currently a director of SR Capital Holdings Inc. He was the undersecretary for privatization at the Department of Finance of the Republic of the Philippines in 2005 to 2006. Prior to joining government, Mr. Singson founded SR Capital Holdings and was its chairman from 2000 to 2005. He was formerly vice chairman of Pilipino Cable Corporation from 1998 to 2004, president of Telemondial Holdings Inc. from 1997 to 2004, chief operating officer in 1996 to 1999 and chief financial officer in 1990 to 1996 of Macondray & Co. Inc., chief financial officer of Macondary Holdings Corp. from 1990 to 1999, as well as a director of Del Monte Philippines Inc. in 1996 to 1999. Mr. Singson graduated magna cum laude in the Business Management Honors Program of Ateneo de Manila University and obtained his MBA in Finance at the Wharton School, University of Pennsylvania.

Independent Directors/Nomination Committee

In compliance with SEC Memorandum Circular No. 16, series of 2002 (now SRC Rule 38), which provides for the guidelines on the nomination and election of independent directors, a Nomination Committee has been constituted to pre-screen and accept the nominations of regular and independent directors.

Accordingly, the Nomination Committee has approved the nominations of 1) Edgardo A. Bautista; 2) Eric O. Recto; 3) Mr. Carmelo L. Bautista; 4) Mr. Vicente S. Perez Jr.; and 5) Mr. Gabriel R. Singson Jr., as independent directors conformably with the criteria prescribed in the said SEC Memo Circular and the Company's Code of Corporate Governance.

Messrs. Edgardo A. Bautista and Recto were formally nominated by Ms. Ester Guerzon. Ms. Guerzon has no relation to Messrs. Bautista and Recto.

Mr. Perez was formally nominated by stockholder Government of Singapore Investment Corporation Pte Ltd. (“GIC”). GIC has no relation to Mr. Perez.

Mr. Carmelo Bautista was formally nominated by Mr. Michael Medado. Mr. Medado has no relation to Mr. Perez.

Mr. Singson was formally nominated by Mr. Marcelino M. Tongco. Mr. Tongco has no relation to Mr. Singson.

Family Relationships

There are no family relationships up to the fourth civil degree either by consanguinity or affinity among directors, executive officers, or persons nominated or chosen by the registrant to become directors or executive officers.

Involvement in Certain Legal Proceedings

To the best of the Company’s knowledge, there has been no occurrence during the past five years of any of the following events since its incorporation which are material to an evaluation of the ability or integrity of any director, person nominated to become a director, executive officer, or control person of the Company:

1. Any insolvency or bankruptcy petition filed by or against any business of which such person was a general partner or executive officer either at the time of the insolvency or within two years prior to that time;

2. Any conviction by final judgment in a criminal proceeding, domestic or foreign, or any pending criminal proceeding, domestic or foreign, excluding traffic violations and other minor offenses;

3. Any final and executory order, judgment, or decree of any court of competent jurisdiction, domestic or foreign, permanently or temporarily enjoining, barring, suspending, or otherwise limiting involvement in any type of business, securities, commodities, or banking activities; and

4. Any final and executory judgment by a domestic or foreign court of competent jurisdiction (in a civil action), the Philippine SEC, or comparable foreign body, or a domestic or foreign exchange or electronic marketplace or self-regulatory organization, for violation of a securities or commodities law.

Mr. Aquino and Ms. Guerzon in their capacity as President and Vice President, respectively, have been impleaded as respondents in three labor cases filed by former Company employees. The Company, however, does not believe that these claims affect either Mr. Aquino or Ms. Guerzon’s ability or integrity as a Company Director or executive officer, respectively.

Certain Relationships and Related Transactions

There has been no transaction during the last two years, nor is any transaction presently proposed, to which the Company was or is to be a party in which any director or executive officer of the Company, or nominee for election as a director, or owner of more than 10% of the Company's voting securities, or voting trust holder of 10% or more of any class of the Company's securities, or any member of the immediate family of any of the foregoing persons had or is to have a direct or indirect material interest. In the ordinary and regular course of business, the Company may have transactions with other companies in which some of the foregoing persons may have an interest.

The 2006 Audited Financial Statements disclose the following related party transactions:

	2006	2005
<i>Due from affiliated companies</i>		
▪ PNO Exploration Corporation	2,498,861	398,060
▪ PNO Petrochemical Development Corporation	1,354,533	1,354,533
▪ PNO Coal Corporation	724,846	724,846
▪ PNO Development and Management Corporation	206,863	116,379
	4,785,103	2,593,818
<i>Due to PNO</i>	350,844,176	364,167,738

- a. Transactions due from affiliated companies represent normally recurring charges and credits which are payable upon presentation of debit/credit notes.
- b. Transactions due to PNO represent the interests and guarantee fees on loans from IBRD and OECF, which were secured by PNO and relent to PNO EDC being the implementing agency, and the ₱200 million balance of loan plus interest obtained directly from PNO. Each re-lending agreement is covered by a subsidiary loan agreement. The agreement provides that PNO EDC shall repay PNO the principal, interest, commitment charges and such other amounts, fees and charges payable by PNO to the lending banks including such amounts incurred by PNO in connection with the purchase of foreign currencies.

Item 6. Compensation of Directors and Executive Officers

The aggregate compensation paid or incurred during the last two fiscal years and estimated to be paid in the ensuing fiscal year to the executive officers and directors of the Company are as follows:

Summary Compensation Table

Name	Position	Year	Salary	Bonus	Other Annual Compensation
Paul A. Aquino	Director, President and CEO				
Agnes C. De Jesus	Vice-President for Environmental and External Affairs				
Marcelino M. Tongco	Vice-President for Operations				
Manuel S. Ogena	Vice-President for Technical Services				
Danilo C. Catigtig	Vice-President for Power and Sales				
Total (Top 5 Executives)		2004	15,899,704	2,416,552	2,142,524
		2005	13,582,222	2,533,457	1,724,703
		2006	13,918,370	9,725,186	2,431,646
		2007 Est.	13,584,000	5,859,000	2,398,000
Total (Executives and Directors)		2004	51,492,088	15,403,942	9,643,791
		2005	44,745,732	15,547,284	8,762,932
		2006	51,155,175	29,484,903	11,001,351
		2007 Est.	41,524,348	17,703,662	9,743,230

Employment Contracts and Termination of Employment and Change-in-Control Arrangements.

In compliance with PNOC Board Resolution No. 1522, S' 2004, the members of the Board are remunerated with a compensation package as follows:

- Monthly director's fee of ₱30,000.00
- Director's allowance of a minimum of ₱14,000.00 per month for one (1) Board meeting per month with an increment of ₱2,000.00 per additional meeting within the month, but not to exceed ₱20,000 per month per director.

Warrants and Options Outstanding: Repricing

Not applicable. The Company has no outstanding warrants and options.

Item 7. Independent Public Accountants

The Company audited financial statements are prepared by the Commission on Audit in compliance with Philippine law.

Since 1987, the Commission on Audit of the Philippines has served as the independent auditor of the Company to audit the Company's financial statements and the Company has not had any material disagreements on accounting matters or financial disclosure matters with the Commission on Audit.

Representatives of the Commission on Audit shall be present at the meeting, will have the opportunity to make a statement if they choose to do so, and will be available to respond to appropriate questions.

Item 8. Compensation Plans

In view of the Company's initial public offering, the Company's Management seeks to formalize by way of stockholders' approval the new compensation package of its Board of Directors consisting of the following:

Item	Amount
Director's Fee	Php 50,000 / month
Attendance Fee	Php 10,000 per Board meeting and Php 5,000 per Committee meeting
Bonus	Equivalent of 1/2% of declared cash dividend
Insurance	Php 330 / month for Group Life Php 1,400.24 / month for Group hospitalization
Car Plan	Inclusion in existing car plan of officers under terms and conditions to be determined by the President/CEO

C. ISSUANCE AND EXCHANGE OF SECURITIES

Item 9. Authorization or Issuance of Securities Otherwise than for Exchange

The Board of Directors is submitting for the stockholders approval the proposal: (i) to increase the authorized capital stock by way of creation of preferred shares, and (ii) to insert a provision on the denial of pre-emptive rights with regard to the issuance of preferred shares.

The Board proposes to increase the authorized capital stock from Fifteen Billion Pesos (Php 15,000,000,000) divided into 15,000,000,000 common shares at a par value of One Peso (Php 1.00 per share), to Fifteen Billion Seventy Five Million (Php 15,075,000,000) divided into 15,000,000,000 common shares with a par value of One Peso (Php 1.00) per share and Seven Billion Five Hundred Million (7,500,000,000) preferred shares with a par value of Php 0.01 per share.

The preferred shares shall be (i) voting, (ii) entitled to an 8% - 10% cumulative dividend rate, (iii) redeemable at par value when the applicable foreign equity limitations under the Philippine

Constitution on entities engaged in the exploration, development, utilization and operation of geothermal energy projects in the Philippines have been removed and the Corporation is no longer engaged in any other activity likewise reserved exclusively to Philippine citizens or corporations or associations at least 60% of whose capital is owned by Philippine citizens, (iv) non-convertible, and (v) have a preference over common shares in case of liquidation or dissolution of the Company. The preferred shares may be subject to certain restrictions, including transferability only to Philippine citizens or corporations or associations at least 60% of whose capital is owned by Philippine citizens.

The creation of the preferred shares has been submitted to the Office of the Government Corporate Counsel for an opinion on its legality.

Item 11. Financial and Other Information

Copies of the Company's audited financial statements and a discussion by Management of its operations is contained in the accompanying Management Report.

D. OTHER MATTERS

Item 15. Action with Respect to Reports:

The Minutes of the previous annual stockholders' meeting will be submitted for stockholder's approval. During the last stockholders' meeting held on June 13, 2006, the stockholders approved the following: (i) minutes of the previous annual meeting held on July 19, 2005; (ii) Management report; (iii) ratification of Management's acts; (iv) activation of paragraphs 3 and 6 of the Corporation's secondary purposes; and (v) election of directors.

Approval of the Minutes constitutes a ratification of the accuracy and faithfulness of the Minutes to the events that transpired during the meeting. This does not constitute a second approval of the same matters taken up at the annual stockholders' meeting, which has been approved.

Included among the acts in the past year until the present date to be submitted for stockholders' ratification, are the following: (i) initial public offering of the Corporation and its privatization; (ii) various power projects.

Item 17. Amendment of Articles of Incorporation by Way of Creation of Preferred Shares

The Board of Directors is submitting for the stockholders approval the proposal: (i) to increase the authorized capital stock by way of creation of preferred shares, and (ii) to insert a provision on the denial of pre-emptive rights with regard to the issuance of preferred shares.

The Board proposes to increase the authorized capital stock from Fifteen Billion Pesos (Php 15,000,000,000) divided into 15,000,000,000 common shares at a par value of One Peso (Php 1.00 per share), to Fifteen Billion Seventy Five Million (Php 15,075,000,000) divided into 15,000,000,000 common shares with a par value of One Peso (Php 1.00) per share and Seven

Billion Five Hundred Million (7,500,000,000) preferred shares with a par value of Php 0.01 per share.

The preferred shares shall be (i) voting, (ii) entitled to an 8% - 10% cumulative dividend rate, (iii) redeemable at par value when the applicable foreign equity limitations under the Philippine Constitution on entities engaged in the exploration, development, utilization and operation of geothermal energy projects in the Philippines have been removed and the Corporation is no longer engaged in any other activity likewise reserved exclusively to Philippine citizens or corporations or associations at least 60% of whose capital is owned by Philippine citizens, (iv) non-convertible, and (v) have a preference over common shares in case of liquidation or dissolution of the Company. The preferred shares may be subject to certain restrictions, including transferability only to Philippine citizens or corporations or associations at least 60% of whose capital is owned by Philippine citizens.

The creation of the preferred shares has been submitted to the Office of the Government Corporate Counsel for an opinion on its legality.

The increase in authorized capital stock by way of creation of preferred shares will enable the Company to carry out a further privatization exercise by allowing additional foreign and domestic investment, while at the same time ensuring that the Company remains a Philippine National upon completion, in a manner that is least dilutive, fastest to execute and most economical

Item 19. Voting Procedure:

For the election of 11 directors, 11 nominees receiving the most number of votes will be elected to the Board of Directors. Cumulative voting will apply.

For the amendment of the articles of incorporation consisting of: the (i) increase in authorized capital stock by way of creation of preferred shares; and (ii) insertion of a provision denying the pre-emptive right with regard to the issuance of preferred shares, the affirmative vote of at least two-thirds of the stockholders owning the outstanding common stock present or represented at the meeting will be necessary. In all cases wherein the law requires a two-thirds vote of the outstanding capital stock, the majority vote of the minority shareholders present or represented at the stockholders' meeting shall likewise be required for validity of decisions in such meetings.

For all other matters to be taken up, majority vote of the outstanding capital stock present or represented at the meeting where a quorum exists will be sufficient.

Voting shall be done *viva voce* or by raising of hands and the votes cast for or against the matter submitted shall be tallied by the Corporate Secretary in case of division of the house.

PART II: INFORMATION REQUIRED IN A PROXY FORM

Item 1. Identification

This proxy is solicited by the Board of Directors and Management of PNOG Energy Development Corporation. The solicited proxy shall be exercised by Mr. Paul A. Aquino, the President and Chief Executive Officer of the Company or the stockholder's authorized representative.

Item 2. Instruction

- a. For agenda items other than election of directors, the proxy form shall be accomplished by marking in the appropriate box either "FOR", "AGAINST" or "ABSTAIN" according to the stockholder's/proxy's preference.

For election of directors, the stockholder/proxy shall mark with an "X" the space across the name of his chosen nominee for regular and independent director.

- b. If no instructions are indicated on a returned and duly signed proxy, the shares represented by the proxy will be voted: FOR the approval of the minutes of previous meeting of the stockholders; FOR the approval of the Management Report and audited financial statements for year ended December 31, 2006; FOR the confirmation and ratification of all acts and resolutions of Management and the Board of Directors from the beginning of the last fiscal year to date as reflected in the books and records of the Company; FOR the approval of the increase in authorized capital stock to Php 15.075 Billion by way of creation of Php 75 Million worth of preferred shares; FOR the approval of the amendment of the Articles of Incorporation by including a provision on the denial of the preemptive right with regard to the issuance of preferred shares; FOR the approval of directors' compensation; and to authorize the Proxy to vote according to discretion of the Company's President or Chairman of the Meeting on the "Election of Board of Directors" and on any matter that may be discussed under "Other Matters".

A Proxy Form that is returned without a signature shall not be valid.

- c. The matters to be taken up in the meeting are enumerated opposite the boxes on the form. The names of the nominee directors are likewise enumerated opposite an appropriate space.

Item 3. Revocability of Proxy

A shareholder may revoke his proxy on or before the date of the Annual Meeting. The proxy may be revoked by the shareholder's written notice to the Corporate Secretary advising the latter of the revocation of the proxy, or by a shareholder's personal attendance during the meeting.

Item 4. Persons Making the Solicitation

This solicitation is made by the Company. No director has informed the Company in writing or otherwise of his intention to oppose any action intended to be taken up at the meeting.

Solicitation of proxies will be done mainly by mail. Certain regular employees of the Company will also solicit proxies in person or by telephone.

The estimated amount to be spent by the Company to solicit proxies for the Board of Directors is Php 20,000. The cost of solicitation will be borne by the Company.

Item 5. Interest of Certain Persons in Matters to be Acted Upon


No member of the Board of Directors or executive officer since the beginning of the last fiscal year, or nominee for election as director, or their associates, has had any substantial interest, direct or indirect, by security holdings or otherwise, in any of the matters to be acted upon in the meeting, other than election to office.

PART III: SIGNATURE PAGE

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this report is true, complete and correct. This report is signed in Makati City on May 17, 2007.

PNOC ENERGY DEVELOPMENT CORP.

By:


Roberto V. San Jose
Corporate Secretary

The Company will provide without charge to each person solicited, upon his written request, a copy of the Company's annual report on SEC Form 17-A duly filed with the Securities and Exchange Commission. At the discretion of Management, a reasonable fee may be charged for the expense incurred in providing a copy of the exhibits. All requests may be sent to the Company's head office and addressed to:

Attention: Mr. Erudito S. Recio
Senior Manager, Investor Relations

PNOC ENERGY DEVELOPMENT CORPORATION

MANAGEMENT REPORT Pursuant to SRC Rule 20

**For the Annual Stockholders' Meeting
On June 14, 2007**

A. Audited Financial Statements for Fiscal Year Ended December 31, 2006

Please refer to the accompanying audited financial statements for 2006.

B. General Nature and Business of the Company

Nature

PNOC Energy Development Corporation (PNOC EDC) was incorporated and registered with the Philippine Securities and Exchange Commission (SEC) on March 5, 1976. It began commercial operations with the commissioning of its first steamfield in 1983 and is now the Philippines' largest producer of geothermal energy. It is primarily in the business of exploring, developing and operating geothermal energy projects in the Philippines.

Prior to its Initial Public Offering (IPO) last December 2006, the Company was a wholly-owned subsidiary of the Philippine National Oil Company (PNOC), a holding company which, through its subsidiaries, engages in the exploration for, development and production of energy resources in the Philippines.

Operational Highlights

From a total sales volume of 8,178 GWh, the Company's gross revenues for 2006 from its steam and electricity business amounted to ₱ 20,747.4 million. As compared to 2005, this is a slight decline in gross revenues and sales volume.

Electricity sales constitute majority of gross revenues at close to 75 % of the total, or at ₱ 15,727.9 million. The balance is split between steam generation and third party drilling services at 24 and 1 % or ₱ 5,019.5 and ₱ 261.4 million, respectively.

Steam Generation

For 2006, steam revenues from the sale of 3,136 GWh amounted to ₱5,019.5 million compared with the 2005 revenues of ₱ 4,967.4 million. The 5.5 GWh drop in surplus steam volume generated was more than compensated for by the ₱ 0.0194 per kwh average increase in price due to inflation adjustments.

The Southern Negros Geothermal Production Field (SNGPF) generated a total sales volume of

1,396 GWh, exceeding its 1,265 GWh take-or-pay volume by as much as 10%, or 131 GWh. Gross revenues amounted to ₱ 2,099.2 million.

In November, production well PN-21D was acidized to increase steam supply capability to NPC's Palinpinon I power plant for it to utilize as much as 105.0 MW, a 9 MW increase from its normal 96 MW.

The Tongonan I Geothermal Production Field contributed 754 Gwh, or approximately 24 % of the total volume sold for the year while sales volume generated by the BacMan Geothermal Production Field (BGPF) continued to be at the take-or-pay level of 986 GWh. For 2006, there was minimal electricity production from the NPC BacMan power plants because of damages sustained as most of the Bicol Region was directly hit by super typhoons "Milenyo" and "Reming" during the last quarter of 2006.

Electricity Generation

For the current year, electricity revenues from the 5,042 GWh sold amounted to ₱ 15,727.9 million. It decreased by ₱ 727.6 million, as compared with the ₱ 16,455.5 million revenues in 2005. The decrease is due to the ₱ 0.0992 per kwh average decrease in electricity prices that resulted from the marked appreciation of the Philippine Peso versus the US Dollar and the appreciable drop in local inflation rates. Furthermore, there was a 71 GWh drop in billed volume due to the reduced nominated energy within NPC's financial capacity for the Leyte BOT power plant and the landslide that affected the Mindanao I & II BOT power plants.

Of the total GWh sales volume, 84 % or 4,244 GWh was generated by the Leyte Geothermal Production Field, the world's largest wet steamfield. Gross revenues for 2006 amounted to ₱ 13,338.6 million as compared to the ₱ 13,874.1 million in 2005.

The Mindanao Geothermal Production Field (MGPF) generated a total sales volume of 798 GWh, exceeding by 10 GWh its minimum energy off-take (MEOT) volume of 788 GWh. PNOC EDC still managed to produce a surplus generation even as it was limited by the time of repair to damages of the Kanlas steamline due to flash floods last August. PNOC EDC personnel fully restored the damaged pipeline in 31 days.

For 2006, revenues from the Mindanao Geothermal Projects reached ₱ 2,389.3 million as compared to the ₱ 2,581.4 million in 2005.

On June 25, 2006, the 125 MW Upper Mahiao Power Plant was transferred to PNOC-EDC by its BOT Contractor CalEnergy. Located in Sitio Upper Mahiao, Kananga, Leyte, it is the world's biggest binary power plant that makes use of the Geothermal Combined Cycle Unit technology.

A number of Electricity Supply Agreements (ESAs) is already in place for the electricity production in Northern Negros Geothermal Project. The first is with the Iloilo I Electric Cooperative, Inc. (ILECO), which was signed last October 2006, covers the supply of approximately 606 GWh over a five-year period. The second is with the Visayan Electric Company, Inc. (VECO), signed in November 2006, for the supply of 635 GWh also for over a five-year period. Plans are underway to find buyers for the electricity to be generated by the power plant from the No. Negros Geothermal Steamfield pursuant to a third ESA.

Third Party Drilling

Third Party Drilling contributed as much as ₱ 261.4 million in 2006 as compared to the ₱ 149.5 million in 2005 primarily from the contract the Company signed off with the Lihir Management Corporation. The contract commenced in August 2005 and was completed in June 2006.

Health, Safety and Environment

Leyte Geothermal Production Field received a Certificate of Recognition from the Department of Energy for attaining 3,329,121 man-hours work with no lost time accident.

The Project also completed geohazard-related activities to avoid landslides even before they happen. The identified high risk areas were the 105 Area and Tower 7.

The BacMan Geothermal Production Field was cited as Region V's eco-tourism destination after the Botong geothermal area was found to serve as habitat of enormous groups of bats known as the golden-crown flying fox (*Acerdon Jubatus*) and large flying fox (*Pteropus vampyrus*). These endangered species are said to be the largest of its kinds and are found only in the Philippines.

Corporate Social Responsibility

PNOC EDC is committed to uplifting the lives of the residents in its host communities as it owes its success not only to its employees but also its stakeholders. As an integral part of its work program, it has always initiated efforts to 1) promote their health, 2) provide educational support, 3) support livelihood development programs and 4) sponsor programs for the environment. In gist, these programs aim to promote social and environmental prosperity through the implementation of a comprehensive, responsive and sustained corporate program on social responsibility, in partnership with its stakeholders and in keeping with its energy objectives.

Following are the Company's accomplishments in 2006:

- **Health Promotion**

Under the Company's 35 medical/dental outreach programs, 3,171 patients received medical treatment/assistance. Other programs conducted by the Company include: 1) feeding and deworming program for 1,346 day care and elementary students; 2) drug abuse awareness trainings for 1,264 students/community members; and 3) trainings on health modules for 570 Health Workers

Five (5) Barangays benefited from the upgrading and construction of their Barangay Health Centers (BHC).

- **Educational Support**

The Company is also an active participant in a quadripartite special education project called "Schools for Excellence" which aims to produce top-quality elementary graduates. It is a 7 year project covering Preparatory to Grade 6 levels in 2 schools located in Ormoc and Kananga, Leyte within the Company's Leyte Geothermal Project. The participants in this project are the Department of Education (DepED), Local Government Unit (LGU), PNOC EDC and parents of the school children. For its part, the Company provides the

needed hardware (classrooms, faculty center, speech laboratory, science laboratory and computer center).

The Company also offers financial support to: 1) high school students, by way of a scholarship program; and 2) elementary students, by providing educational supplies and answering for miscellaneous fees.

▪ **Livelihood Development**

The Company had assisted 85 forest communities in its 5 project sites comprising about 3,742 households, representing 22% of the target 16,900 households in 43 Barangays. There were 36 new livelihood projects established while some 129 existing livelihood projects were improved to enhance their overall economic viability. Integrated and commercially viable livelihood projects (coffee plantation, goat dairy production, and fish culture) were piloted in a number of Barangays. About 664 small-scale contracts amounting to ₱53.69M were created and awarded to associations by the Company to provide for a more viable and stable income source for the recipient communities.

▪ **Environmental Enhancement Projects**

Certain CSR projects were undertaken to increase the awareness and participation of the host communities and employees as stewards of the environment such as, six (6) clean up drives, five (5) tree planting activities, and two (2) solid waste management trainings.

Business of the Issuer

Principal Products or Services and their markets

The Company operates six geothermal steamfields in the four geothermal service contract areas where it is principally involved in:

- (i) the production of geothermal steam for sale to National Power Corporation (NPC) pursuant to Steam Sales Agreements (SSAs) and
- (ii) the production of steam for delivery to Build Operate Transfer (BOT) power plants which convert steam to electricity for sale by PNOC EDC to NPC pursuant to Power Purchase Agreements (PPAs).

Additionally, the Company has evolved into being one of the world's leading geothermal energy producers with the expertise it has accumulated for geothermal energy exploration and development, reservoir engineering and management, drilling, engineering design and construction, environmental management and energy research and development.

In 2006, it provided drilling equipment and rig personnel to the Lihir Management Company.

Percentage of sales or revenues contributed by foreign sales

In addition to the ₱ 20,747.4 million in revenues from steam and electricity sales, the Company generated close to ₱ 261.4 million from the dispatch of personnel and equipment to Lihir, Papua New Guinea on a contract with the Lihir Management Company. This represents only 1.24 % of the Company's gross revenues for 2006.

Distribution methods of products or services

In 2006, all of the 8,178 GWh generated by the Company's from its steam and electricity business was sold to NPC. It is the NPC's responsibility to convey the electricity generated, by either its own or the Company's geothermal power plant, through the high voltage backbone system to distribution utilities, electric cooperatives or bulk power customers.

New Products or Services

Sale of the Company's electricity production from its Northern Negros Geothermal Project shall only commence in 2007. As earlier mentioned, two (2) Electricity Supply Agreements (ESAs) had already been consummated: 1) Iloilo I Electric Cooperative, Inc. (ILECO); and 2) Visayan Electric Company, Inc. (VECO).

Competition

The Company competes against other energy sources used for the production of electricity, particularly coal, natural gas and oil. Of these, coal and oil are imported.

The following table sets out the Department of Energy's estimate of the breakdown of total installed capacity and electricity production by energy source for 2006.

Energy Source	Installed Capacity		Power Generation	
	MW	%	GWH	%
Coal	3,967.0	25.2	15,598.2	27.8
Oil Based	3,829.0	24.3	3,956.9	7.0
Geothermal	1,905.0	12.1	11,458.4	20.4
PNOC EDC	1,149.0	7.3	6,681.0	11.9
Chevron	756.0	4.8	4,777.4	8.5
Hydro	3,217.0	20.4	9,372.8	16.7
Natural Gas	2,763.0	17.5	1,760.8	28.1
Renewable/Others	75.0	0.5	1.3	<.1%
Total	15,756.0	100	56,148.4	100

For the supply of geothermal energy, the only other company operating in the Philippines is Unocal Philippines Inc., recently acquired by Chevron Philippines Geothermal Holdings.

With the Government committed to the privatization of the majority of NPC-owned power generation facilities and the establishment of Wholesale Electricity Spot Market (WESM), the Company will be exposed to a diversified base of Independent Power Producer (IPP) offtakers (at some point in time in the future).

Additionally, non-Philippine companies that are providing geothermal consultancy services in the Asia-Pacific region are West Japan Engineering Consultancy, GeothermEx and Sinclair Knight Merz Engineering Consultancy.

Dependence on one or a few major customers and identity of any such major customers

The Company's 2006 steam and electricity revenues were derived from existing long term supply agreements with NPC.

Patents, trademarks, licenses, franchises, concessions, royalty payments

The four geothermal service contract areas where the Company's geothermal steamfields are located are:

- Leyte Geothermal Production Field (expiring on 2031)
- Southern Negros Geothermal Production Field (expiring on 2031)
- BacMan Geothermal Production Field in Luzon (expiring on 2031)
- Mindanao Geothermal Production Field (expiring on 2017)

These contract areas are located in four islands of the Philippines, namely Luzon, Leyte, Negros and Mindanao. The following table summarizes highlights of the Company's individual steam and electricity sales agreements as of December 31, 2006:

Geothermal Steamfields and Power Plants by Product ⁽¹⁾	Installed Capacity ⁽²⁾ (MW)	Take-or-Pay or MEOT ⁽³⁾ (GWh)	Expiration of SSA or PPA	Transfer of Plants ⁽⁴⁾	Revenue for 2005 (₱ million)	Revenue for 2006 (₱ million)
Steam						
Tongonan I	112.5	739.0	2008	2007/08	1,219.8	1,268.0
Palinpinon I	112.5	739.0	2008	2007/08	1,241.9	1,266.1
Palinpinon II	80.0	526.0	2018	2007/08	902.7	833.1
BacMan I	110.0	723.0	2018	2009/10	1,219.4	1,262.7
BacMan II	40.0	263.0	2019	2009/10	383.6	389.6
Electricity						
Unified Leyte ⁽⁵⁾		4,211.0	2022		13,874.1	13,338.6
Upper Mahiao	125.0			2006		
Malitbog	232.5			2007		
Mahanagdong	180.0			2007		
Optimization	50.9			2007		
Bottoming	14.6					
Topping	36.3					
Mindanao I	52.3	390.0	2022	2009	1,329.0	1,215.7
Mindanao II	54.0	398.0	2024	2009	1,252.4	1,173.5

Notes:

- (1) Product refers to geothermal steam or electricity which the Company supplies to NPC under SSAs or PPAs, respectively. It provides for nearly all of the Company's revenues.
- (2) Installed capacity is the rated gross electrical output of the power plant measured at the generator terminals.
- (3) Take-or-pay and Minimum Energy Offtake ("MEOT") refer to the guaranteed volume of steam and electrical energy, respectively, that NPC guarantees to use each contract year. These are the bases for the minimum payments NPC is required to make to the Company. The take-or-pay volume for steam sales is expressed in equivalent units of electrical energy, GWh, and is computed at 75% of the electrical energy that would be generated if the power plant were running at its installed capacity for the entire contract year. The Minimum Energy Offtake ("MEOT") corresponds to the nominated annual amount of electricity NPC commits to take from the Company-owned power plants (currently at or about 80 to 85 % of plant capacity).
- (4) Transfer of plants means, in relation to the first 5 plants enumerated (the NPC-owned power plants), indicative dates at which these plants are to be sold to the private sector as part of the ongoing restructuring and privatization of the electric power industry in the Philippines. In relation to the 7 remaining plants enumerated (the BOT plants), the date that the plants are transferred from the BOT Contractors to the Company pursuant to the terms of the relevant ECA.
- (5) Unified Leyte consists of the Upper Mahiao, Malitbog, Mahanagdong and Optimization plants in Leyte that deliver electricity to NPC pursuant to a single PPA.

Cost and effects of compliance with environmental laws

The Company's geothermal steamfield and power generation operations are subject to extensive, evolving and increasingly stringent safety, health and environmental laws and regulations. These laws and regulations address, among other things, air emissions, wastewater discharges as well as the generation, handling, storage, transportation, treatment and disposal of toxic or hazardous chemicals, materials and waste, workplace conditions and employee exposure to hazardous substances.

The total cost incurred by the Company to comply with these laws and regulations for the years 2005 and 2006 were approximately ₱ 113.4 million and ₱ 85.8 million, respectively.

Employees and Labor Relations

As of December 31, 2006 the Company had 2,446 employees, of which 1,211 are Managerial, Professional and Technical (MPT) employees. In particular, the distribution of employees by sector is as follows:

Sector	Number	%
General Management	23	1
Environment and External Relations	179	7
Operations	1,202	49
Power and Sales	192	8
Technical Services	564	23
Corporate Services	<u>286</u>	<u>12</u>
Total Headcount	2,446	100

There are ten labor unions, each representing a specific collective bargaining unit allowed by law, within the Company. They are distributed in the different locations as follows:

Name of Union	Location/Project
1. PNOC Energy Group of Employees Association (PEGEA)	Head Office (Fort Bonifacio)
2. National Union of Rig Workers (NURIWO)	Drilling
3. PNOC EDC NNGP Employees Rank and File (PENERFU)	Northern Negros Geothermal Project
4. Demokratikong Samahang Manggagawa ng BGPF/Association of Democratic Labor Unions (DSM-BGPF)	Bacon-Manito Geothermal Production Field
5. Tongonan Workers' Union (TWU)	Leyte Geothermal Production Field
6. Leyte A Geothermal Project Employees' Union (LAGPEU)	Leyte Geothermal Production Field
7. Mt. Apo Workers Union (MAWU)	Mt. Apo Geothermal Production Field
8. PNOC EDC SNGP Rank and File Union	Southern Negros Geothermal Production Field
9. PNOC EDC SNGP Supervisory Association – Association of Professional, Supervisory, Office and Technical Employees Union	Southern Negros Geothermal Production Field
10. PNOC EDC- LGPF and TIPF Association of Technical, Supervisory and Professional Employees	Leyte Geothermal Production Field

These unions enter into regular collective bargaining agreements with the Company as regard to number of working hours, compensation, employee benefits, and other employee entitlements as provided under Philippine labor laws.

Management believes that the Company's current relationship with its employees is generally good. Although the Company is involved in arbitrations with its employees' labor unions, the Company has not experienced a work stoppage as a result of labor disagreements.

Property

The Company is the registered owner of land located in various parts of the Philippines. As of July 16, 2004, these lands were valued by General Appraisal Company (Philippines), Inc., an independent appraiser, at approximately ₱ 1,990.0 million. The Company's landholdings include the site of its principal office in Fort Bonifacio, Taguig, Metro Manila, other parcels used or to be used for its various projects, such as sites for power plants for the Leyte Geothermal Production Field and the Northern Negros Geothermal Project.

The following table sets out certain information regarding the Company's landholdings:

Location/Project	Parcels of Land	Area (hectares)	Under Expropriation	Leased	Acquired	
					w/ title to PNOC EDC	Title for Consolidation
Fort Bonifacio	1	3.27	None	None	1	None
Baguio	1	0.25	None	None	1	None
Bacon-Manito Geothermal Project	104	29.59	None	None	12	92
Northern Negros Geothermal Project	261	153.21	23	111	11	116
Southern Negros Geothermal Project	89	122.93	4	6	0	79
Leyte Geothermal Project	929	502.8	13	2	14	900
Various ⁽¹⁾	8	7.89	None	None	8	None
No. Luzon Wind Project	1,963	456.8	None	1,963	None	None
Total	3,356	1,276.74	40	2,082	47	1,187

Note: (1) Various parcels of land associated with the Company's DES project.

The Company's Head Office is located in an estimated land area of 2.9 hectares within the Energy Center Complex at Merritt Road, Fort Bonifacio, Taguig City. Negotiations are ongoing negotiations for the transfer of the 2.9 hectares to PNOC. Both PNOC and PNOC EDC have agreed to submit for arbitration the issue as regard the sale of the Fort Bonifacio lot by PNOC EDC to PNOC. The Company anticipates that after the land is transferred to PNOC, it may be required to make lease payments to PNOC in respect of the land on which its head offices are located.

Legal Proceedings

Except as disclosed herein, there are no material pending legal proceedings to which the Company is a party or to which any of its material properties are subject. If the Company is not successful in one or more of the proceedings described below, it could incur damages and costs which could be substantial and could have a material adverse effect on the Company's business, financial condition, results of operations and liquidity.

▪ Expropriation Proceedings

Several expropriation proceedings filed by PNOC and DOE to acquire land needed by the Company for certain of its power plants and projects are still pending before various Philippine courts, in particular, in respect of the land requirements for the Leyte Geothermal Production Field, the Southern Negros Geothermal Production Field, and the Northern Negros Geothermal Project. As of December 31, 2006, there were 35 such cases pending and the aggregate amount claimed by the landowners as just compensation is approximately ₱250,341,299. To date, PNOC's and the DOE's authority to expropriate land for the Company's use and the Company's possession of the land expropriated has not been questioned in the pending expropriation proceedings. Generally, the issue in those cases is the amount of compensation to be paid to the owners of expropriated lands. The Company does not expect the final judgement amounts to be the amount claimed.

- **Tax Cases**

- a) ***Real Property Taxes***

In Leyte, the Company has started to negotiate the settlement of the ₱2.0 billion real property taxes assessed against the BOT Power Plants located in the province of Leyte. The settlement of these real property taxes are crucial so that PNOC EDC may be issued the necessary tax clearances required for the transfer of title of the power plant from the respective BOT Contractors. The Upper Mahiao plant was transferred to the Company in June 2006. The rest of the Leyte plants shall be transferred to the Company in the third quarter of 2007.

Also in Leyte province, a ₱2.6 billion assessment is currently under appeal with the Local Board of Assessment Appeals of Tacloban City, docketed as LBAA Case No. 19, entitled PNOC EDC vs. Province of Leyte, et. al., raising as the Company's main argument its tax exemption under the 1981 Geothermal Service Contract with the Republic of the Philippines, and the Local Government Code exemption from real property taxes of machinery and equipment that are actually, directly and exclusively used by GOCC's in the generation and transmission of electric power. At present, there are two (2) pending motions filed by the Province for the termination of this appeal based on the compromise agreement.

Finally, real property tax assessments issued by the City of Taguig and Quezon City, amounting to ₱55.6 million and ₱8.3 million, respectively, on PNOC EDC's Metro Manila properties are likewise currently under negotiation. This notwithstanding, the Company had raised the necessary appeals on these assessments to the respective Local Board of Assessment Appeals.

- b) ***Franchise Taxes***

The province of Leyte has assessed the Company franchise taxes amounting to an aggregate of ₱274,168,686 with respect to the operations from 2000 to 2004 of its geothermal power plants in the province. The Company has filed the corresponding appeals before the Regional Trial Court of Tacloban City, Leyte, docketed as Civil Cases No. 2006-07-77, 2006-05-49, and 2006-05-48, all entitled PNOC EDC vs. Province of Leyte, et. al., seeking the annulment of the assessments. The Company believes that it is not liable for franchise taxes because it does not have the legislative franchise, national or local, necessary so that franchise taxes will accrue. This position is bolstered by the fact that under the EPIRA, power generation is not a public utility activity and does not require a franchise. Moreover, the franchise tax assessment is illegal because the assessed tax was based on the power plant revenues of the BOT operators, and not the Company.

- c) ***Business Taxes***

In February 2006, PNOC EDC's BOT Contractor for the 180 MW Mahanagdong Power Plant, CE Luzon Geothermal Power Company, Inc. (CE Luzon), filed a Complaint against the Municipality of Kananga, et. al., seeking to permanently enjoin the Defendant Municipality from collecting business taxes from the Complainant. The case arose from the assessment made by the Defendant Municipality against the Complainant for business taxes amounting to Php 62 Million covering the period 2001-2003. Despite instituting PNOC EDC as a necessary party in the case, CE Luzon does not seek any adverse relief against the Company.

- **Civil Cases**

The plaintiffs in one case, “Manobo Apao Descendants Ancestral Domain vs. PNOG Energy Development Corporation, et al.”, filed in 2004 before the Regional Trial Court of Kidapawan City, North Cotabato in Mindanao, have claimed that, as indigenous peoples with alleged preferential rights to the natural resources in the Mt. Apo area (including its geothermal reservation), they are entitled to 40% of the Company’s profits and damages in excess of ₱400,000 per household. As indicated, the Mindanao I and Mindanao II geothermal power plants are located in the Mt. Apo geothermal reservation area. The Company moved to dismiss the case, principally by invoking its rights under its GSC and pointing out that the plaintiffs’ alleged rights are limited to their ancestral domain claim which excludes the geothermal reservation. The court has referred the dispute to the National Commission on Indigenous Peoples. To date, nine out of the ten tribal elders that filed the case have executed affidavits of desistance withdrawing their claims.

- **Labor Cases**

As of December 31, 2006, there were 19 pending labor cases against the Company, most of which deal with plaintiffs claiming their employment with the Company had been illegally terminated. In three of these cases, the Company’s President and certain officers and employees were impleaded as party respondents. Although the aggregate monetary amount of the claims in these cases is approximately ₱95,992,549, the Company does not believe that any of them pose a material risk to the Company’s operations..

C. Management’s Discussion and Analysis of Financial Condition and Results of Operations

RESULTS OF OPERATIONS

2006 vs. 2005

Net Sales

Net sales for the year ended December 31, 2006 decreased by ₱563.5 million, or 2.6%, to ₱21,008.9 million from ₱21,572.4 million in 2005 primarily due to the decrease in both the inflation indices and billed volume for electricity sales.

Sales of Electricity

Sales of electricity decreased by ₱727.6 million, or 4.4%, to ₱15,727.9 million in 2006 from ₱16,455.5 million in 2005. The decline was attributed to the combined decrease in average inflation indices by ₱0.0992/KWh, as influenced by the appreciation of Peso against the US dollar, and billed volume by 71 GWh owing to the landslide that affected Mindanao I & II BOT plants in August 2006 and the reduction of nominated energy to within NPC’s financial capacity for the Leyte BOT starting July 25, 2006.

Sales of Steam

Sales of steam increased by ₱52.1 million, or 1.1%, to ₱5,019.5 million in 2006 from ₱4,967.4 million in 2005. The increase was the result of higher average inflation indices in 2006 by ₱0.0194/Kwh. The 2006 surplus generation volume is lower by 5.5 GWh than the 2005 surplus generation volume.

Sales of Drilling Services

Sales from drilling services increased by ₱111.9 million, or 75%, to ₱261.4 million in 2006 from ₱149.5 million in 2005, primarily due to the drilling contract with Lihir Management Corporation in Lihir, Papua New Guinea which began in August 2005 and ended in June 2006.

Cost of Sales

Cost of sales decreased by ₱860.1 million, or 8%, in 2006 to ₱9,936.1 million from ₱10,796.2 million in 2005, primarily due to lower BOT fees on account of the appreciation of the Peso against the US dollar and the expiration of the BOT contract for Upper Mahiao on June 25, 2006.

Operating Expenses

Operating expenses decreased by ₱86.6 million, or 4.5%, in 2006 to ₱1,825.5 million from ₱1,912.1 million in 2005, primarily due to the previous year's higher employee costs attributable to the Company's manpower reduction program.

Other Operating Income

Other operating income increased by ₱702.5 million, or 102.9%, in 2006 to ₱1,385.0 million from ₱682.5 million in 2005, primarily due to the following:

- ₱737.6 million reduction of the provision for doubtful accounts on VAT claims because of BIR's issuance of tax credit certificate in January 2006 for the VAT refund claim amounting to ₱811.2 million.
- ₱125.0 million fair value of the Upper Mahiao Power Plant materials inventory turned over the BOT contractor at the end of the ten-year cooperation period.
- ₱77.8 million prior year' interest income

The foregoing income items were reduced by the ₱227.6 million combined drop in prior year's inflation adjustments both for electricity and steam sales, amounting to ₱126.5 million and ₱101.1 million, respectively, due to the effect of the Peso appreciation against the US Dollar.

Other Operating Expenses

Other operating expenses increased by ₱979.5 million to ₱1,069.3 million in 2006 from ₱89.8 million in 2005 mainly due to the ₱554.9 million prior years' foreign exchange adjustments coupled with the ₱462.0 million adjustments of prior years' expenses.

The ₱554.9 million foreign exchange adjustments were traced primarily to the following:

- ₱559.7 million foreign exchange loss on the amortization adjustments of Malitbog's BOT lease obligation due mainly to the one year billing period not included in computing the net present value of the plant and BOT lease obligation;
- ₱0.9 million foreign exchange gain on the adjustments of the Mindanao I's BOT lease obligation due to the extension to 2009 of the energy conversion agreement which would mature in 2007.
- ₱3.9 million foreign exchange gains on various prior years' transactions.

The ₱462.0 million prior year's expense adjustments were largely accounted for by the following:

- ₱285.7 million recognition of additional guarantee fees on outstanding long-term loans
- ₱70.0 million adjustment of Upper Mahiao's BOT obligation amortization which ended in June 2006.
- ₱66.5 settlement of previously contested energy efficiency billings in accordance with the provision of the Mindanao I's extension agreement executed on November 17, 2006..

Finance Costs

Finance costs decreased by ₱11.4 million, or 0.5%, to ₱2,099.0 million in 2006 from ₱2,110.3 million in 2005. This decrease was brought about by the full payment of JP Morgan Chase and BOTM foreign loans in 2006 and the appreciation of Peso against the US Dollar.

Foreign Exchange Loss (Gain)

The Company posted lower foreign exchange gain of ₱3,533.5 million, or 55.1%, to ₱2,885.1 million in 2006 from ₱6,418.6 million in 2005 primarily due to lower depreciation of the Yen against the US Dollar despite the higher appreciation of the Peso against the US Dollar this year as compared to the 2005 exchange rates.

Benefit from (Provision for) Income Tax

Current taxes increased by ₱20.6 million or 1.2%, to ₱1,698.0 million in 2006 from ₱1,677.4 million in 2005 mainly due to the increase in income tax rate from 32% to 35% starting November 2005 coupled with this year's higher taxable income.

Deferred taxes decreased by ₱303.4 million, or 14%, to ₱1,868.2 million in 2006 from ₱2,171.6 million in 2005 mainly because of lower unrealized foreign exchange gain on realignment of long-term loans in 2006 offset by the reduction in 2006 of the allowance for doubtful accounts on VAT claim from the BIR - issued with TCC on January 31, 2006.

Net Income

As a result of all the foregoing, net income decreased by ₱3,133.2 million, or 31.6%, to ₱6,782.9 million in 2006 from ₱9,916.1 million in 2005. In 2006, net income represented 32.3% of total revenue compared to 46% of total revenue in 2005, primarily due to lower foreign exchange gains.

2005 vs. 2004

Net Sales

Net sales for 2005 increased by ₱927.9 million, or 4.5%, to ₱21,572.4 million from ₱20,644.5 million in 2004 primarily due to higher sales volume of Unified Leyte on account of higher Nominated Energy level recognized by NPC, in addition to higher average inflation indices.

Sale of Steam

Sales of steam increased by ₱281.7 million, or 6.0%, to ₱4,967.4 million in 2005 from ₱4,685.7 million in 2004. The increase was a result of higher average inflation adjustment for steam although the billed volume of 3,141 GWh in 2005 was less than the billed volume of 3,162 GWh in 2004. The decrease in sales volume was due to the Cawayan Power Plant's surplus generation in 2004 and lower surplus generation of Tongonan I and Palinpinon II due to NPC's lower dispatch in 2005 compared to 2004.

Sale of Electricity

Sales increased by P498.3 million, or 3.0%, to ₱16,455.5 million in 2005 from ₱15,957.2 million in 2004 on account of a higher accepted Nominated Energy level under the Unified Leyte PPA from 4,177 GWh for the period January to July 2004 compared to 4,268 GWh starting in August 2004 through to the end of 2005, and an increase in average electricity prices due to higher inflation indices.

Sale of Drilling and Consultancy Services

Sales were P149.5 million in 2005 compared to ₱1.6 million in 2004. The increase was attributable to the new drilling contract with LMC in Papua New Guinea. Operations under the LMC contract began on August 22, 2005.

Cost of Sales

A decrease of ₱804.1 million, or 6.9%, from ₱11,600.3 million in 2004 to ₱10,796.2 million was posted in 2005. The reduction was primarily accounted for by lower BOT fees due to the appreciation of the Peso against the Dollar in 2005.

Other Operating Income

A decrease of ₱505.7 million, or 42.6%, from ₱1,188.2 million in 2004 to ₱682.5 million was recorded in 2005. The decrease mainly arose from a one time ₱480 million adjustment in 2004 (in compliance with PAS No. 21 (The Effects of Changes in Foreign Exchange Rates) on foreign exchange losses on BOT lease obligations to reflect the variation between the contracted energy originally used in the establishment of the BOT lease obligation as compared to the nominated capacity fees actually paid

Operating Expenses

A decrease of ₱252.3 million, or 11.7%, from ₱2,164.4 million in 2004 to ₱1,912.1 million was recorded in 2005. This was primarily due to the payment of arrangement, agency and legal fees

relating to a \$75 million syndicated five-year term loan in 2004 coupled with 2005's lower insurance expenses due to reduction in premium rates and lower provision for doubtful accounts.

Other Operating Expenses

A decrease of P709.4 million, or 88.8%, from P799.2 million in 2004 to P89.8 million was recorded in 2005. This was caused mainly by the ₱361 million accelerated amortization of wells and the ₱315 million adjustment on account of the DOE-mediated resolution of the Company's and NPC's contract implementation issues in 2004.

Finance Costs

An increase of ₱290 million, or 15.9%, from ₱1,820.4 million in 2004 to ₱2,110.3 million was reported in 2005. This was due to the increase in interest expense related to a \$75 million syndicated five-year loan in August 2004 and a ₱1.5 billion loan from Land Bank of the Philippines which were drawn down from August 2004 to December 2005.

Foreign Exchange Loss (Gain)

Foreign exchange gains were ₱6,418.6 million in 2005 compared to a ₱1,938.2 million foreign exchange losses in 2004. The gain was accounted for by the effect of the depreciation of the Yen and appreciation of the Peso against the Dollar (¥117.855 : ₱ 53.062 at the end of 2005; ¥103.050 : ₱ 56.341 at the end of 2004) on the Company's outstanding obligations.

Benefit from (Provision for) Income Tax

Current tax expense increased by P557.0 million or 49.7%, to P1,677.4 million in 2005 from P1,120.4 million in 2004. This was due largely to lower deductible expenses pursuant to the GSC of the entire Palanpinon area of 30% in 2005 compared to 65% in 2004, higher BOT electricity sales in 2005 and the accelerated amortization of the NNGP CT-1D well and the Victoria project in 2004.

A deferred tax liability of ₱2,171.6 million was recognized in 2005 on account of the foreign exchange gains in contrast with the ₱51.9 million deferred tax assets from foreign exchange losses in 2004.

Net Income

As a result of all the foregoing, net income increased by ₱7,474.4 million, or 306.1%, to ₱9,916.1 million in 2005 from ₱2,441.7 million in 2004 due to foreign exchange gains. In 2005, net income represented 46% of total revenue compared to 12% of total revenue in 2004, primarily due to foreign exchange gains in 2005, in contrast to foreign exchange losses in 2004.

First Quarter 2006 vs. First Quarter 2005

Please refer to attached SEC Form 17Q.

FACTORS AFFECTING THE COMPANY'S RESULTS OF OPERATIONS

Set out below are some of the more significant factors that have affected and continue to affect the Company's results of operations.

▪ *The Company's Relationship with NPC*

Contractual framework. As per the Company's SSAs and PPAs with its only customer, NPC is obligated to pay for a minimum quantity of steam and electricity pursuant to its take-or-pay and minimum energy offtake (MEOT) obligations. The average remaining life on these contracts are 7 and 15-year for the SSA and PPAs, respectively. The Company and NPC, through mediation by the DOE, are continuing to work on a settlement agreement in respect of disputed billings amounting to ₱ 3,117.6 million.

▪ *Exchange Rate Fluctuations*

The Company's accounting records and financial statements are prepared in Pesos, although its payments for debt service, BOT fees and major materials and services are denominated substantially in US Dollars and Japanese Yen. Changes in the exchange rate between the Peso and foreign currencies also influence the cost, in Peso terms, of the Company's Dollar-denominated and Japanese Yen-denominated borrowings, as well as the Peso value of such borrowings in the Company's balance sheet.

In 2005 and 2006, the Company recorded a foreign exchange gain of ₱ 6,418.6 million and ₱ 2,885.1 million, respectively.

Also, the unit prices for majority of the SSAs and PPAs are indexed to movements in the US Dollars vis-a-vis the Philippine Peso. Changes in the exchange rate between the two currencies influence the rate at which the Company's gross revenues change as the individual steam and electricity prices are either inflated or deflated.

FINANCIAL CONDITION

Financial Statements	2006	2005	2004
a) Cash and Cash Equivalents			
Cash in Bank (Peso)	8	9	10
Cash in Bank (US\$)	17	385	1
Cash in Bank (Yen)	2	95	61
Marketable Securities (Peso)	9,705	3952	404
Marketable Securities (US\$)	267	9	370
Total	9,999	4,450	846
b) Accounts Receivables – Others			
Unapplied withholding taxes/tax certificates	711	-	-
Others	146	239	342
Total	857	239	342
c) Selling and Administrative Expenses			
Administrative charges	700	775	961
Employee costs	314	426	381
Provision for doubtful accounts	299	239	301

Financial Statements	2006	2005	2004
Rent, insurance and taxes	217	163	229
Purchased services and utilities	159	143	137
Materials and supplies	48	39	28
Depreciation and amortization	42	87	89
Maintenance and repairs	12	10	11
Business and others expense	34	30	25
Provision for impairment in the value of assets	-	-	2
Total	1,825	1,912	2,164
d) Other Income, Interest Expense and Others			
Interest income	330	368	412
Interest expense	2,099	2,110	1,820
Foreign exchange gain (loss)	2,885	6,419	(1,938)
Miscellaneous	2,124	404	1,575
Total	7,438	9,301	1,869

▪ **2006**

The Company's total resources as of December 31, 2006, amounted to ₱75,140.6 million, 7.35% or ₱5,145.5 million higher than the December 31, 2005 year-end level of ₱69,995.1 million. PNOC EDC's debt ratio improved to 56:44 as of December 31, 2006 from 78:22 of December 31, 2005. Current ratio stood at 1.64, better than 0.79 last year. The Company's 2006 year-end debt ratio and current ratio passed the ratios required by the World Bank.

Trade and other receivables decreased by ₱221.2 million (4.8%) on account primarily on the collection of inflation adjustment and surplus billings for 2005.

Parts and supplies inventories increased by ₱204.2 million mainly traceable to additional requisition for:

- Construction & hardware supplies, office supplies and other spares & supplies (12/06 - ₱141.2 million vs. 12/05 - ₱15.4 million) increased by ₱125.8 million.
- Drilling tubular products and equipment spares (12/06 - ₱515.5 million vs. 2/05 - ₱468.4 million) higher by ₱47.1 million.
- Chemical, chemical products, gases & catalyst (12/06 - ₱94.5 million vs. 12/05 - ₱65.4 million) up by ₱29.1 million.

Investment in available-for-sale securities went down by ₱1,448.0 million primarily due to the maturity of retail treasury bonds.

Other current assets increased by ₱1,355.0 million attributed to prepayment to contractors to draw from the OECF 21st Yen loan for Northern Negros Geothermal Power Plant.

Exploratory and development costs increased by ₱788.2 million mainly due to higher development costs in Northern Negros Geothermal project and Leyte project.

Other noncurrent assets went down by ₱451.4 million on account mainly of the reclassification of the tax credit certificate and prepayment to contractors for Northern Negros Geothermal Power Plant.

Trade and other payables decreased by ₱47.1 million on account primarily of lower accrued capacity fees for the BOT plants due to the full payment of BOT lease obligations for Upper Mahiao power plant in June 2006.

Royalty fee payable went up by ₱198.4 million triggered by higher accrual of royalty fee payable to the Department of Energy for the Southern Negros Geothermal Project – Palinpinon I.

BOT lease obligations were reduced by ₱4,656.0 million mainly due to repayment of capital cost recovery fees to BOT contractors.

Long-term debt went down to ₱35,697.7 million from December 31, 2005 balance of ₱40,524.0 million on account mainly by the full payment of loans obtained from JP Morgan Chase and Bank of Tokyo Mitsubishi, which were partly trimmed down by loan availment from OECF in 2006.

Equity increased by ₱16,082.2 million on account of the additional subscribed capital of five billion shares in 2006, excess over the par value of the three billion primary shares sold in December 13, 2006 and the net income for the year under retained earnings- unappropriated.

▪ 2005

Total resources as of December 31, 2005, aggregated ₱69,995.1 million, slightly lower by ₱1,989.4 million than the 2004 year-end level of ₱71,984.5 million. The decline was attributed mainly to the withdrawal of deposit from BSP for payment of BOT fees. The Company's debt ratio recovered from 97:03 as of December 31, 2004 to 78.22 as a result of the net income from operations. On the other hand, the current ratio went down to 0.79:1 from 0.85:1 in 2004. Both ratios failed to meet the required ratios by the World Bank.

Cash and cash equivalents increased by ₱3,603.8 million mainly from internally generated funds from operations and proceeds of loan from OECF 21st yen and Land Bank of the Philippines.

The soaring inflation indices and the increase in average steam/electricity sales price mainly accounted for the ₱143.2 million upturn in receivables-net.

The investment in available-for-sale securities of ₱2,726.6 million as of December 31, 2005 pertain mainly to the reclassification of investments from other current assets account in compliance with Philippine Accounting Standard (PAS) Nos. 32 and 29.

Income tax payable increased by ₱1,296.7 million as the liability for the 3rd quarter of 2004 up to 3rd quarter of 2005 were only paid in 2006 since income tax computations for 2004 and 2005 were reverted back to finance lease method for BOT transactions.

BOT lease obligations decreased by ₱6,836.2 million on account of the repayment of capital cost recovery fees to BOT contractors and foreign exchange gains on realignment of outstanding loans due to the appreciation of the peso against the US dollar.

Long-term debt was reduced by ₱7,549.1 million primarily due to foreign exchange gains on realignment of outstanding loans on account of the depreciation of yen and appreciation of peso against the US dollar.

Equity went up by ₱10,026.4 million on account of the ₱9,916.1 million earnings for the period ended December 2005 and unrealized gain in cost versus fair value of investment securities in compliance with PAS Nos. 32 and 39.

CASH FLOWS

▪ 2006 vs. 2005

PNOC EDC registered a net cash from operating activities of ₱5,219.5 million this year, lower than the year-to-date level in December 2005 of ₱11,023.8 million owing to higher cash paid to suppliers and employees by ₱2,972.3 million and the payment of income tax due for the years 2004 and 2005 of ₱1,933.9 million since income tax computation was reverted to finance lease method for BOT transactions after resolving the issue with the BIR.

Net cash used for investing activities went up to ₱2,254.7 million during the year, ₱1,575.2 million higher compared to the 2005 level of ₱679.5 million. This was primarily accounted by the ₱2,935.1 million capital expenditures largely for the Northern Negros Geothermal Project. The ₱1,274.0 million inflow from the maturity and pre-termination of the investments available for sale was used for working capital requirements.

The Company posted in 2006 ₱2,584.3 million net cash from financing activities as compared to the ₱6,740.6 million net cash used for financing activities. The ₱9,324.9 turnaround was primarily due to the ₱9,413.2 million proceeds from the IPO offering. Other offsetting factors include the ₱1,123.9 million increment in payments to long-term debt due to start of the principal amortization of the US\$90 million 5-year term-loan and the ₱1.5 billion loan from Land Bank of the Philippines and the ₱747.2 million drop in the payment of the BOT lease obligations. For temporary funding gap, short-term financing of ₱1,1150.0 million was drawn against existing credit lines in 2006, which was also paid within the year.

▪ 2005 vs. 2004

PNOC EDC registered a higher net cash from operating activities of ₱11,023.8 million this year compared with ₱2,072.3 million last year due to lower cash paid to suppliers ₱4,162.4 million on account of the deferral of drilling activities coupled with the non payment of income tax due ₱1,933.9 million as income tax computation was based on operating lease method. Cash receipts from customers were higher by ₱2,865.3 million due to the collection in 2005 of the November 2004 receivables and prior year's inflation adjustments from the NPC.

Net cash used for financing activities increased by ₱1,183.4 million in 2005 as compared to the 2004 level of ₱5,557.1 million mainly due to the ₱2,045.4 million drop in loan drawdown on account of the full availment of US\$ 75 million loan in December 2004 and the ₱101.8 million increase in payment of long term debt, which were offset by the ₱630 million decline in payment of BOT lease obligations on brought about by the peso appreciation against US dollar.

First Quarter 2006 vs. First Quarter 2005

Please refer to attached SEC Form 17Q.

Top Five (5) Key Performance Indicators

Ratio	Dec - 06	Dec - 05
Current Ratio	1.64:1	0.85:1
Debt-to-Equity Ratio	1.28:1	3.44:1
Net Debt-to-Equity Ratio	0.92:1	3.07:1
Return on Assets (%)	9.3	13.9
Return on Equity (%)	34.25	146.9

Exchange Rate Volatility

Any volatility in the exchange rate implies not only cost uncertainties for PNO-EDC, both in terms of operating and capital expenses, but also the level of its revenues. As the peso depreciates the cost of imported products increases, which is the same for net sales since some sales agreements have included as component in their inflator indices the peso-dollar volatility. Conversely, as the peso appreciates, costs decrease but net sales also decrease.

The peso was one of Asia's strongest performing currencies in 2006, which continued into the first six weeks of 2007. The local currency gained its strength from a number of factors, including the improving fiscal outlook, record levels of workers' remittances, the ending of monetary policy tightening in the US and booming exports.

The peso appreciation has its positive and negative impact to the Philippine economy. The negative impact is that Philippine exports become less competitive in the international market as they become relatively more expensive. Meanwhile, the positive impact is that inflation is lowered by cheaper imports, especially oil and other raw materials used by the manufacturing sector. An appreciating peso is largely beneficial to firms that import a lot of their raw materials.

Inflation and Interest Rates

Inflation averaged 6.2 percent in 2006 compared to the 7.6% level registered in 2005. Given the favorable inflation rate and positive developments in the government's financial position, interest rates will remain at relatively low levels beginning 2007. In 2006, the 91-day T-bill rate averaged at 5.35 percent.

Any events that will trigger direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation

The Company has entered into long-term loan arrangements with domestic and international financial institutions, including the JBIC, the World Bank, Land Bank of the Philippines, JP Morgan Chase and Bank of Tokyo Mitsubishi, and term loans syndicated by ING and Standard Chartered Bank for its various development projects and working capital requirements. For some of these loans, the Government or PNO-EDC is the initial borrower with sub-lending arrangements with the Company. For other loans the Company is the borrower with the obligations guaranteed by the Government. In these transactions, the Company pays a guarantee fee of 1% on the outstanding balance to the Government. The Company is required to abide by procurement standards and procedures established by the lenders for capital expenditure financed through respective loans.

Certain of the Company's long-term loans, such as those obtained from the World Bank contain financial covenants. Under its obligations with the World Bank, the Company was required to maintain (i) a ratio of current assets to current liabilities of not less than 1.0:1, (ii) a ratio of debt to equity not greater than 70:30 and (iii) a debt service ratio (estimated net revenues divided by estimated debt service requirements) of 1.21:1 or 1.25:1. Since 1999, the Company has been unable to maintain the financial ratios set out in its World Bank loans. However, the Company has received a waiver from the World Bank for each year that it has not been able to meet its financial ratios from 1999 to 2005. In November 2006, the Company and the World Bank entered into certain amendments to the financial ratios set out above and the Company does not require a waiver for 2006.

Under the US\$90 million syndicated five-year loan facility guaranteed by the Government in 2003, the Company is required to maintain a debt service ratio of 1.1:1. The \$75 million syndicated 5-year term loan guaranteed by the Government, the Company is also required to maintain a debt service ratio of 1:1.

Future Prospects

Over the past 15 years, there has been a significant increase in the global demand for environment-friendly sources of energy as a number of international conventions that assign emission quotas to countries have come into effect. The Company is at the forefront of this growing global demand for clean energy. All of the Company's existing geothermal projects produce electricity from resources that are clean, renewable and generally sustainable. Unlike electricity produced from burning fossil fuels, electricity produced from geothermal resources is produced without emissions of certain harmful pollutants, such as nitrogen oxide and with far lower emissions of other pollutants, such as carbon dioxide.

Such clean and renewable characteristics give the Company a competitive advantage over fossil fuel-based electricity generation as the Philippines and other countries increasingly seek to balance environmental concerns with demands for reliable sources of electricity. Additionally, the price of renewable energy, such as geothermal energy, is not necessarily tied to the cost of crude oil which has risen steadily over the past several years. The Company believes that this fact will also help increase the global demand for its expertise and services.

Any significant elements of income or loss (from continuing operations)

There were no significant elements of income or loss from continuing operations.

Seasonal aspects that has material effect on the FS

There were no seasonal items that materially affect the financial statements.

All material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the company with unconsolidated entities or other persons created during the reporting period

During the reporting period, there were no off-balance sheet transactions, obligations and arrangements with unconsolidated entities or persons.

Material Commitments for Capital Expenditures

The Company has budgeted capital expenditures of approximately ₱2,981.2 million for 2007. The planned 2007 capital expenditures include the expenditures of ₱1,355.0 million relating to the North Luzon Wind Power Project Phase I, whose bids for the wind farm are already under technical evaluation and prequalification of bidders for the transmission line is set in April 2007.

D. Information on Independent Accountant / External Auditor

The Company's audited financial statements are prepared by the Commission on Audit in compliance with Philippine law.

There is no other assurance and related services rendered by the external auditor. There are no other services provided by the external auditor other than the services reported above.

Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

Since 1987, the Commission on Audit of the Philippines has served as the external auditor of the Company to audit the Company's financial statements and the Company has not had any material disagreements on accounting matters or financial disclosure matters with the Commission on Audit.

Audit and Audit-Related Fees

The following table sets out the aggregate fees billed for each of the last three fiscal years for professional services rendered by the Commission on Audit.

	Year-ended December 31,		
	2004	2005	2006*
Audit Fees (in Pesos)	<u>1,800,000.00</u>	<u>2,000,000.00</u>	<u>1,500,000.00</u>

*This only covers the audit fees for audit of the 2006 interim financial statements relative to the IPO offering.

Except the foregoing, there are no other tax fees billed by the Commission on Audit. Neither has the Commission on Audit performed services other than the ones mentioned above.

E. Market Price of and Dividends on the Registrant's Common Equity

Market Information

The Company's common equity was listed in the Philippine Stock Exchange last December 13, 2006 at an Initial Public Offering price of ₱3.20 per share. The high and low share prices for December 2006 are indicated in the following table:

Period	Highest Close		Lowest Close	
	Price	Date	Price	Date
December 2006	₱4.85	Dec. 29, 2006	₱4.15	Dec. 14, 2006

Price as of last trading day of the year, December 29, 2006, was ₱4.85 per share. As of May 11, 2007, the Company's trading price closed at P 5.70 per share.

Dividends

The Company has declared dividends in the last two fiscal years, as follows:

Date of Board Approval	Amount (₱ thousands)	Nature of Dividends Declared
September 2006	2,000,000	Stock dividend

The Company's Board of Directors is authorized to declare dividends. Stock dividend declaration requires the further approval of stockholders representing at least two-thirds of the stockholders of record entitled to vote of the Company's outstanding capital stock. The Corporation Code defines the term "outstanding capital stock" to mean the "total shares of stock issued" regardless of nomenclature, classification or voting rights, "except treasury shares." Such stockholders approval may be given at a general or special meeting duly called for the purpose. Dividends may be declared only from unrestricted retained earnings. Some of the Company's loan agreements carry covenants that restrict declaration or payments of dividends under certain circumstances.

Subject to the availability of unrestricted retained earnings, holders of common shares are entitled to receive annual cash dividends of at least 30% of the prior year's recurring net income based on the recommendation of the Board of Directors. Such recommendation will take into consideration factors such as current and prospective debt service requirements and loan covenants, the implementation of business plans, operating expenses, budgets, funding for new investments and acquisitions, appropriate reserves and working capital, among others. In this connection, covenants in certain loan agreements entered into by the Company restrict the distribution of dividends to the Company's stockholders if such distribution will impair the Company's ability to pay its obligations or if an event of default or a prospective event of default (as defined in the loan agreement) has occurred and has not been remedied to the satisfaction of the creditor(s).

Stockholders

The total number of stockholders as of December 31, 2006 was 2,480.

As of March 31, 2007, the total number of stockholders was 1,010.

List of Top 20 Stockholders as of March 31, 2007

Rank	Name	Nationality	No. of Shares	%
1	Philippine National Oil Company	Filipino	8,999,999,991	40.00
2	PCD Nominee Corporation	Foreign	5,253,856,354	35.03
3	PCD Nominee Corporation	Filipino	724,790,646	4.83
4	Domingo U. Lim	Filipino	2,000,000	0.01
5	ALG Holdings Corporation	Filipino	700,000	0.00
6	Manuel S. Ogena	Filipino	600,001	0.00
7	The Insular Life Assurance Co., Ltd.	Filipino	600,000	0.00
8	Rosalind Camara	Filipino	531,000	0.00
9	Peter &/or Annabelle C. Mar	Filipino	400,000	0.00
10	Marcelino M. Tongco	Filipino	330,001	0.00
11	Northwest Insurance & Surety Co. Inc.	Filipino	300,000	0.00
12	Hans T. Sy	Filipino	300,000	0.00
13	Edgar V. Cadungog	Filipino	250,000	0.00
14	Catherine L. Tan	Filipino	250,000	0.00
15	Miguel T. Tan	Filipino	250,000	0.00
16	Engracio A. Sanchez	Filipino	220,000	0.00
17	Agnes C. de Jesus	Filipino	200,001	0.00
18	Asuncion J. Espina	Filipino	200,001	0.00
19	Danilo M. Capapas	Filipino	200,000	0.00
20	Daniel D. Tagaza	Filipino	200,000	0.00

Company's Share Capital

The Company's securities consist entirely of common shares. As of December 31, 2006, the total authorized and outstanding capital stocks consist of 15,000,000,000 shares with a par value of ₱1.00 per share.

Each common share is equal in all respects to every other common share. All the common shares have full voting and dividend rights. The rights of Company's shareholders include the right to notice of shareholders' meetings, the right of inspection of the Company's corporate books and other shareholders' rights contained in the Corporation Code. Notice of shareholders' meetings is provided by mail or by hand.

Holders of common shares are entitled to receive annual cash dividends of at least 30% of the prior year's recurring net income based on the recommendation of the Board of Directors. Such recommendation will take into consideration factors such as current and prospective debt service requirements and loan covenants, the implementation of business plans, operating expenses, budgets, funding for new investments and acquisitions, appropriate reserves and working capital, among others. In this connection, covenants in certain loan agreements entered into by the Company restrict the distribution of dividends to the Company's stockholders if such distribution will impair the Company's ability to pay its obligations or if an event of default or a prospective event of default (as defined in the loan agreement) has occurred and has not been remedied to the satisfaction of the creditor(s).

E. Compliance with Corporate Governance Practices

Manual on Corporate Governance

On November 15, 2006, the Company adopted a Manual on Corporate Governance (the “Manual”). The Manual principally sets forth the principles and practices of good corporate governance to be followed by the Company and to be observed by its Directors, Officers and Employees. It provides for the responsibilities and fiduciary duties of the Board of Directors as well as the individual directors consistent with sound corporate governance.

To ensure compliance with the principles of corporate governance, the following Committees were created by the Board of Directors:

Audit and Governance Committee

The Company’s Audit and Governance Committee will be composed of at least a majority of independent Directors and shall be chaired by an independent Director. The Audit and Governance Committee shall be principally tasked with the review of financial statements; the conduct of oversight function in the management of the Company’s internal controls; and the review of Internal Audit’s plans, activities, organizational structure and effectiveness in complying with the International Standards for the Professional Practice of Internal Auditing. The Committee’s Charter also reflects such other duties and responsibilities involving oversight and review of potential conflicts of interest and related party transactions.

Nominations and Compensation Committee

The Nominations and Compensation Committee will be composed of three Directors, one of whom will be an independent director, who shall be the Chairman of the Committee. The committee’s charter includes the following duties and responsibilities: to pre-screen and qualify candidates nominated for any vacancies on the Board in accordance with prescribed standards; to consider and recommend to the Board the disqualification of any director for established grounds; to conduct an annual Board evaluation process to assess the effectiveness of the Board; and establish the terms of reference, competencies and qualifications required for the selection of senior executives of the Company, including the CEO and Vice Presidents, which shall include, among others, commercial, financial and/or technical experience and expertise in running a business enterprise; to establish a formal and transparent procedure for developing a policy on executed remuneration and for fixing the remuneration packages of corporate officers and directors; to recommend to the President and/or the Board changes pertaining to compensation and benefits of President/CEO, Vice Presidents and Senior Managers; to undertake any special projects or investigations which the Board or President may request.

Risk Management Committee

The Risk Management Committee shall be composed of three directors. It shall have the following duties and responsibilities: assist the Board in its oversight responsibility over Management’s activities in managing the identified risks affecting the Company; conduct of yearly evaluation of the Company’s risk assessment and risk management programs; recommend risk mitigation/control measures; review periodically the security, safety and physical loss control measures and the specific Emergency Response Team adopted by the Company to ensure compliance with measures intended to cover all identified risks.

Procurement Committee

The Procurement Committee, which is composed of three (3) members of the Board, principally tasked with exercising oversight functions over the Bids and Awards Committee (BAC), as well as reviewing and approving award of contracts for procurement of goods and services of more than P5 Million but not more than P50 Million.

Independent Directors

The By-Laws of the Company provides for the election three (3) independent directors, who shall pass the qualifications provided for by law and the Manual, as certified and nominated by the Nominations and Compensation Committee. The election of the independent directors is scheduled in the annual stockholders' meeting to be held in June 2007.

Corporate Secretary and Assistant Corporate Secretary

The Board has already elected Atty. Roberto V. San Jose and Atty. Ana Maria A. Katigbak, as Corporate Secretary and Assistant Corporate Secretary. The Corporate Secretary and Assistant Corporate Secretary shall implement such corporate governance improvements to be adopted by the Board from time to time, as well as conduct and/or organize corporate governance training and seminars for the members of the Board.

Compliance Officer

The President has appointed Atty. Michael A. Medado as the Compliance Officer, and his appointment has been duly disclosed to the Securities and Exchange Commission (SEC).

The Company will provide without charge to each person solicited, upon his written request, a copy of the Company's annual report on SEC Form 17-A duly filed with the Securities and Exchange Commission. At the discretion of Management, a reasonable fee may be charged for the expense incurred in providing a copy of the exhibits. All requests may be sent to the Company's head office and addressed to:

**Attention: Mr. Erudito S. Recio
Senior Manager, Investor Relations**



PNOC ENERGY DEVELOPMENT CORPORATION

Merritt Road, Fort Bonifacio, 1200 Taguig City, Philippines
P.O. Box 2102 MCPO, Tel. Nos. 893-6001 to 47/893-1320 Fax No. 840-1575

**STATEMENT OF MANAGEMENT'S RESPONSIBILITY
FOR FINANCIAL STATEMENTS**


The management of PNOC Energy Development Corporation is responsible for all information and representations contained in the financial statements for the years ended December 31, 2006 and 2005. The financial statements have been prepared in conformity with generally accepted accounting principles in the Philippines as set forth in Philippine Financial Reporting Standards (PFRSs) and the applicable practices of the oil and gas industry not covered by PFRS/PAS and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration to materiality.

In this regard, management maintains a system of accounting and reporting which provides for the necessary internal controls to ensure that transactions are properly authorized and recorded, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The management likewise discloses to the company's audit committee and to its external auditor: (i) all significant deficiencies in the design or operation of internal controls that could adversely affect its ability to record, process, and report financial data; (ii) material weaknesses in the internal controls; and (iii) any fraud that involves management or other employees who exercise significant roles in internal controls.


The Board of Directors through its Audit and Governance Committee reviews the financial statements before such statements are authorized for issue.

The Commission on Audit, the constitutional body mandated to audit government-owned-and-controlled corporations, has examined the financial statements of the company in accordance with generally accepted auditing standards in the Philippines and has expressed its opinion on the fairness of presentation upon completion of such examination, in its report to the Board of Directors and stockholders.

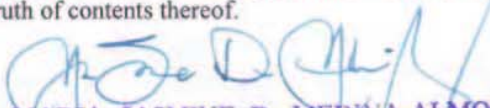
Signed under oath by the following:


ANTONIO M. CAILAO
Chairman of the Board


PAUL A. AQUINO
President and Chief Executive Officer


FENINA O.T. RODRIGUEZ
Treasurer and Chief Financial Officer

SUBSCRIBED AND SWORN TO before me, a Notary Public for and in the City of Taguig, Metro Manila, this MAY 04, 2007, affiants being personally known to me and signed this instrument in my presence and avowed under penalty of law to the whole truth of contents thereof.


ATTY. MARIA JASMINE D. MEDINA-ALMOGINO
Notary Public for the City of Taguig until 12/31/2008
Appointed by ... 58 (2007-2008)
3rd Floor, ... Energy Center
Merritt Road, Fort Bonifacio, Taguig City
Roll No. 40123, 05/23/01
PTR No. 0096130-A, 1/09/07, Taguig City
IBP No. 694547, 12/15/06, Pasig City

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Republic of the Philippines
COMMISSION ON AUDIT
Commonwealth Ave., Quezon City, Philippines

STATE AUDITOR'S REPORT

The Stockholders and Board of Directors

PNOC Energy Development Corporation

We have audited the accompanying financial statements of **PNOC Energy Development Corporation** (a subsidiary of the Philippine National Oil Company), which comprise the balance sheet as of December 31, 2006, and the income statement, statement of changes in equity and cash flow statement for the year 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.

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 financial statements present fairly, in all material respects, the financial position of the **PNOC Energy Development Corporation** as of December 31, 2006, and its financial performance and cash flows for the year then ended in accordance with Philippine Financial Reporting Standards.

COMMISSION ON AUDIT



ROLAND A. REY
Director IV

March 27, 2007



PNOC ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)

BALANCE SHEET

December 31, 2006

(With comparative figures for 2005)

In Philippine Peso

	Notes	2006	2005
ASSETS			
Current Assets			
Cash and cash equivalents	4	9,999,202,227	4,450,089,945
Cash - restricted	5	33,212,957	-
Trade and other receivables, net	6	4,378,239,217	4,599,415,154
Parts and supplies inventories	7	1,160,998,435	956,762,872
Due from affiliated companies	46	4,785,103	2,593,818
Investment in available-for-sale securities	9	1,278,631,449	2,726,590,585
Other current assets	8	1,885,512,228	530,474,808
Total Current Assets		18,740,581,616	13,265,927,182
Non-Current Assets			
Investments at cost	10	45,000,000	45,062,500
Property and equipment, net	11	14,594,476,289	12,482,198,662
Production wells, net	12	11,905,737,284	11,959,279,891
Power plant, net	13	2,373,564,909	-
BOT power plants, net	14 and 40	17,637,817,500	20,870,005,021
Exploratory and development costs	15	5,524,511,412	4,736,303,160
Investment property, net	16	278,921,181	279,774,800
Deferred tax assets	17	2,429,844,439	4,298,051,056
Other non-current assets, net	18	1,602,404,960	2,053,771,643
Total Non-Current Assets		56,392,277,974	56,724,446,733
Non-Current Assets Held for Sale	19	7,720,559	4,757,472
TOTAL ASSETS		75,140,580,149	69,995,131,387
LIABILITIES AND EQUITY			
LIABILITIES			
Current Liabilities			
Trade and other payables	20	4,091,156,339	4,138,292,512
Income tax payable		507,932,215	2,087,551,142
Due to PNOC	46	350,844,177	364,167,738
Royalty fee payable	21 and 38	524,644,631	613,194,966
BOT lease obligations	22 and 40	2,766,401,494	5,058,280,501
Long-term debt	23	3,171,351,515	4,616,888,191
Total Current Liabilities		11,412,330,371	16,878,375,050
Non-Current Liabilities			
Royalty fee payable, net of current portion	21 and 38	1,816,945,624	1,529,978,668
BOT lease obligations, net of current portion	22 and 40	413,180,565	2,777,311,576
Long-term debt, net of current portion	23	32,526,343,253	35,907,099,711
Retirement benefit obligation	43	869,569,338	903,521,207
Other long-term liabilities	24	256,432,845	235,220,993
Total Non-Current Liabilities		35,882,471,625	41,353,132,155
TOTAL LIABILITIES		47,294,801,996	58,231,507,205
EQUITY		27,845,778,153	11,763,624,182
TOTAL LIABILITIES AND EQUITY		75,140,580,149	69,995,131,387

See accompanying Notes to Financial Statements.

PNOC ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
INCOME STATEMENT
For the year ended December 31, 2006
(With comparative figures for 2005 and 2004)
In Philippine Peso

	Notes	2006	2005	2004
Net Sales	28, 39 and 41	21,008,888,031	21,572,382,035	20,644,488,402
Cost of Sales	29 and 40	(9,936,146,249)	(10,796,235,673)	(11,600,314,705)
Gross Profit		11,072,741,782	10,776,146,362	9,044,173,697
Other Operating Income	30	1,384,976,406	682,488,520	1,188,186,237
Operating Expenses	31	(1,825,461,636)	(1,912,076,431)	(2,164,372,255)
Other Operating Expenses	32	(1,069,292,001)	(89,787,142)	(799,216,269)
Income from Operations		9,562,964,551	9,456,771,309	7,268,771,410
Finance Costs	33	(2,098,952,898)	(2,110,339,649)	(1,820,378,000)
Foreign Exchange Gain (Loss)	34	2,885,094,749	6,418,640,384	(1,938,165,015)
Income Before Income Tax		10,349,106,402	13,765,072,044	3,510,228,395
(Provision for) Benefit from Income Tax				
Current tax	35	(1,697,975,135)	(1,677,383,618)	(1,120,406,825)
Deferred tax	35	(1,868,206,616)	(2,171,591,063)	51,856,074
Net Income		6,782,924,651	9,916,097,363	2,441,677,644
<i>See accompanying Notes to Financial Statements.</i>				
Earnings Per Share (EPS)				
Basic/Diluted	36	0.640	0.992	0.244

PNO ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
STATEMENT OF CHANGES IN EQUITY
For the year ended December 31, 2006
(With comparative figures for 2005 and 2004)
In Philippine Peso

	Capital Stock (Note 25)	Additional Paid-in Capital (Note 25)	Fair Value and Other Reserves (Note 27)	Appropriated Retained Earnings (Note 26)	Unappropriated Retained Earnings (Deficit)	Total Equity
Balance, January 1, 2004	10,000,000,000				(10,704,459,964)	(704,459,964)
Net Income					2,441,677,644	2,441,677,644
Balance, December 31, 2004	10,000,000,000				(8,262,782,320)	1,737,217,680
Balance, January 1, 2005	10,000,000,000				(8,262,782,320)	1,737,217,680
Net Income					9,916,097,363	9,916,097,363
Unrealized Holding Gain on Available-for- Sale Investments			110,309,139			110,309,139
Balance, December 31, 2005	10,000,000,000		110,309,139		-	11,763,624,182
Balance, January 1, 2006	10,000,000,000		110,309,139		1,653,315,043	11,763,624,182
Appropriation for exploration projects				1,653,315,043	(1,653,315,043)	-
Net Income					6,782,924,651	6,782,924,651
Stock dividend of 2,000,000,000 common shares at P1 par value as PNOC Subscription in the P5,000,000,000 increase in authorized capital stock	2,000,000,000				(2,000,000,000)	-
Public offering of 3,000,000,000 common shares with P1 par value at P3.20 per share	3,000,000,000	6,600,000,000				9,600,000,000
Expenses related to the sale of 3,000,000,000 common shares thru public offering			(321,924,352)			(321,924,352)
Unrealized Holding Gain on Available-for- Sale Investments			21,153,672			21,153,672
Balance, December 31, 2006	15,000,000,000	6,278,075,648	131,462,811	1,653,315,043	4,782,924,651	27,845,778,153

See accompanying Notes to Financial Statements.

PNOO ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
CASH FLOW STATEMENT
For the year ended December 31, 2006
(With comparative figures for 2005 and 2004)
In Philippine Peso

	2006	2005 (as restated)	2004 (as restated)
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash receipts from customers	20,661,919,926	21,273,307,451	18,407,985,139
Cash paid to suppliers and employees	(10,761,739,881)	(7,789,438,422)	(11,951,884,377)
Cash Generated from Operations	9,900,180,045	13,483,869,029	6,456,100,762
Interest expenses paid	(1,935,801,867)	(2,460,031,454)	(3,414,487,314)
Income taxes paid	(2,744,837,433)	-	(345,403,765)
Net cash from operating activities	5,219,540,745	11,023,837,575	2,696,209,683
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of property and equipment	(2,935,077,297)	(342,749,631)	(309,608,069)
Exploratory and development costs	(593,660,155)	(364,904,435)	(407,944,154)
Stocks and other investments	-	-	48,245,320
Investments in available-for-sale securities	1,274,000,000	28,139,181	-
Net cash used in investing activities	(2,254,737,452)	(679,514,885)	(669,306,903)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds of PNOO EDC's shares Initial Public Offering	9,413,245,000	-	-
Payment of BOT lease obligations	(5,042,087,781)	(5,789,262,776)	(6,419,508,001)
Payment of long-term debt	(4,512,480,992)	(3,388,597,422)	(3,286,770,010)
Payment of short-term loan	(1,150,000,000)	-	(2,333,516,000)
Long-term loan drawdowns	2,725,632,762	2,437,307,488	4,482,698,396
Proceeds of short-term loan	1,150,000,000	-	2,000,000,000
Net cash from (used in) financing activities	2,584,308,989	(6,740,552,710)	(5,557,095,615)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	5,549,112,282	3,603,769,980	(3,530,192,835)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	4,450,089,945	846,319,965	4,376,512,800
CASH AND CASH EQUIVALENTS AT END OF YEAR	9,999,202,227	4,450,089,945	846,319,965

See accompanying Notes to Financial Statements.

1. CORPORATE INFORMATION

PNOC Energy Development Corporation (PNOC EDC or the Company) was incorporated and registered with the Philippine Securities and Exchange Commission (SEC) on March 5, 1976.

PNOC EDC is a subsidiary of the Philippine National Oil Company which was created under Presidential Decree No. 334 on November 9, 1973.

Presidential Decree Number 334, otherwise known as the Charter of the Philippine National Oil Company (PNOC), empowered PNOC to undertake exploration, discovery and development of all forms of energy resources, including geothermal services of heat and power. In line with this decree, the Company, being a subsidiary of PNOC, entered into service contracts with the Department of Energy (DOE) in 1981 to develop the geothermal resources in Tongonan, Leyte; Palinpinon, Negros Oriental; and Bacon-Manito in Albay and Sorsogon. New service contracts were signed with the DOE for the development of Mt. Apo in North Cotabato (March 24, 1992), Mt. Labo in Camarines Norte (March 14, 1994), Northern Negros (March 24, 1994), and Mt. Cabalian in Southern Leyte (January 13, 1997). The contracts grant certain rights and privileges to the Company in the form of tax exemptions (except income tax) and other incentives.

The registered office address of the Company is Merritt Road, Ft. Bonifacio, Taguig City, Metro Manila.

The Board of Directors approved and authorized for issue the Company's financial statements on March 20, 2007.

2. STATUS OF OPERATIONS

Geothermal

Commercial steam production in Tongonan, Leyte and Palinpinon I, Negros Oriental was started in January 1984 while the Bacon-Manito (Bacman) I geothermal project in the provinces of Albay and Sorsogon was started in May 1993. Bacman II's first modular plant (Cawayan) commercially began operation in March 1994, while its second modular plant (Botong) started in December 1997. Palinpinon II's four modular plants started in December 1993 (Nasuji), November 1994 (Okoy), January 1995 (Sogongon #1) and March 1995 (Sogongon #2).

Nasulo Geothermal Project

In March 2006, PNOC EDC Management decided not to pursue a rebidding of the full turnkey contract for the power plant. Instead, the power plant will be offered to private investors with the project offering a Geothermal Resource Sales Contract (GRSC) to the chosen Independent Power Producer (IPP). On October 9, 2006, IPPs were invited to submit proposals for the purchase of geothermal steam from the project. A pre-auction

conference was held last October 25, 2006. The deadline for the submission of proposals was on December 12, 2006, which only Trans-Asia Oil and Energy Development Corporation was able to comply. On February 9, 2007, Trans-Asia was informed that its improved proposal for the geothermal steam is not acceptable. On February 19, 2007, PNOC EDC requested the Department of Energy to allow the Company to construct the power plant itself. The request is still under review.

Tanawon Geothermal Project

The project is located within the Bacon-Manito area. Except for the drilling of two production wells in 2000, no other activity has been conducted for this project. The original project feasibility, which includes the development of the steamfield and construction of the power plant by PNOC EDC, was withdrawn from the National Economic and Development Authority (NEDA) due to the change in implementation strategy. A revised Project Feasibility Study covering only the steamfield development will be submitted to NEDA once the project implementation schedule has been finalized.

Northern Negros Geothermal Project

The Northern Negros Geothermal Project (NNGP) involves the development of a geothermal steamfield and the installation of a 40 MW base-load power plant to meet the projected increased power demand in Negros Island. It includes the following components: (a) drilling of 15 production wells and 3 reinjection wells; (b) construction of a fluid collection and recycling system (FCRS); (c) construction of a 40 MW power plant including a switchyard; (d) construction of a 24-km transmission line to connect to an NPC substation; and (e) consulting services for the implementation of the project.

The project received NEDA approval on February 15, 1994 and was later confirmed for financing under the 21st Overseas Economic Cooperation Fund (OECF) Yen Package with a total loan amount of ¥14,460 million. On November 16, 2005, NEDA approved the proposed project cost increase from a revised estimate of P6,880.5 million in 2002 to P7,836.0 million in 2005.

The power plant engineering, procurement and construction (EPC) turnkey contract was awarded to Kanematsu Corporation on January 26, 2005 and a notice for the contractor to proceed was given on March 3, 2005. As of end December 2006, physical accomplishment for the project (i.e. power plant, transmission line, FCRS and technical consultancy) is 94.89%. The power plant is scheduled to be commissioned by February 2007.

Power Generation

The Company marked its formal entry into power generation business with the commercial operation of its Build-Operate-Transfer (BOT) power projects in 1997: the Leyte-Cebu power facilities (comprised of the 125 MW Upper Mahiao and 77 MW Malitbog 1 power plants) in November 1997 and the 47 MW Mindanao I geothermal power project in North Cotabato in March 1997. The Leyte-Luzon power facilities (comprised of the 154 MW Malitbog 2 & 3, 180 MW Mahanagdong and 49 MW Leyte Optimization power plants) started commercial operation in June 1998. The 48.25 MW Mindanao II geothermal power project in North Cotabato started commercial operation in June 1999.

Wind Power

Northern Luzon Wind Power Project Phase I (Saoit Wind Power Project)

The ¥5,857 million JBIC Special Yen Loan granted to PNOC EDC for the construction of a 40 MW Wind Farm and ancillary 42 km. 230 KV transmission lines in Barangay Saoit, Burgos, Ilocos Norte have been effected since March 2002. The yen-denominated loan, although highly concessional with its 40-year tenor at an interest rate of 0.95% p. a., requires that at least 50% of the cost of the contracts funded be of Japanese origin.

The project's budget includes the Consultancy Contract for the project implementation, which the contract was awarded to Tokyo Electric Power Services Company Ltd. (TEPSCO) of Japan in October 2005.

The bidding for the engineering, procurement and construction (EPC) contracts for the 40 MW wind farm and 230 KV Transmission Lines, respectively, resulted in bids substantially beyond the estimated contract amounts per the project appraisal conducted by JBIC in November 2001, significantly affecting the project's financial viability.

In November 2005, PNOC EDC undertook a re-validation study and recommended a revised implementation plan which was approved by the PNOC EDC Board on April 24, 2006 and endorsed by the NEDA-ICC (Cabinet Committee) on November 10, 2006. Highlights of the revised implementation plan are as follows:

- a. Saoit Wind Power Project – Wind Farm Component
 - i. Reduction of wind farm capacity from 40 MW to 30 MW and use of the existing ¥5,857 Million (US\$50.94 Million at ¥115/US\$) JBIC Special Yen Loan
 - ii. Rejection of the November 2004 bids submitted and re-bid of the Wind Farm EPC Contract on the basis of substantial changes in the project scope
- b. 42 km Burgos-Laoag Transmission Line
 - i. Reduction of transmission line specifications from 230 KV Double Circuit Single Strung to 115 KV Single Circuit
 - ii. Deletion of the transmission line component from the scope of the JBIC Special Yen Loan package
 - iii. Rejection of the November 2004 bids submitted as a result of substantial changes in the project scope and cancellation of this component of the project from the JBIC Loan
 - iv. Re-bidding of the Transmission Line EPC Contract using local financing under RA 9184 procurement guidelines.

Total project cost was revised from the originally approved cost of Php2,910.54 million to Php3,575.94 million.

TEPSCO declined the request to reconfirm the validity of the Consultancy Contract signed in November 2004 as the contract did not become effective due to the delay in project implementation. With JBIC's concurrence, PNOC EDC approached the next ranked bidders and Pacific Consultants Inc. solely signified interest. Negotiations with PCI for the Consultancy Contract are currently on-going.

The pre-bid conference for the Wind Farm Component of the project was held on December 20, 2006 and the submission of the bids was scheduled on March 6, 2007. There were only two bidders who submitted their bids which are presently under technical evaluation.

For the Transmission Line Component of the project, prequalification was scheduled on March 9, 2007. Only the partnership of MIESCOR-FABMIK showed interest for prequalification. The project proponent decided to revise the terms of reference to attract more bidders and set another round of prequalification in April 2007.

While already endorsed by the NEDA-ICC (Cabinet Committee), the project's change in scope and cost increase are still awaiting NEDA Board approval. Commercial operation of the project is scheduled in February 2009.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Financial Statement Preparation

The accompanying financial statements have been prepared under the historical cost convention method except for fair market valuation of financial instruments (financial assets, financial liabilities and equity instruments). The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

These financial statements are presented in Philippine peso because this is the currency of the primary economic environment in which the Company operates.

Statement of Compliance

These financial statements have been prepared in accordance with the accounting principles generally accepted in the Philippines as set forth in Philippine Financial Reporting Standards (PFRSs) and the applicable practices of the oil and gas industry not covered by the existing PFRS/PAS.

PNOE EDC has adopted the following new and amended PFRS and International Financial Reporting Interpretation Committee (IFRIC) interpretations during the year.

Adoption of these revised standards and interpretations did not have significant impact on PNOE EDC's financial statements.

- Amendments to Philippine Accounting Standards (PAS) 19, *Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures*, introduced an additional option for recognition of actuarial gains and losses in post-employment defined benefit plans. The amendment permits an entity to recognize actuarial gains and losses in the period in which they occur outside profit or loss. The amendment also requires additional disclosures on the financial statements to provide information about trends in the assets and liabilities in the defined benefit plans and the assumptions underlying the components of the defined benefit cost. The adoption of amendments to PAS 19 did not have an effect on PNOE EDC's result of operations and financial position. PNOE EDC elected to continue to recognize a portion of actuarial gains and losses in profit and loss if the cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded the greater of the 10% of the present value of defined obligation or 10% of the fair value of plan assets. Additional disclosures required by the amendments were included in the financial statements, where applicable.
- Amendments to PAS 21, *The Effects of Changes in Foreign Exchange Rates*, state that all exchange differences arising from a nonmonetary item that forms part of investment in foreign operation are recognized in a separate component of equity in the financial statement regardless of the currency in which the monetary item is denominated. PNOE EDC did not have any nonmonetary item that forms part of the net investment in foreign operations.
- Amendments to PAS 39, *Financial Instruments: Recognition and Measurement*, (a) *Amendment for financial guarantee contracts* (issued August 2005), amended the scope of PAS 39 to require financial guarantee contracts that are not considered as insurance contracts to be recognized initially at fair value and to be remeasured at the

higher of the amount determined in accordance with PAS 37, *Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognized less, when appropriate, cumulative amortization recognized in accordance with PAS 18, *Revenue*; (b) *Amendment for hedges of forecast intragroup transactions* (issued April 2005), allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in a cash flow hedge provided that the transaction is denominated in a currency other than the functional currency of the entity entering into transaction and that the foreign currency risk will affect the financial statements of income; and (c) *Amendment for the fair value option* (issued June 2005), prescribes the conditions under which the fair value option on classification of financial instruments at fair value through profit or loss (FVPL) maybe used.

- PFRS 6, *Exploration for and Evaluation of Mineral Resources*, permits an entity to develop an accounting policy for exploration and evaluation of assets without specifically considering the requirements of PAS 8, *Accounting Policies, Changes in Accounting Estimates and Error*.
- IFRIC Interpretation 4, *Determining Whether an Arrangement Contains a Lease*, provides for guidance in determining whether arrangements contain a lease to which lease accounting must be applied.
- IFRIC Interpretation 5, *Rights to Interest Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*, provides the accounting treatment for funds established to help finance decommissioning for PNOC EDC's assets. PNOC EDC does not operate in a country where such funds exist.
- IFRIC Interpretation 6, *Liabilities Arising from Participating in a Specific Market*, establishes the recognition date for liabilities arising from the European Union (EU) Directive relating to the disposal of Waste Electrical and Electronic Equipment. Adoption of this interpretation had no impact on the financial statements as PNOC EDC has no operations in countries covered by the EU Directive.

Future Changes in Accounting Policies

PFRS 7 Financial Instruments: Disclosures

PFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, as well as sensitivity analysis to market risk. It replaces PAS 30, *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*, and the disclosure requirement in PAS 32, *Financial Instruments: Disclosure and Presentation*. It is applicable to all entities that report under PFRS. PNOC EDC will adopt PFRS 7 beginning January 1, 2007.

Amendment to PAS 1 Presentation of Financial Statements

The amendment to PAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. PNOC EDC is currently assessing the impact of PFRS 7 and the amendment to PAS 1 and expects that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by PFRS 7 and the amendment to PAS 1. PNOC EDC will adopt the amendment to PAS 1 starting January 1, 2007.

IFRIC 8 Scope PFRS 2

IFRIC Interpretation 8 becomes effective for financial years beginning on or after May 1, 2006. This interpretation requires IFRS 2 to be applied to any arrangements where equity instruments are issued for consideration which appears to be less than fair value. As

equity instruments are only issued to employees in accordance with the employee share scheme, PNO C EDC does not expect the interpretation to have any impact on its financial position since at present it has no employee share scheme.

IFRIC 9 Reassessment of Embedded Derivatives

IFRIC Interpretation 9 was issued in March 2006 and became effective for financial years beginning on or after June 1, 2006. This interpretation establishes that the date to assess the existence of an embedded derivative is the date an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. PNO C EDC expects that the adoption of this interpretation will have no significant impact on its financial statements.

IFRIC 10 Interim Financial Reporting and Impairment

IFRIC Interpretation 10, which becomes effective for financial years beginning or after November 1, 2006, provides that the frequency of financial reporting does affect the amount of impairment charge to be recognized in the annual financial reporting with respect to goodwill and AFS investments. It prohibits the reversal of impairment losses on goodwill and AFS equity investments recognized in the interim financial reports even if impairment is no longer present at the annual balance sheet date. PNO C EDC expects that the adoption of this interpretation will have no significant impact on its financial statements.

Revenue Recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business.

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 use for a consideration called the sales price, net of sales discounts in case of generation beyond the contracted capacity.

Sale of electricity is consummated whenever the electricity generated by the Company is transmitted to the transmission line of the buyer for a consideration.

Interest income is accrued on a time proportion basis, by reference to the principal outstanding loan and at the effective interest rate applicable.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Company as Lessor

Amounts due from lessees under finance leases are recorded as receivables at the amount of the Company's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on the Company's net investment outstanding in respect of the leases.

Rental income from operating leases is recognized on a straight-line basis over the term of the relevant lease.

The Company as Lessee

Assets held under finance leases are recognized as assets of the Company at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the Company's general policy on borrowing costs.

Build-Operate-Transfer (BOT) Projects

The Company adopts the finance lease accounting method for its BOT projects. Under this method, the present value of the stream of future cash payments (for capital cost recovery fee) during the ten-year cooperation period is recognized as the capitalized cost of the BOT plant and the corresponding liability is set up. The capitalized cost will be amortized as depreciation expense over the useful life of the asset.

Financial Assets

Financial assets are recognized on the Company's balance sheet when the Company becomes a party to the contractual provisions of the instrument.

Cash and Cash Equivalents

Cash includes cash on hand and in banks. Cash equivalents are short-term, highly-liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

Trade and Other Receivables

Trade and other receivables are stated at face value as reduced by appropriate allowances for doubtful accounts.

Allowance for Doubtful Accounts

At each balance sheet date, the Company assesses whether there is objective evidence that a financial asset or a group of financial assets is impaired.

For trade receivables, the Company performs 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 ability to collect payments. The review is designed to identify whether objective evidence exists for non-collection of receivables and provide with the appropriate allowance for impairment losses.

For other receivables, impairment of individually significant balances are separately assessed and allowance made when it is probable that the cash due will not be received in full. Impairment of individually non-significant balances is measured on a portfolio or group basis. The Company performs a regular review of the age and status of the individual accounts and portfolio/group of accounts relative to historical collections,

changes in customer payment terms and other factors that may affect ability to collect payments.

Investments

Investments are initially measured at cost, plus directly attributable transaction costs and are recognized and derecognized on the settlement date where a purchase or sale of an investment is under a contract whose terms require delivery of the investment within the time frame established by the market concerned.

Investments are classified as available-for-sale and are measured at subsequent reporting dates at fair value. Gains and losses arising from changes in fair value are recognized directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognized in equity is included in the net profit or loss for the period.

Parts and Supplies Inventories

Inventories are stated 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 estimated selling price less all estimated costs to sell.

Investment Property

Investment property, which is property held to earn rentals and/or for capital appreciation, is stated at cost, less any subsequent accumulated depreciation and impairment losses.

Depreciation is computed on the straight-line method based on the 30 years estimated useful life of the building.

The useful life and method of depreciation are reviewed periodically to ensure that the period and method of depreciation are consistent with the expected pattern of economic benefits from items of investment property.

Property and Equipment

Property and equipment, except for land, are stated at cost less accumulated depreciation and any impairment in value, while land is stated at cost less any impairment in value.

The initial cost of property and equipment consists of its purchase price and costs directly attributable to bringing the asset to its working condition for its intended use. Subsequent expenditures relating to an item of property and equipment that have already been recognized are added to the carrying amount of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the Company. All other subsequent expenditures are recognized as expenses in the period in which they are incurred.

Major spare parts and stand-by equipment qualify as property and equipment when the Company expects to use them for more than one period. Similarly, if the spare parts and servicing equipment can be used only in connection with an item of property and equipment, they are accounted for as property and equipment.

Depreciation is computed on the straight-line method based on the estimated useful lives of the assets as follows:

Buildings and improvements	5-30 years
Exploration, machinery and equipment	2-10 years
Furniture, fixtures & equipment	3-10 years
Laboratory equipment	5-10 years
Transportation equipment	5 years

The useful life and method of depreciation are reviewed periodically to ensure that the period and method of depreciation are consistent with the expected pattern of economic benefits from items of property and equipment.

Stand-by equipment is depreciated from the date it is made available for use over the shorter of the life of the stand-by equipment or the life of the asset for which the stand-by equipment is part of, while major spare parts are depreciated over the period starting when these are brought into service, continuing over the lesser of their useful lives and the remaining expected useful life of the asset to which they relate.

The carrying amount of the component parts and spare parts replaced are derecognized upon replacement and charged as period's expense.

Gain or loss arising from the disposal or retirement of an asset is determined by computing the difference between the sales proceeds and the carrying amount of the asset and is recognized as income or expense for the period.

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

Exploratory and Development Costs

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 outright to expense.

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 Exploratory and Development Costs account. These costs include the following:

- a. costs associated with the acquisition of leases;
- b. costs of drilling exploratory and exploratory-type stratigraphic test wells, pending determination of whether the wells can produce proved reserves and;
- c. cost 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.

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

On the other hand, wells that have commercial steam quantity and good steam quality are further developed and the costs associated with these wells are accumulated and deferred under the Exploratory and Development Cost account. These costs include the following:

- a. costs of drilling wells exploratory and exploratory-type stratigraphic test , pending determination of whether the wells can produce proved reserves, wells which do not produce proved reserves but for which management has decided to utilize as recycling wells or as waste disposal wells;
- b. allocated costs from Management Service groups and Geothermal Division during the project development stage;
- 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 development drilling activities on production, recycling or waste disposal wells;
- d. costs incurred in the construction and commissioning of the fluid collection and recycling system (FCRS); and
- e. borrowing costs on loans utilized for the project.

Upon commercial operation of a plant, all drilling costs, including related costs, of wells hooked to the FCRS and those wells that are to be utilized either for recycling or waste disposal are transferred to Production Wells account and amortized over the estimated useful life of the properties.

The costs of wells drilled but not hooked remain in the Exploratory and Development Costs account until such time that the wells are hooked to the operating plants or until such time that all the plants under a particular service contract area are fully operational and producing and an evaluation as to the economic value of all the remaining wells drilled but not hooked to any plant is made. The accumulated costs of wells evaluated to have an economic value to a plant are transferred to Production Wells account and amortized over the remaining life of the plant, while the accumulated cost of wells evaluated to have no economic value are charged outright to expense.

Production Wells

Production wells are initially measured at cost, less any subsequent accumulated amortization and impairment losses. The cost of the wells includes all operating and non-operating costs pertaining to the wells hooked to the fluid collection and recycling system (FCRS) of the operating plants and those which are utilized either for recycling or waste disposal. These assets are provided with the appropriate amortization over the useful life of the property.

The amortization of production wells is computed on the straight-line method based on the estimated useful life of 30 years.

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 the temporary investment of specific borrowings, pending their

expenditure on qualifying assets, is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

Income Taxes

Current tax is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are neither taxable nor deductible or items that are taxable or deductible in other years. The Company's liability for current tax is calculated using the applicable tax rates.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible 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 profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Impairment of Assets

At each balance sheet date, the Company reviews the carrying amounts of its tangible assets to determine whether there is any indication that the assets have suffered impairment losses. If any such indication exists, the recoverable amounts of the assets are estimated in order to determine the extent of the impairment loss (if any). When the assets generate cash flows that are dependent from other assets, the Company estimates the recoverable amount of the cash-generating unit to which the assets belong.

An intangible asset with an indefinite useful life is tested for impairment annually and whenever there is an indication that the asset may have been impaired.

Recoverable amount is the higher of value in use and fair value less costs to sell. 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 for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

When an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Non-current Assets Held for Sale

Non-current assets are classified as held for sale if their carrying amounts will be recovered 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.

Non-current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Financial Liability and Equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities.

Trade Payables

Trade payables are stated at their nominal value.

Bank Borrowings

Interest-bearing bank loans are recorded at face value under the Long-Term Debt account. Direct issue costs are charged directly to expense as incurred. Outstanding balances of bank borrowings denominated in foreign currencies are restated using the prevailing rate of exchange at balance sheet date.

Foreign Currencies

Transactions in currencies other than Philippine peso are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Gains and losses arising on retranslation are included in net profit or loss for the period, except for exchange differences arising on non-monetary assets and liabilities where the changes in fair value are recognized directly in equity.

Retirement Benefit Costs

For defined benefit retirement plan, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are amortized over the expected average remaining

working lives of the employees participating in the plan. The amortized portion of these actuarial gains and losses is recognized as income or expense for the period.

The retirement benefit obligation recognized in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognized past service cost and actuarial gains and losses. It is reduced by the fair value of plan assets.

4. CASH AND CASH EQUIVALENTS

This account consists of the following:

	2006	2005
Cash on hand and in banks	27,167,605	488,683,210
Cash equivalents	9,972,034,622	3,961,406,735
	9,999,202,227	4,450,089,945

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 and earned interest of ₱318,098,112 in 2006 and ₱438,752,858 in 2005 for the same period.

5. CASH – RESTRICTED

The cash – restricted in 2006 represents the balance of fixed term deposits and cash in bank with the Land Bank of the Philippines intended for the payment of West-Jec consultancy services advanced by Japan Bank International Cooperation (JBIC) under the OECF 21st Yen Loan.

6. TRADE AND OTHER RECEIVABLES

This account consists of the following:

	2006	2005
Trade	4,232,642,072	4,371,867,879
Others	145,597,145	239,083,089
	4,378,239,217	4,610,950,968
Allowance for doubtful accounts (Note 18)	-	(11,535,814)
	4,378,239,217	4,599,415,154

Other receivables comprise mainly of receivables from employees, contractors and suppliers.

7. PARTS AND SUPPLIES INVENTORIES

This account consists of the following:

	2006	2005
Landed		
Drilling tubular products & equipment spares	515,495,138	468,393,332
Pump, production/steam gathering system, steam turbine, valves & valve spares	180,648,919	152,192,928
Construction & hardware supplies, stationers & office supplies, hoses, communication & other spares and supplies	141,178,526	15,359,428
Chemical, chemical products, gases & catalyst	94,503,340	65,409,371
Heavy equipment spares	86,901,635	87,160,495
Electrical, cable, wire product & compressor spares	50,031,092	54,184,027
Measuring instruments, indicators & tools, safety equipment and supplies	34,738,670	26,208,093
Automotive, mechanical, bearing, seals, v-belt, gasket, tires & batteries	34,711,525	38,616,437
	1,138,208,845	907,524,111
In transit	22,789,590	49,238,761
	1,160,998,435	956,762,872

In-transit inventories include items not yet received but ownership or title to the goods already passed to PNOC EDC.

The amount of inventories is net of uninstalled inventory of major spare parts for the FCRS such as valve assemblies which the Company classified into Property and Equipment (Note 11).

8. OTHER CURRENT ASSETS

This account consists of the following:

	2006	2005
Advances to contractors	1,053,172,238	510,664,066
Tax Credit Certificates	711,222,564	-
Prepaid expenses	121,117,426	19,810,742
	1,885,512,228	530,474,808

Advances to contractors largely pertain to the 25% advance payment to Kanematsu Corporation for the Northern Negros Geothermal Power Plant Project. Compared to 2005, the increase in 2006 was mainly brought about by the reclassification of the advance payment to Kanematsu Corporation from the Other Non-Current Assets Prepaid Expenses account .

The Tax Credit Certificates pertains mainly to the reclassification of ₱811,222,564 from non-current to other current assets due to receipt of the certificate issued by the BIR last January 2006. Of this amount, ₱100,000,000 was already applied to the 2nd quarter income tax due.

9. INVESTMENTS IN AVAILABLE-FOR-SALE SECURITIES

The account includes investments in long-term government debt securities (peso and US dollar denominated) amounting to ₱1,278,631,449 in 2006 and ₱2,726,590,586 in 2005. The fair values of these securities are based on quoted market prices as at balance sheet date. Accumulated unrealized holding gain on bonds and other investments is presented under equity and amounted to ₱131,462,811 and ₱110,309,139 for the years-ended December 31, 2006 and 2005, respectively.

10. INVESTMENTS AT COST

This account consists of investments in the following:

	2006	2005
NRMDC	45,000,000	45,000,000
Kenmare Gold (unquoted shares)	-	62,500
	45,000,000	45,062,500

Pursuant to the Memorandum dated April 9, 2003 of Her Excellency Gloria Macapagal-Arroyo, President of the Republic of the Philippines, PNO EDC and Natural Resources Development Corporation (NRDC), the Department of Environment and Natural Resources' (DENR) corporate arm was authorized to incorporate, and invest in the equity of Natural Resources Mining Development Corporation (NRMDC). NRMDC shall be engaged in mining and is being programmed to explore and exploit the gold resources initially in Mt. Diwalwal. Under such presidential directive, the NRMDC shall have an authorized capital stock of P100 million, 55% of which shall be owned by DENR's NRDC and 45% by PNO EDC. The Company's investment of ₱45,000,000 in NRMDC was approved under PNO EDC Board Resolution No. 33, Series of 2004.

On August 24, 2005, the Securities and Exchange Commission (SEC) approved NRMDC's increase in authorized capital stock to ₱125 million. The ₱25 million increase was subscribed by the National Development Company (NDC), corporate arm of the Department of Trade and Industry (DTI). The ₱125 million total capitalization of NRMDC is shared by NRDC (44%), PNO EDC (36%) and NDC (20%).

NRDC is the dominant interest in NRMDC in terms of holdings and management oversight as well as strategic directions and review of NRMDC management's work program and directions through the operational relationship of the DENR and its monitoring bureaus and units of NRMDC. On the other hand, PNO EDC and NDC interests in NRMDC are that of financial investors; thus, these companies do not exercise significant influence.

In 2006, investment with Kenmare Gold was found impaired and subsequently reclassified to the Other Non-Current Assets account with a value of ₱1.

11. PROPERTY AND EQUIPMENT

The rollforward analysis of this account follows:

	Buildings and Improvements	Exploration Machinery & Equipment	Transportation Equipment	Furniture, Fixtures & Equipment	Laboratory Equipment	Major Spare Parts (Note 7)	Land, Leases & Improvement	Construction in Progress	Total
COST									
January 1, 2006	13,953,879,284	1,696,961,761	289,106,865	258,705,823	106,850,181	19,531,878	1,712,937,830	604,251,429	18,642,225,051
Additions	14	63	12	435	133	1,691,110	14,703,878	3,371,997,124	3,388,392,769
Reclassifications	60,233,670	15,667,233	4,019,374	28,079,258	7,625,297	(6,013,997)	-	(520,836,518)	(411,225,683)
Disposals	(16,416)	(8,725,481)	(25,069,115)	(6,785,510)	(4,175,938)	-	-	-	(61,172,463)
Dec. 31, 2006	13,997,696,549	1,703,903,576	268,057,136	280,000,006	110,299,673	15,208,991	1,727,641,708	3,455,412,035	21,558,219,674
ACCUMULATED DEPRECIATION									
January 1, 2006	(4,513,088,795)	(1,078,314,410)	(248,991,073)	(227,939,248)	(91,692,863)	-	-	-	(6,160,026,389)
Provision	(704,351,212)	(103,362,222)	(20,310,536)	(23,388,334)	(6,468,385)	-	-	-	(857,880,689)
Disposals	10,991,194	7,731,879	24,628,603	6,745,291	4,066,726	-	-	-	54,163,693
Dec. 31, 2006	(5,206,448,813)	(1,173,944,753)	(244,673,006)	(244,582,291)	(94,094,522)	-	-	-	(6,963,743,385)
Carrying Amount Dec. 31, 2006	8,791,247,736	529,958,823	23,384,130	35,417,715	16,205,151	15,208,991	1,727,641,708	3,455,412,035	14,594,476,289

	Buildings and Improvements	Exploration Machinery & Equipment	Transportation Equipment	Furniture, Fixtures & Equipment	Laboratory Equipment	Major Spare Parts (Note 7)	Land, Leases & Improvement	Construction in Progress	Total
COST									
January 1, 2005	13,716,518,518	1,701,645,867	293,321,410	251,042,330	103,615,634	28,208,384	1,686,214,172	459,308,520	18,239,874,835
Additions	-	-	-	190,031	-	6,858,000	26,734,830	584,767,059	618,549,920
Reclassifications	247,111,387	10,455,970	5,128,999	20,296,362	4,601,527	(15,534,506)	(11,172)	(439,824,150)	(167,775,583)
Disposals	(9,750,621)	(15,140,076)	(9,343,544)	(12,822,900)	(1,366,980)	-	-	-	(48,424,121)
Dec. 31, 2005	13,953,879,284	1,696,961,761	289,106,865	258,705,823	106,850,181	19,531,878	1,712,937,830	604,251,429	18,642,225,051
ACCUMULATED DEPRECIATION									
January 1, 2005	(3,764,852,815)	(982,414,693)	(220,836,641)	(217,961,931)	(87,572,926)	-	-	-	(5,273,639,006)
Provision	(753,769,929)	(110,853,440)	(37,256,459)	(22,735,186)	(5,486,850)	-	-	-	(930,101,864)
Disposals	5,533,949	14,953,723	9,102,027	12,757,869	1,366,913	-	-	-	43,714,481
Dec. 31, 2005	(4,513,088,795)	(1,078,314,410)	(248,991,073)	(227,939,248)	(91,692,863)	-	-	-	(6,160,026,389)
Carrying Amount Dec. 31, 2005	9,440,790,489	618,647,351	40,115,792	30,766,575	15,157,318	19,531,878	1,712,937,830	604,251,429	12,482,198,662

Provisions for depreciation are allocated as follows:

	2006	2005
Operating cost	721,022,627	876,190,075
Exploratory and development cost	136,858,062	53,911,789
	857,880,689	930,101,864

Total costs of assets retired/written-off amounted to ₱7,008,770.63 in 2006 and ₱4,709,640 in 2005 - net of ₱54,163,693 and ₱43,714,481 accumulated depreciation, respectively.

Total purchase commitments for the year amounted to ₱64,515,011.43.

Management believes that, based on the assessment performed, there are no assets found impaired.

12. PRODUCTION WELLS

The rollforward analysis of this account follows:

COST	
January 1, 2006	17,921,809,990
Additions	602,627,454
December 31, 2006	18,524,437,444

ACCUMULATED AMORTIZATION	
January 1, 2006	(5,962,530,099)
Provision	(656,170,061)
December 31, 2006	(6,618,700,160)

CARRYING AMOUNT, December 31, 2006	11,905,737,284
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	Amount
COST	
January 1, 2005	17,553,806,386
Additions	368,003,604
December 31, 2005	17,921,809,990

CARRYING AMOUNT, December 31, 2005	11,959,279,891
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Amortization expenses of ₱656,170,061 in 2006 and ₱602,966,406 in 2005 have been charged to cost of sales.

Management believes that, based on the assessment performed, there are no assets found impaired.

13. POWER PLANT

This account pertains to the Upper Mahiao power plant which was turned-over to PNO C EDC by CE Cebu (BOT contractor) on June 25, 2006 with a cost of ₱3,670,775,022 and accumulated depreciation of ₱1,174,966,440. Provision for the year amounted to ₱122,243,673.

14. BOT POWER PLANTS

This account pertains to the capitalized present value of the stream of future cash payments for capital cost recovery (CCR) fees of the following BOT power plants during the ten-year cooperation period discounted at the buy-out rate indicated in the BOT contracts:

	Malitbog	Mahanagdong	Mindanao I	Mindanao II	Tongonan I Optimization	Upper Mahiao	Total
COST							
January 1, 2006	12,287,865,264	7,853,473,973	2,186,029,391	2,798,177,959	470,881,120	3,670,775,022	29,267,202,729
Additions	170,161,059	-	-	-	-	-	170,161,059
Reclassifications			(1,214,473)			(3,670,775,022)	(3,671,989,495)
Dec. 31, 2006	12,458,026,323	7,853,473,973	2,184,814,918	2,798,177,959	470,881,120	-	25,765,374,293
ACCUMULATED DEPRECIATION							
January 1, 2006	(3,602,961,628)	(2,228,238,322)	(644,687,190)	(615,543,816)	(130,800,310)	(1,174,966,440)	(8,397,197,706)
Provision	(411,003,453)	(261,504,545)	(72,819,971)	(93,208,576)	(15,696,037)	(101,869,738)	(956,102,320)
Adjustment	(52,466,326)						(52,466,326)
Reclassifications			1,373,381			1,276,836,178	1,278,209,559
Dec. 31, 2006	(4,066,431,407)	(2,489,742,867)	(716,133,780)	(708,752,392)	(146,496,347)	-	(8,127,556,793)
Carrying Amount, Dec. 31, 2006	8,391,594,916	5,363,731,106	1,468,681,138	2,089,425,567	324,384,773	-	17,637,817,500
	Malitbog	Mahanagdong	Mindanao I	Mindanao II	Tongonan I Optimization	Upper Mahiao	Total
COST							
January 1	12,287,865,263	7,853,473,973	2,186,029,391	2,798,177,959	470,881,120	3,670,775,022	29,267,202,728
Additions	-	-	-	-	-	-	-
Disposals	-	-	-	-	-	-	-
Dec. 31, 2006	12,287,865,263	7,853,473,973	2,186,029,391	2,798,177,959	470,881,120	3,670,775,022	29,267,202,728
ACCUMULATED DEPRECIATION							
January 1	3,193,376,184	1,966,733,777	571,867,873	522,335,241	115,104,273	1,052,722,755	7,422,140,103
Provision	409,585,444	261,504,545	72,819,317	93,208,575	15,696,037	122,243,686	975,057,604
Impairment Loss	-	-	-	-	-	-	-
Disposals	-	-	-	-	-	-	-
Dec. 31, 2005	3,602,961,628	2,228,238,322	644,687,190	615,543,816	130,800,310	1,174,966,441	8,397,197,707
Carrying Amount, Dec. 31, 2005	8,684,903,635	5,625,235,651	1,541,342,201	2,182,634,143	340,080,810	2,495,808,581	20,870,005,021

Depreciation expenses amounting to ₱956,102,320 in 2006 and ₱975,057,604 in 2005 have been charged to cost of sales, respectively.

The corresponding liability account set up for BOT Power Plants is the BOT Lease Obligations.

Management believes that, based on the assessment performed, there are no assets found impaired.

15. EXPLORATORY AND DEVELOPMENT COSTS

Deferred costs of exploration and development pertain to the following project areas:

	2006	2005
Northern Negros	4,245,358,796	3,443,029,257
Malitbog	193,663,514	483,473,760
Upper Mahiao	190,273,726	212,765,481
Cabalian, So. Leyte	363,970,378	269,467,788
Mahanagdong	143,114,524	143,077,033
Tongonan	90,107,844	-
Mindanao	53,224,641	53,197,601
Ilocos Norte	39,546,367	39,558,144
Bacman-Tanawon	37,315,026	37,204,177
Other areas	167,936,596	54,529,919
	5,524,511,412	4,736,303,160

The increase in exploratory and development costs was mainly due to the additional development and drilling costs in the geothermal projects mainly in Northern Negros, Malitbog and Upper Mahiao in Leyte and Cabalian, So. Leyte.

16. INVESTMENT PROPERTY

This rollforward analysis of this account follows:

	Land	Building	Total
Cost			
January 1, 2006	272,945,855	6,828,945	279,774,800
Accumulated depreciation	-	(853,619)	(853,619)
Carrying Amount, December 31, 2006	272,945,855	5,975,326	278,921,181
	Land	Building	Total
Cost			
January 1, 2005	272,945,855	7,682,563	280,628,418
Accumulated depreciation	-	(853,618)	(853,618)
Carrying Amount, December 31, 2005	272,945,855	6,828,945	279,774,800

Depreciation expenses amounting to ₱853,619 for the year were charged to operating expenses.

Management believes that, based on the assessment performed, there are no assets found impaired.

17. DEFERRED TAX ASSETS

The analysis of deferred income tax for financial reporting purposes follows:

	2006	2005
Deferred tax assets	7,876,742,165	9,669,431,092
Deferred tax liability	(5,446,897,726)	(5,371,380,036)
Net	2,429,844,439	4,298,051,056

The deferred tax assets consist mainly of the undepreciated balance of the foreign exchange losses on payment and realignment of BOT lease obligations capitalized under BIR reporting, unrealized foreign exchange losses on foreign loans and allowance for doubtful accounts. The account is net of deferred tax liability on the deductible expenses provided under PD 1442 and the increase in fair value of property and equipment applied as deemed costs recognized during the conversion to PFRS.

The composition of deferred income taxes recognized by the Company is as follows:

Deferred Tax Assets					
	Foreign exchange losses (gains) -BOT Power Plants	Unrealized foreign exchange losses (gains)	Allowance for doubtful accounts	Others	Total
At January 1, 2006	5,607,478,024	2,732,004,460	1,217,680,716	112,267,892	9,669,431,092
Charged to income for the period	(245,557,122)	(1,329,956,014)	(153,433,785)	(63,742,006)	(1,792,688,927)
At December 31, 2006	5,361,920,902	1,402,048,446	1,064,246,931	48,525,886	7,876,742,165

Deferred Tax Assets					
	Foreign exchange losses (gains) -BOT Power Plants	Unrealized foreign exchange losses (gains)	Allowance for doubtful accounts	Others	Total
At January 1, 2004	5,917,839,824	4,392,131,375	1,055,245,870	110,559,874	11,475,776,943
Charge to income for the period	(325,113,254)	289,923,536	(3,647,276)	(13,148,608)	(51,985,602)
At January 1, 2005	5,592,726,570	4,682,054,911	1,051,598,594	97,411,266	11,423,791,341
Charge to income for the period	(473,169,043)	(2,394,281,166)	77,462,684	5,315,440	(2,784,672,085)
Adjustment of deferred tax balance as of 12/31/05 at 35% income tax rate	487,920,497	444,230,715	88,619,438	9,541,186	1,030,311,836
At December 31, 2005	5,607,478,024	2,732,004,460	1,217,680,716	112,267,892	9,669,431,092

Deferred Tax Liability			
	Increase in Fair Value Applied as Deemed Costs	Deductible Expenses Per PD 1442	Total
At January 1, 2006	(1,887,142,599)	(3,484,237,437)	(5,371,380,036)
Charged to income for the period	40,526,291	(116,043,981)	(75,517,690)
At December 31, 2006	(1,846,616,308)	(3,600,281,418)	(5,446,897,726)

Deferred Tax Liability			
	Increase in Fair Value Applied as Deemed Costs	Deductible Expenses Per PD 1442	Total
At January 1, 2004	(1,993,157,824)	(3,064,833,075)	(5,057,990,899)
Charge to income for the period	149,031,811	(45,190,135)	103,841,676
At January 1, 2005	(1,844,126,013)	(3,110,023,210)	(4,954,149,223)
Charge to income for the period	144,599,215	(91,388,094)	53,211,121
Adjustment of deferred tax balance as of 12/31/05 at 35% income tax rate	(187,615,801)	(282,826,133)	(470,441,934)
At December 31, 2005	(1,887,142,599)	(3,484,237,437)	(5,371,380,036)

The 2005 balance of deferred tax assets and deferred tax liabilities as previously reported were restated to conform with the 2006 presentation.

18. OTHER NON-CURRENT ASSETS

This account consists of the following:

	2006	2005
Long-term receivables	3,660,076,242	4,394,666,305
Deferred royalty fee	896,949,151	697,795,289
Prepaid guarantee fee on Miyazawa II loan	351,708,984	452,552,486
Special deposits & funds	27,826,772	22,851,782
Investments in available-for-sale securities	12,146,829	12,182,285
Cash collateral on PCIR Bonds	3,632,164	4,415,325
Others	247,631,940	35,196,737
Prepaid expenses (Note 8)	-	457,486,009
	5,199,972,082	6,077,146,218
Allowance for doubtful accounts	(3,597,567,122)	(4,023,374,575)
	1,602,404,960	2,053,771,643

The decrease in long-term receivables pertains mainly to the reclassification to other current assets portion of the VAT receivable from BIR for which a Tax Credit Certificate was already issued by BIR on January 31, 2006 amounting to ₱811,222,564.

The composition of long-term receivables and related allowances for doubtful accounts are as follows:

Particulars	2006	2005
Claims for VAT Refund	1,894,719,994	2,707,006,565
NPC Accounts and Other Receivables	1,765,356,248	1,687,659,740
	3,660,076,242	4,394,666,305
Allowances for Doubtful Accounts:		
- Claims for VAT Refund	(1,894,719,994)	(2,632,061,435)
- NPC Accounts and Other Receivables	(1,702,847,128)	(1,391,313,140)
	(3,597,567,122)	(4,023,374,575)
	62,509,120	371,291,730

Additional allowance for doubtful accounts of ₱299,176,115 was provided for NPC accounts in 2006 while the allowance for doubtful accounts pertaining to claims from BIR was reduced by ₱737,558,359 during the year as a result of the receipt from the BIR of a Tax Credit Certificate amounting to ₱811,222,564 on January 31, 2006.

The BIR related claims pertain to PNOC EDC's claims for the refund of input VAT on BOT fees amounting to ₱1,894,478,700 which was initially denied by the BIR regional level on July 2, 2002. Subsequently, on September 2, 2002, PNOC EDC submitted a letter for reconsideration, RDO 50 endorsed the request for reconsideration to the BIR Head Office legal department and the review of the claims is still on going.

Guarantee fee on Miyazawa II pertains to the upfront fees subject to amortization starting on the 6th year towards the end of the 10-year loan period.

The decrease in prepaid expenses was mainly due to the reclassification to other current assets of the 25% advance payment to Kanematsu Corporation for the construction of Northern Negros Geothermal Power Plant Project.

The special deposits and funds mainly consisted of the ₱11 million sinking fund required by the Department of Finance to cover the long-term loans payment and ₱4 million escrow account in favor of terminated LAGPEU members/employees.

The Investment in Available-for-Sale Securities account pertains to other investments which afford the Company with opportunity for return through capital appreciation and trading gains. This account is quoted in fair market value based on market prices as at balance sheet date.

The accounts grouped as Others mainly consisted of the ₱121 million input VAT on the purchase of goods and services which will be claimed for refund from the Bureau of Internal Revenue and ₱118 million typhoon related claims from insurance.

In 2006, the allowance for doubtful accounts for trade receivables was established after the Company performed the 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 ability to collect payments. Except for accounts covered by special agreements with NPC, it was estimated that accounts outstanding over one year should have 100% provision.

Likewise, for other receivables, it was also established that accounts outstanding less than one year should have no provision but accounts outstanding over one year should have a 100% provision, which was arrived at after assessing 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 ability to collect payments.

19. NON-CURRENT ASSETS HELD FOR SALE

This account consists of the following:

	2006	2005
Materials and supplies inventory for disposal	3,453,711	3,420,946
Surplus property available for sale	4,266,848	1,336,526
	7,720,559	4,757,472

20. TRADE AND OTHER PAYABLES

This account consists of the following:

	2006	2005
Accounts payable – trade	2,964,522,262	3,229,261,853
Accrued interest and guarantee fees	1,011,270,018	649,419,909
Withholding and other taxes payable	95,908,096	158,112,173
Deferred credits	6,846,940	64,639,428
SSS and other contributions	5,454,446	23,877,693
Liability for annuity – current	1,239,028	9,580,927
Miscellaneous current liabilities	5,915,549	3,400,529
	4,091,156,339	4,138,292,512

Accounts Payable – Trade, which comprised mainly of the accrued capacity fees for BOT plants, decreased due to the full payment of BOT lease obligations for Upper Mahiao power plant. The comparative amounts include recognition of DOE's initial revalidation of its assessment amounting to ₱866,399,332 representing royalty fees for the period 1996 to 1998 relative to PNOC EDC's service contracts for SNGPF. This will be settled in the second quarter of 2007 upon final validation of interest and foreign exchange changes for 1996 to 2003.

The increase in accrued interest and guarantee fees pertains mainly to the accrual of guarantee fees on long-term loans.

Liability for Annuity – Current pertains to the accrued computed sick leave, vacation leave and separation benefits of employees who will retire in 2007. Liability to employees who will retire in the succeeding years is presented under long-term liabilities.

21. ROYALTY FEE PAYABLE

This account consists of payables for royalty to the following:

	2006	2005
Due Department of Energy (Note 38)	2,016,945,624	1,729,978,668
Due Local Government Units (Note 38)	324,644,631	413,194,966
	2,341,590,255	2,143,173,634
Current portion	(524,644,631)	(613,194,966)
Long-term portion	1,816,945,624	1,529,978,668

22. BOT LEASE OBLIGATIONS

This account consists of the following:

	Minimum Lease Payments		Present Value of Minimum Lease Payments	
	2006	2005	2006	2005
Amounts payable under finance leases:				
Within one year	2,904,781,721	5,538,025,533	2,766,401,494	5,058,280,501
In the second to fifth years inclusive	434,680,911	2,934,961,447	413,180,565	2,777,311,576
Future finance charges	(159,880,573)	(637,394,903)	-	-
	[email]			
Present value of lease obligations	3,179,582,059	7,835,592,077	3,179,582,059	7,835,592,077
Amount due for settlement within 12 months (shown under current liabilities)	(2,766,401,494)	(5,058,280,501)	(2,766,401,494)	(5,058,280,501)
Amount due for settlement after 12 months	413,180,565	2,777,311,576	413,180,565	2,777,311,576

This account pertains to the liability set up for the present value of the stream of future cash payments for capital cost recovery fees of the BOT power plants during the ten-year cooperation period discounted at the buy-out rate indicated in the BOT contracts. The BOT lease obligations are denominated in US dollar and realigned to Philippine peso based on the year-end closing rate at the balance sheet date.



23. LONG-TERM DEBT

The Company's foreign-currency denominated long-term debts were translated into Philippine pesos based on the prevailing foreign exchange rates at balance sheet date (USD1=JPY118.934: USD1=PHP49.045 on December 31, 2006 and USD1=JPY117.855: USD1=PHP53.062 on December 31, 2005).

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

CREDITOR/PROJECT	MATURITIES	INTEREST RATE	2006	2005
IBRD				
2969 PH Bacon-Manito Geothermal Power Plant – US\$41 million	1994 to 2008	½ of 1% over cost of qualified borrowings	464,006,909	700,991,542
3164 PH Energy Sector Loan – US\$118 million	1995 to 2010	½ of 1% over cost of qualified borrowings	2,017,103,046	2,613,720,357
3702 PH Geothermal Exploration Project – US\$64 million	1999 to 2013	½ of 1% over cost of qualified borrowings	1,516,373,173	1,751,831,109
3747 PH Geothermal Exploration Project - US\$114 million - JPY12.4 billion	1999 to 2014 1999 to 2014	½ of 1% over cost of qualified borrowings/3.5%	1,701,179,610 1,270,302,115	1,950,460,737 1,573,036,407
OECF				
8 th Yen Tongonan I Geothermal Power Plant (share in OECF-NPC loan) - JPY5.8 billion - JPY1.5 billion (Restructured)	1990 to 2010	3.0% 3.2%	411,272,172 163,260,896	577,411,044 210,575,227
9 th Yen Palinpinon I Geothermal Power Plant - JPY 10.8 billion	1991 to 2011	3.0%	770,899,584	1,028,717,214
15 th Yen Palinpinon I Geothermal Power Plant - JPY4.0 billion	1999 to 2019	5.7%	800,031,045	943,362,515
18 th Yen Palinpinon II Geothermal Power Plant - JPY77.4 million	2003 to 2023	3.0%	25,681,845	29,739,136
19 th Yen Mt. Labo Geothermal Project - JPY10.8 billion	2004 to 2024	4.9%	115,897,514	133,568,251
21 st Yen No. Negros Geothermal Project - JPY14.5 billion, of which JPY5.9 billion was drawn during the year	2007 to 2027	2.7%/2.3%	4,299,364,022	2,056,852,409

CREDITOR/PROJECT	MATURITIES	INTEREST RATE	2006	2005
National Government				
Principal Collateralized Interest Reduction Bonds (PCIR)		Year 1 - 4 ¼%		
		2 - 5 ¼%		
		3 - 5 ¾%		
		4-5 - 6 ¼%		
- US\$328 thousand	1992 to 2017	6-25 - 6 ½%	16,082,359	17,399,574
Miyazawa I				
- JPY5.2 billion		Tranche A=3.78%	2,127,831,058	2,341,201,564
- JPY6.8 billion	June 1, 2009	Tranche B=1.60% + LIBOR	2,820,613,262	3,061,571,276
Miyazawa II				
- JPY22.0 billion	June 26, 2010	2.37%	9,072,147,920	9,905,083,540
JP Morgan Chase Manhattan				
- US\$110 million	Oct. 19, 2006	3.85% + 6 mos. LIBOR (2.42375)	-	1,167,364,000
Bank of Tokyo Mitsubishi				
- US\$30 million	Dec. 14, 2006	3.85% + 6 mos. LIBOR (1.90875)	-	318,372,000
US\$90 Million Five Years Guaranteed Loan Facility				
- US\$45.7 million		Tranche 1=3.70% + 6 mos. LIBOR	1,807,602,533	2,424,933,400
- US\$44.3 million	Feb. 21, 2008	Tranche 2=3.39% + 6 mos. LIBOR	1,736,716,159	2,350,646,600
Land Bank of the Phils.				
- PHP1.5 Billion	June 29, 2008	Ave. 91-day T-Bill + 2%	882,954,546	1,387,500,000
Syndicated 5-Year Loan				
-US\$75 million	Aug. 4, 2009	LIBOR + 2.22%	3,678,375,000	3,979,650,000
Total Current portion			35,697,694,768	40,523,987,902
			(3,171,351,515)	(4,616,888,191)
Long-term portion			32,526,343,253	35,907,099,711

24. OTHER LONG-TERM LIABILITIES

This account consists of accrued vacation and sick leave cumulative balances as of balance sheet date that can be carried over beyond 12 months.

25. CAPITAL STOCK

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 and other mineral resources. The Company's shares of stocks are 60% owned by PNOC and 40% owned by various investors, both local and foreign.

Details are as follows:

	2006	2005
Common stock		
Authorized & subscribed	15,000,000,000	10,000,000,000
2006 - 15,000,000,000 shares @ ₱1 par value		
2005 - 10,000,000 shares @ ₱1,000 par value		
Additional paid-in capital	6,278,075,648	-
	21,278,075,648	10,000,000,000

On September 19, 2006, the stockholders, through Resolution No. 5, Series of 2006, approved and ratified PNOC EDC Board Resolution No. 84, Series of 2006, which approved and authorized the increase of the authorized capital from ₱10 billion divided into 10 million shares with par value of ₱1,000 each, to ₱15 billion divided into 15 billion shares with par value of ₱1.00 each. The stockholders also approved in the same resolution the declaration of stock dividends amounting to ₱2 billion equivalent to 2 billion shares to Philippine National Oil Company as full payment for the subscription to the increase in authorized capital.

The increase in capital stock was filed and approved by the Securities and Exchange Commission on September 25, 2006 and October 9, 2006, respectively.

On December 13, 2006, 6 billion shares were offered to the public at ₱3.20 per share, of which 3 billion shares were primary or unissued shares and 3 billion shares were secondary or issued shares owned by the Philippine National Oil Company. The additional paid-in capital of ₱6.6 billion, which pertains to the excess over the par value of the 3 billion par value of primary shares, was reduced by direct expenses of ₱321,924,352 incurred during the initial public offering.

As of year end, there are 2,480 stockholders of PNOC EDC.

26. RETAINED EARNINGS

The Board of Directors approved on May 22, 2006 per Board Resolution No. 45, series of 2006 the appropriation of ₱1,653 million retained earnings as of December 31, 2005 to meet the Company's cash requirements for exploration projects for additional 270 MW within the next two (2) years.

The Board declared on September 18, 2006 stock dividends of ₱2 billion out of the ₱3,413.3 million audited unrestricted retained earnings as of July 31, 2006. This was approved and ratified on September 19, 2006 by the stockholders through Resolution No. 5, Series of 2006.

27. RESERVES

This account consists of the following:

	2006	2005
Accumulated unrealized gain on investments in available-for-sale securities	131,462,811	110,309,139

This account pertains to the gains on the realignment of investments in bonds and stocks classified as available-for-sale securities charged to equity (Note 9).

28. NET SALES

This account consists of the following:

	2006	2005	2004
Electricity	15,727,908,745	16,455,494,955	15,957,212,444
Steam	5,019,529,299	4,967,362,240	4,685,671,153
Drilling	261,449,987	149,524,840	1,604,805
	21,008,888,031	21,572,382,035	20,644,488,402

29. COST OF SALES

This account consists of the following:

	2006	2005	2004
Purchased services and utilities	5,041,131,929	5,932,641,439	7,182,173,191
Depreciation and amortization	2,269,399,961	2,374,500,160	2,374,033,754
Employee costs	886,024,220	940,921,235	769,611,327
Royalty fee	470,394,682	528,839,664	373,972,212
Materials and supplies	362,618,388	333,292,650	285,117,735
Maintenance and repairs	312,380,499	256,055,276	259,323,058
Technical support charges	296,167,148	280,933,242	197,466,237
Rental, insurance and taxes	263,084,064	123,720,722	139,310,524
Business and other expenses	34,945,358	25,331,285	19,306,667
	9,936,146,249	10,796,235,673	11,600,314,705

The 2005 and 2004 balances of some accounts were reclassified to conform with the 2006 presentation.

30. OTHER OPERATING INCOME

This account consists of the following:

	2006	2005	2004
Reduction on allowance for doubtful accounts	737,558,359	-	-
Interest income – net of final tax	330,161,680	368,370,603	411,728,305
Fair value increase on Upper Mahiao Power Plant materials inventory turned over	125,636,878	-	-
Inflation adjustment on prior year's			
- electricity revenues	45,282,758	171,761,386	-
- steam sales	17,753,029	118,824,859	-
Gain on sale of securities	29,278,973	-	-
Waste disposal fees	18,011,912	-	-
Prior year's adjustments			
- interest income	77,794,479	-	-
- amortization of capitalized interest charges	-	6,411,618	-
- foreign exchange losses on BOT lease Obligations		-	479,989,743
- prior year's expenses		-	221,882,715
Miscellaneous income	3,498,338	17,120,054	74,585,474
	1,384,976,406	682,488,520	1,188,186,237

The credit adjustment on allowance for doubtful accounts pertains mainly to the provision for doubtful accounts previously provided on receivables for VAT claims amounting to ₱811,222,564 which was refunded by the Bureau of Internal Revenue through the issuance of Tax Credit Certificate on January 31, 2006.

31. OPERATING EXPENSES

This account consists of the following:

	2006	2005	2004
Administrative charges	662,147,642	775,205,084	960,707,478
Employee costs	314,263,270	426,231,771	381,111,660
Provision for doubtful accounts	299,176,115	238,503,085	301,007,307
Rental, insurance and taxes	216,877,247	163,337,215	228,819,357
Purchased services and utilities	159,361,592	142,345,778	137,685,038
Materials and supplies	48,133,906	39,222,725	28,621,253
Depreciation	79,743,917	87,001,383	88,911,513
Business and other expenses	33,699,466	30,026,319	24,622,397
Maintenance and repairs	12,058,481	10,203,071	11,069,890
Provision for impairment in the value of assets	-	-	1,816,362
	1,825,461,636	1,912,076,431	2,164,372,255

32. OTHER OPERATING EXPENSES

This account consists of the following:

	2006	2005	2004
Prior years' adjustments			
- foreign exchange	554,895,904	-	-
- prior year's expenses	462,042,269	-	-
- taxes and documentary stamp charges	8,156,199	-	-
- BOT energy fees	-	43,077,748	68,399,272
Mineral Exploration/ North Luzon's operating expenses	18,998,648	12,088,516	6,189,789
Bank charges	6,200,119	-	-
Losses on			
- typhoon damages	-	18,939,216	-
- disposal and sale of assets	-	13,936,752	9,540,199
Accelerated amortization of wells/project	-	-	361,114,717
Inflation adjustments on prior year's			
- steam sales	-	-	323,796,262
- electricity sales	-	-	20,564,239
Miscellaneous expenses	18,998,862	1,744,910	9,611,791
	1,069,292,001	89,787,142	799,216,269

The one time prior year's net foreign exchange adjustments pertain to the amortization adjustments of BOT lease obligations for Malitbog and Mindanao 1 power plants due to change in estimates owing to changes in contracts provisions.

Prior year's expenses are accounted mainly by the ₱285,686,577 guarantee fees on long-term foreign loans coupled with the ₱70,122,322 adjustments on prior year's Capital Cost Recovery amortization of the Upper Mahiao BOT lease obligation, which was completed in June 2006, and the ₱66,516,137 payment to Mindanao 1 Geothermal Partnership of the previously contested energy efficiency from March 4, 1997 to December 31, 2005 in accordance with the provision included in the contract extension executed on November 17, 2006.

33. FINANCE COSTS

This account consists of the following:

	2006	2005	2004
Interest on long-term loans	2,274,584,618	2,220,453,119	1,822,098,658
Interest on short-term loans	5,704,019	-	18,212,207
	2,280,288,637	2,220,453,119	1,840,310,865
Amounts included in the cost of qualifying assets	(181,335,739)	(110,113,470)	(19,932,865)
	2,098,952,898	2,110,339,649	1,820,378,000

This account pertains to interest charges on long-term loans. The amount included in the cost of qualifying assets represents the capitalized interest charges on loans utilized for the development of Northern Negros Geothermal Power Plant Project.

34. FOREIGN EXCHANGE GAIN (LOSS)

This account consists of the following:

	2006	2005	2004
Foreign exchange gains (losses) on long-term loans	3,029,487,100	6,583,671,373	(2,033,475,304)
Foreign exchange gains (losses) on other accounts	(144,392,351)	(165,030,989)	95,310,289
Net	2,885,094,749	6,418,640,384	(1,938,165,015)

This account pertains to foreign exchange gain (loss) on repayment and realignment of foreign loans, short-term placements in US dollar denomination and cash in banks in US dollar and Japanese yen currencies. The foreign exchange gain was attributed largely to the realignment of foreign loans because of the depreciation of yen and appreciation of peso against the US dollar currency (12/31/2006: US\$1=JPY118.934/ PHP49.045; 12/31/2005: US\$1-JPY117.855/PHP53.062; 12/31/2004 US\$1-JPY103.050/PHP56.341).

35. INCOME TAXES

Components of income tax expense are as follows:

	2006	2005	2004
Current tax	1,697,975,135	1,677,383,618	1,120,406,825
Deferred tax	1,868,206,616	2,171,591,063	(51,856,074)
	3,566,181,751	3,848,974,681	1,068,550,751

A numerical reconciliation between tax expense and the product of accounting income multiplied by the tax rates of 35% in 2006 and November to December 2005 and of 32% from January to October 2005 is as follows:

	2006	2005	2004
Accounting income	10,349,106,402	13,765,072,044	3,510,228,395
Tax expense at 35%	3,622,187,241	802,962,536	-
Tax expense at 32%	-	3,670,685,878	1,123,273,086
Tax effect of non-deductible interest expense	55,866,123	56,284,818	46,775,739
Excess of Foreign Contractors' Tax over the allowable tax credit from Lihir operations	2,200,505	-	-
Interest income - net of final tax	(114,072,117)	(121,088,650)	(101,498,074)
Adjustment on the realignment of deferred tax asset balance as of 12/31/2005 at 35%	-	(559,869,901)	-
	3,566,181,752	3,848,974,681	1,068,550,751

36. EARNINGS PER SHARE (EPS)

The earning's per share amount was computed as follows:

	2006	2005	2004
Net income attributable to common shareholders	6,782,924,651	9,916,097,363	2,441,677,644
Weighted average numbers of shares for EPS	10,597,379,392	10,000,000,000	10,000,000,000
Basic/Diluted earnings per share	0.640	0.992	0.244

Computation of weighted average number of shares for earnings per share

	Beginning Balance	Shares Issued	Outstanding Shares	No. of Days ⁽¹⁾	No. of Days ⁽²⁾
Dec. 31, 2005	10,000,000,000		10,000,000,000	282	365
Oct. 9, 2006	10,000,000,000	2,000,000,000	12,000,000,000	65	83
Dec. 13, 2006	12,000,000,000	2,608,695,652	14,608,695,652	5	18
Dec. 18, 2006	14,608,695,252	391,304,348	15,000,000,000	13	13
Dec. 31, 2006				365	
Weighted Average Number of Shares for EPS (1)		10,597,379,392			
Weighted Average Number of Shares for EPS (2)		10,597,379,392			

37. STAFF COSTS

This account consists of the following:

	2006	2005	2004
The aggregate remuneration comprises of:			
Salaries and other benefits	1,968,065,036	1,905,208,595	1,926,364,360
Retirement benefit costs (see Note 43)	121,063,507	504,917,081	232,663,015
Social security costs	35,299,516	35,626,807	36,415,498
	2,124,428,059	2,445,752,483	2,195,442,873

38. SERVICE CONTRACTS

By virtue of PD 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 P180 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 P200 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 PNOC EDC operating projects. However, remittances to the local government units of their share in royalty fees are made as they fall due pursuant to the Local Government Code.

Total royalty fees due to DOE and to LGUs are shown in Note 21.

The DOE approved the application of PNOC EDC for the 20-year extension of the Tongonan, Palinpinon and Bacon-Manito Geothermal Service Contracts (GSCs). 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.

39. GEOTHERMAL STEAM SALES CONTRACT

The geothermal energy currently produced by the Company's geothermal projects is supplied to its BOT contractors and the power plants owned and operated by NPC pursuant to the following 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 twenty-five years.

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 twenty years commencing on December 25, 1988.

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 twenty-five years for each module commencing 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 twenty-five years commencing 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 twenty-five years commencing in March 1994 for Cawayan and December 1997 for Botong.

40. BUILD-OPERATE-TRANSFER (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 commencing 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 PNOC EDC on June 25, 2006.

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 commencing 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.

41. POWER PURCHASE AGREEMENTS

The electricity produced by the Company, through its BOT Contractors, is sold to NPC, pursuant to the following Power Purchase Agreements (PPA):

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 PNOC EDC 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 combined annual nominated energy starting July 25, 2000 is currently under negotiation with NPC. The contracts are for a period of twenty-five 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 twenty-five years commencing 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 twenty-five years commencing in June 1999.

42. PRIVATIZATION

The Company was granted approval by then President Fidel V. Ramos on June 14, 1996 to divest 60% of the National Government shareholdings in the Company through PNOC, in line with the government's policy of restructuring the power sector. In April 1997, the Committee on Privatization (COP) approved the proposed privatization plan recommending for the sale of approximately 30% to 40% of the Company's shares through an initial public offering (IPO) and the remaining 20% to 30% of shareholdings to a strategic investor through an auction process. The plan was approved by then President Fidel V. Ramos in July 1997.

On November 5, 1997, the PNOC Board, upon recommendation of the privatization advisors, decided to postpone the Company's privatization, in view of the unfavorable equity market conditions.

On November 23, 2004 and December 10, 2004, the Board of Directors of PNOC EDC & PNOC, respectively, approved the re-activation of plans to privatize PNOC EDC.

In February 2005, PNOC EDC awarded the mandate for financial advisory/underwriting/global coordinating services to CLSA Exchange Capital, Inc.

PNOE EDC's approach to privatization involves the sale through public bidding of PNOE EDC shares of stock after a pre-negotiated Steam Sales Agreement (SSA) between Power Sector Assets and Liabilities Management Corporation (PSALM) and PNOE EDC is finalized. This was presented to and approved by the PNOE EDC and PNOE Boards in October and November 2005, respectively.

In May 2006, a resolution was passed by the Joint Congressional Power Commission (JCPC) endorsing the proposed plan to sell as a package each geothermal plant combined with a specific long-term SSA between PNOE EDC and Power Sector Assets and Liability Management (PSALM).

In June 2006, the Privatization Council (PrC) approved PNOE EDC's privatization plan, involving the following:

- a. The sale through an Initial Public Offering (IPO) of approximately 30% to 40% of PNOE EDC's outstanding capital stock (after subscribing to 1.76 to 2.5 billion shares of the newly created 5.0 billion shares).
- b. The break-up of the IPO into approximately equal number of primary and secondary shares.

PNOE EDC successfully completed its IPO of 5.22 billion shares last December 13, 2006 at ₱3.20 per share. These shares represent 35.73% of the Company's outstanding capital. Another 0.78 billion shares, representing the over allotment option were listed last December 18, 2006 when CLSA exercised its "greenshoe option". This brings to 6.0 billion the number of PNOE EDC shares already sold to the public as of December 31, 2006, i.e., representing 40% of the Company's outstanding capital.

From the IPO, PNOE and PNOE EDC's gross proceeds reached ₱9.6 billion each from the sale of secondary and primary shares, respectively.

43. RETIREMENT BENEFIT PLANS

The Company established a funded, non-contributory retirement plan administered by a trustee bank, covering all its regular employees. Retirement costs include current service cost, experience adjustments and changes in actuarial assumptions. Actuarial gains and losses are recognized as income or expense when the cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains and losses are recognized over the expected average remaining working lives of the employees participating in the plan.

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out for December 31, 2006 by Feliciano F. Miravite, Inc. The present value of the defined benefit obligation and the related current service cost was measured using the projected unit credit method.

	Valuation at	
	2006	2005
Key assumptions used:		
Discount rate p.a.	7.00%	10.12%
Expected return on plan assets p.a.	10.00%	11.87%
Expected rate of salary increases p.a.	6.00%	7.00%

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 MART. The assumption on the expected rate of return on plan assets is based on asset allocation while the expected rate of salary increases is based on discussion with the management which is around 1%-2% more than the projected inflation rate of about 4%-5%.

Amounts recognized in income and expense in respect of these defined benefit plan are as follows:

	2006	2005
Current service cost	97,756,610	119,616,100
Interest cost	150,770,729	192,005,800
Expected return on plan assets	(122,261,769)	(197,662,400)
Recognition of actuarial gain	(33,404,348)	(43,356,400)
	92,861,222	70,603,100

The actual return on plan assets was ₦152.8 million in 2006 and ₦144.7 million in 2005.

The amount included in the balance sheet arising from the Company's obligations in respect of its defined retirement benefit plan is as follows:

	2006	2005
Present value of defined benefit obligations	2,187,879,669	1,791,112,900
Fair value of plan assets	(1,468,777,785)	(1,222,617,693)
Deficit in plan	719,101,884	568,495,207
Unamortized portion of actuarial gains	150,467,454	335,026,000
Liability recognized in the balance sheet	869,569,338	903,521,207

Movements in the present value of defined benefit obligations in the current period were as follows:

	2006	2005
At January 1	1,507,707,292	1,758,346,871
Service cost	97,756,610	119,616,100
Interest cost	150,770,729	192,005,800
Actuarial losses	465,063,808	358,560,000
Actual pension payments	(33,418,770)	(13,975,200)
Effect of settlement	-	(623,440,671)
At December 31	2,187,879,669	1,791,112,900

The difference in the present value of defined benefit obligation as of December 31, 2005 and as at January 1, 2006 was due to the estimated/tentative data used when the actuarial valuation study was conducted in December 2005.

Movements in the fair value of plan assets in the current period were as follows:

	2006	2005
At January 1	1,222,617,693	1,594,938,211
Expected return on plan assets	122,261,769	197,662,400
Actuarial gains and (losses)	30,504,002	(52,946,718)
Contributions from the sponsoring companies	126,813,090	110,767,300
Benefits paid	(33,418,770)	(627,803,500)
At December 31	1,468,777,784	1,222,617,693

The breakdown of the investment portfolio is as follows:

	2006	2005
Debt instruments	1,262,184,201	1,096,892,483
Equity instruments	156,841,630	59,376,328
Property	27,855,825	27,855,825
Other assets	13,286,126	37,607,191
	1,460,167,782	1,221,731,827

44. CONTINGENT LIABILITIES

As Petitioner

Case No.	Particulars
CA GR CV 962449	PNOE EDC vs. PNG Construction and Dev. Corp., et al. Venue: Court of Appeals, Manila Re: Breach of contract and damages PNOE EDC's claim against PNG

This case resulted from the contract entered into between PNOE EDC and China State Construction and Engineering Corporation (CSCEC) for the construction of the Bacon-Manito I Fluid Collection and Disposal System. Among other things, this contract provided for the construction of the Logistics and Control Center (LCC). CSCEC sub-contracted the LCC portion of the project to PNG Construction and subsequently assigned and transferred to PNOE EDC all its rights, interests, liabilities and obligations in the sub-contract agreement. PNG Construction failed to finish the job contract. PNOE EDC filed the instant case but the Regional Trial Court of Makati City ruled in favor of PNG Construction. PNOE EDC then appealed the case to the Court of Appeals where the case is still pending resolution.

As Defendant

Case No.	Particulars
CA G. R. Sp. No. 81231	Frederick Ubag, et al vs. PNOC EDC/ NCV/JMQ/RBC Venue: Court of Appeals, Cebu City Re: Illegal Dismissal This is a labor case involving contractual/term employees hired and engaged in connection with the construction and development stage of the Palimpinon II Fluid Collection and Reinjection System (Pal II FCRS). When the civil works for the construction and development stage of the Pal II FCRS had been substantially completed, the respective periods of employment of the contractual/term employees indicated in the contracts likewise ended. PNOC EDC, thus, had to let go of said contractual/term employees, as it had no more activities for which their services can be utilized. Thirty (30) days prior to the termination of their contracts, the concerned employees were served their notices of termination. These employees, numbering more than a hundred, filed their individual complaints which were consolidated by the National Labor Relations Commission (NLRC) Sub-Regional Branch VII, Tacloban City. The Labor Arbiter decided against PNOC EDC, which Decision was modified by the NLRC. PNOC EDC filed a Special Civil Action for Certiorari with the Court of Appeals, Cebu City, which sustained both the Labor Arbiter and the NLRC re: the issue of illegal dismissal but reduced the monetary reward from P2,068,541.36 to P1,182,661.72.
CA G.R. Sp. No. 81542	Nationwide Security & Allied Services, Inc. vs. PNOC EDC Venue: Court of Appeals, Manila Re: Injunction and Damages Claims against PNOC EDC This case stemmed from the public bidding for the security services at PNOC EDC's premises wherein Lockheed Detective and Watchman Agency, Inc. emerged as the lowest qualified bidder. The lowest bidder was actually King Investigation and Security Services, Inc. but was declared not qualified. Nationwide Security & Allied Services, Inc. filed a complaint with the Regional Trial Court (RTC) of Makati City claiming that it was the next lowest bidder. The said complaint was decided in favor of PNOC EDC in respect of the prayer for Temporary Restraining Order and Nationwide Security appealed to the Court of Appeals, Manila, which was decided in PNOC EDC's favor. The main case for Injunction and Damages is set for pre-trial before the RTC of Makati City.
CC 2006-07-77	PNOC EDC vs. Province of Leyte and Loreto B. Ballais et. al. Venue: Eighth Judicial Region, RTC Br. 8, Tacloban City Re: Appeal on Denial of Franchise Tax Protest (P95,097,013.06)
CC 2006-05-49	PNOC EDC vs. Province of Leyte and Loreto B. Ballais et. al. Venue: Eighth Judicial Region, RTC Br. 6, Tacloban City Re: Appeal on Denial of Franchise Tax Protest (P8,298,712.62)

Case No.	Particulars
CC 2006-05-48	<p data-bbox="516 226 1218 258">PNOC EDC vs. Province of Leyte and Loreto B. Ballais et. al.</p> <p data-bbox="516 296 1185 327">Venue: Eighth Judicial Region, RTC Br. 6, Tacloban City</p> <p data-bbox="516 359 1295 390">Re: Appeal on Denial of Franchise Tax Protest (P P8,298,712.62)</p> <p data-bbox="516 422 1541 646">The aforementioned cases resulted from the assessment made by the Provincial Government of Leyte for franchise taxes against PNOC EDC. PNOC EDC timely filed the appropriate protests with the Office of the Provincial Treasurer since the assessments have neither factual nor legal bases. PNOC EDC failed to receive the required response, hence the appeals with the Regional Trial Court of Tacloban City. The corresponding Answers and Replies have already been filed, hence, the parties are just waiting for the notice setting the date for Pre-trial.</p>
	<p data-bbox="516 646 1461 678">PNOC EDC vs. Province of Leyte and Loreto B. Ballais and Atty. Rafael M. Iriarte</p> <p data-bbox="516 709 1266 741">Venue: Local Board of Assessment Appeals, Province of Leyte</p> <p data-bbox="516 772 1541 846">Re: Petition on Cancellation of the Assessment Notice entitled Real Property Tax Order of Payment (RPTOP)</p> <p data-bbox="516 877 1541 1098">This Appeal before the Province of Leyte Local Board of Assessment Appeals filed last October 13, 2006 seeks the cancellation of the Assessment Notice entitled Real Property Tax Order of Payment (RPTOP) dated August 7, 2006 issued by the Leyte Provincial Assessor and Provincial Treasurer, seeking to collect realty taxes on real properties from PNOC EDC located in the municipalities of Kananga, Burauen, Jaro, Albuera and Dagami, all in the province of Leyte, in the aggregate amount of Php 2,603,595,425.30. The first hearing of the case is still to be scheduled.</p>
CA G.R. Sp. No. 94359	<p data-bbox="516 1129 954 1161">A. A. Buenviaje vs. PNOC EDC, et. al.</p> <p data-bbox="516 1192 909 1224">Venue: Court of Appeals, Manila</p> <p data-bbox="516 1255 755 1287">Re: Illegal Dismissal</p> <p data-bbox="516 1318 1541 1455">Labor Arbiter Elias Salinas ruled that A. A. Buenviaje was illegally dismissed by PNOC EDC. Upon appeal by PNOC EDC, said decision, however, was reversed by the NLRC (Third Division) but awarded backwages and other benefits to AAB. Both parties appealed to the Court of Appeals where the case is now pending resolution.</p>
NLRC CA No. 048768-06	<p data-bbox="516 1486 917 1518">J. L. Estrella vs. PNOC EDC, et. al.</p> <p data-bbox="516 1549 828 1581">Venue: NLRC, Quezon City</p> <p data-bbox="516 1612 763 1644">Re: Illegal Dismissal</p> <p data-bbox="516 1675 1541 1770">Labor Arbiter Felipe Pati ruled in favor of J. L. Estrella and the NLRC (Second Division) affirmed the same. PNOC EDC moved for reconsideration. Said motion is still pending resolution.</p>

Case No.	Particulars
NLRC CA No.	J. Fabico vs. PNOC EDC, et. al.
048840-06	Venue: NLRC, Quezon City Re: Illegal Dismissal Labor Arbiter Virginia Luyas-Azarraga ruled in favor of J. Fabico and ordered PNOC EDC to reinstate him to his former position without loss of seniority rights and privileges. The case is on appeal at the Commission Level.

45. SUPPLEMENTARY DISCLOSURES OF GEOTHERMAL RESERVES

In October 2004, PNOC EDC has contracted GeothermEX to provide an independent review of the updated geothermal energy reserves estimation made by the PNOC EDC's Reservoir Engineering Department for four geothermal fields: Bacon-Manito (Luzon), Mindanao (Mindanao), Palinpinon (Negros) and Greater Tongonan (Leyte).

Five available methods of estimating geothermal reserves were considered as regards their applicability to PNOC EDC'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 estimation and numerical simulation are generally useful to PNOC EDC in estimating reserves. PNOC EDC has conducted numerical simulation to most of its fields. A detailed review of one 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 December 2004, used the same volumetric reserve estimation method used by PNOC EDC for the various geothermal fields patterned after the United States Geological Survey but differ only in the heat recovery factor. GeothermEX concluded that PNOC EDC's estimation is conservative due to the low heat recovery factor values of 0.10 to 0.30. On the other hand, GeothermEX estimates of reserves in these field locations are 2.25 times more than those of PNOC EDC.

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 found to be commercial in the future.

The following table shows a comparison of estimated geothermal energy reserves from PNOC EDC and GeothermEx:

Estimated Geothermal Energy Reserves

Field	Mean Reserves PNOC EDC Estimates (MWe)	Mean Reserves GeothermEx Estimates (MWe)	Proved Reserves GeothermEx Estimates (MMBFOE)	Proved Reserves GeothermEx Estimates (GWh of energy)
Greater Tongonan (Leyte)	415	867	145.4	96,940
Palinpinon (Negros Oriental)	170	440	74.4	49,612
Bacon-Manito (Luzon)	185	421	65.3	43,542
Mindanao	203	478	54.1	36,105
Total	973	2,206	339.2	226,199

Source: GeothermEx Report, December 2004

GeothermEx Estimates of Reserves in Million Barrels of Oil Equivalent

Field	Proved Reserves (MMBFOE)	Proved + Probable Reserves (MMBFOE)	Proved + Probable + Possible Reserves (MMBFOE)
Greater Tongonan	145.4	247.2	455.6
Bacon-Manito	65.3	98.2	222.9
Palinpinon	74.4	189.0	211.8
Mindanao	54.1	97.3	171.9
Total	339.2	631.7	1,062.2

Source: GeothermEx Report, December 2004

46. RELATED PARTY TRANSACTIONS

The Due from affiliated companies and due to PNOC accounts consist of the following:

	2006	2005
<i>Due from affiliated companies</i>		
- PNOC Exploration Corporation	2,498,861	398,060
- PNOC Petrochemical Dev't. Corporation	1,354,533	1,354,533
- PNOC Coal Corporation	724,846	724,846
- PNOC Dev't. and Mgt. Corp.	206,863	116,379
	4,785,103	2,593,818
<i>Due to PNOC</i>	350,844,176	364,167,738

- a. Transactions due from affiliated companies represent normally recurring charges and credits which are payable upon presentation of debit/credit notes.
- b. Transactions due to PNOC represent the interests and guarantee fees on loans from IBRD and OECF, which were acquired by PNOC and relented to PNOC EDC being the implementing agency, and the interest on the ₱200 million balance of loan obtained directly from PNOC. Each re-lending agreement is covered by a subsidiary loan agreement. The agreement provides that PNOC EDC shall repay PNOC the principal, interest, commitment charges and such other amounts, fees and charges payable by

PNOG to the lending banks including such amounts incurred by PNOG in connection with the purchase of foreign currencies. Outstanding liabilities of PNOG EDC on such loans are shown as part of the Long-term debt account.

Remuneration of Key Management Personnel

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

	2006	2005	2004
Short-term employee benefits	92,987,472	52,340,297	73,323,538
Post-employment benefits	14,122,040	23,414,458	6,706,292
	107,109,512	75,754,755	80,029,830

47. FINANCIAL RISK MANAGEMENT

The Company's activities expose it to a variety of risks such as liquidity risk, foreign currency risk, interest rate risk, and credit risk. The Company's Enterprise Wide Risk Management Program identifies these risks based on the likelihood of occurrence and impact to the business, formulates risk management strategies, assesses risk management capabilities and continuously monitors the risk management efforts.

Liquidity risk

The Company manages its liquidity profile to be able to finance working and capital expenditures and service debt obligations.

As part of the liquidity risk management program, the Company regularly evaluates the projected and actual cash flow information and continuously assesses conditions in the financial markets for opportunities to pursue fund-raising initiatives. These initiatives include utilization of short-term credit facilities with banks, bank loans and debt capital and equity market issues.

Foreign currency risk

The Company holds financial assets and liabilities that are denominated in U.S. dollar and Japanese yen. Thus, it is exposed to foreign exchange risk arising from the volatility of these currencies. Foreign exchange risk mainly arises from future payments of foreign loans, BOT lease obligations and other commercial transactions.

Meanwhile, the Company's geothermal service contracts, steam sales agreements and power purchase agreements have built-in mechanisms to mitigate the financial risks of movements in foreign currency exchange rates. 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.

The following table shows the Company's foreign currency-denominated monetary assets and liabilities and their peso equivalents as at December 31, 2006 and 2005:

	2006			2005		
	Original Currency		Peso Equivalent ¹	Original Currency		Peso Equivalent ²
	Yen	US Dollar		Yen	US Dollar	
Current Financial Assets						
Cash and cash equivalents	4,508,865	11,190,872	550,838,620	215,569,331	14,212,786	851,214,880
Cash restricted	62,194,849	154,259	33,212,957	-	-	-
Trade and other receivables		401,967	21,167,557		1,158,735	61,578,524
Investment in available-for-sale securities		23,390,000	1,278,631,448		25,390,000	1,460,016,610
Total Financial Assets	66,703,714	35,137,098	1,883,850,582	215,569,331	40,761,521	2,372,810,014

	2006			2005		
	Original Currency		Peso Equivalent ¹	Original Currency		Peso Equivalent ²
	Yen	US Dollar		Yen	US Dollar	
Current Financial Liabilities						
Trade and other payables	1,017,262,067	4,427,423	636,631,670	888,975,132	4,202,692	623,247,498
Due to parent companies	45,067,955	1,555,445	90,639,645	50,416,093	1,512,795	102,970,826
Interest-bearing financial liabilities	1,854,675,232	95,185,940	5,433,207,555	1,360,315,376	161,286,174	9,170,623,237
Total current financial liabilities	2,917,005,254	101,168,808	6,160,478,870	2,299,706,601	167,001,661	9,896,841,561
Noncurrent Financial Liabilities						
Interest-bearing financial liabilities – net of current portion	51,197,880,324	233,431,062	32,561,114,727	47,195,015,517	311,951,951	37,801,456,741
Total Financial Liabilities	54,114,885,578	334,599,870	38,721,593,597	49,494,722,118	478,953,612	47,698,298,302

¹US\$1=JPY118.934 and US\$1= ₱49.045 ²US\$1=JPY117.855 and US\$1= ₱53.062

The Company plans to manage foreign exchange risks, stabilize cash flows, and improve investment and cash flow planning by entering into forward foreign exchange contracts, foreign currency swap contracts and other hedging products aimed at managing the adverse impact of changes in foreign exchange rates in the operating results and cash flows. However, these hedges may not cover all exposures to foreign exchange risks.

Interest rate risk

The Company's income and operating cash flows are substantially independent of changes in market interest rates. The interest rates of finance leases to which the Company is a lessee are fixed at the inception of the lease. These leases expose the Company to fair value interest rate risk.

The Company's cash flow interest rate risk arises from long-term borrowings. Borrowings issued at floating rate expose the Company to cash flow interest rate risk mostly on intervals of six months.

Note 23 shows the Company's long-term foreign currency-denominated obligations with fixed and floating interest rates as at December 31, 2006 and 2005.

Credit risk

The credit risk associated with the Company is its dependence on only one customer – the National Power Corporation, a government-owned-and-controlled corporation.

SEC Number 66381
File Number _____

PNOC ENERGY DEVELOPMENT CORPORATION
(Company's full Name)

PNPC Complex, Merritt Road, Ft. Bonifacio, Taguig City
(Company's Address)

(632) 893-6001
(Telephone Number)

March 31, 2007
(Quarter Ending)

SEC FORM 17-Q
(Form Type)

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-Q

QUARTERLY REPORT PURSUANT TO SECTION 17 OF THE SECURITIES
REGULATION CODE AND SRC RULE 17(2)(b) THEREUNDER

1. For the quarterly period ended **March 31, 2007**
2. Commission identification number: **66381**
3. BIR Tax Identification No. **000-169-125-000**
4. Exact name of issuer as specified in its charter: **PNOC ENERGY DEVELOPMENT CORPORATION**
5. Province, country or other jurisdiction of incorporation or organization: **PHILIPPINES**
6. Industry Classification Code: (SEC Use Only)
7. Address of issuer's principal office Postal Code
PNPC Complex, Merritt Road, Ft. Bonifacio, Taguig City **1201**
8. Issuer's telephone number, including area code: **(632) 893-6001**
9. Former name, former address and former fiscal year, if changed since last report: **Not Applicable**
10. Securities registered pursuant to Sections 8 and 12 of the Code, or Sections 4 and 8 of the RSA

<u>common stock outstanding</u>	Number of shares of <u>Title of each Class</u>
Common Stock, P1.00 par value	15,000,000,000

11. Are any or all of the securities listed on a Stock Exchange? **Yes**

If yes, state the name of such Stock Exchange and the class/es of securities listed therein:

Philippine Stock Exchange

Common Stock

12. Indicate by check mark whether the registrant:

(a) has filed all reports required to be filed by Section 17 of the Code and SRC Rule 17 thereunder or Sections 11 of the RSA and RSA Rule 11(a)-1 thereunder, and Sections 26 and 141 of the Corporation Code of the Philippines, during the preceding twelve (12) months (or for such shorter period the registrant was required to file such reports)

Yes [] No []

(b) has been subject to such filing requirements for the past ninety (90) days.

Yes [] No []

PART 1 FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Our unaudited financial statements for the quarter ended March 31, 2007 have been prepared in accordance with generally accepted accounting principles in the Philippines (“Philippine GAAP”) and are filed as Annex I of this report.

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (“MD & A”)

The following is a discussion and analysis of the Company’s financial performance for the quarter ended March 31, 2007. The prime objective of this MD&A is to help the readers understand the dynamics of our Company’s business and the key factors underlying our financial results. Hence, our MD&A is comprised of a discussion of our core business, and an analysis of the results of operations. This section also focuses on key statistics from the unaudited financial statements and pertains to risks and uncertainties relating to the geothermal industry in the Philippines where we operate up to the stated reporting period. However, our MD&A should not be considered all inclusive, as it excludes unknown risks, uncertainties and changes that may occur in the general economic, political and environment condition after the stated reporting date.

Our MD&A should be read in conjunction with our unaudited financial statements and the accompanying notes. All financial information is reported in Philippine Pesos (PhP) unless otherwise stated.

Any references in this MD&A to “we”, “us”, “our”, “Company” means the PNOC Energy Development Corporation.

Additional information about our Company can be found on our corporate website www.energy.com.ph.

OVERVIEW OF OUR BUSINESS

Principal Products or Services

As of March 31, 2007, with the inauguration of the Northern Negros Geothermal Project in February, the Company now operates twelve geothermal projects in the five geothermal service contract areas where it is principally involved in:

1. the production of geothermal steam for sale to National Power Corporation (NPC) pursuant to Steam Sales Agreements (SSAs) and
2. the generation of electricity for sale to NPC, and for Northern Negros, to electric cooperative and distribution utilities.

As a result of this, the Company has evolved into being one of the world's leading geothermal energy producers with the expertise it has accumulated for geothermal energy exploration and development, reservoir engineering and management, drilling, engineering design and construction, environmental management and energy research and development.

In 2007, it is once again providing drilling equipment and rig personnel to the Lihir Management Company based on the contract signed in February this year.

Percentage of sales of or revenues contributed by foreign sales

In addition to the ₱4,967.6 million in revenues from steam and electricity sales, the Company generated ₱126.3 million from the contract it entered into with Lihir Management Company in Papua, New Guinea. This represents 2.4% of the Company's gross revenues for the first quarter of 2007.

Distribution method of products and services

All of the 1,470 GWh generated by the Company from its steam and electricity business was sold to NPC. It is NPC's responsibility to convey the electricity generated, by either its own or the Company's geothermal power plant, through the high voltage backbone system to distribution utilities, electric cooperatives or bulk power customers.

New Products or Services

Commercial sale of the Company's electricity production from its Northern Negros Geothermal Project, which was inaugurated on February 2, 2007, is scheduled to commence in June 2007 after the power plant commissioning tests have been concluded. As previously disclosed, two (2) Electricity Supply Agreements (ESAs) had already been consummated in 2006. These are with the Iloilo I Electric Cooperative, Inc. (ILECO) and the Visayan Electric Company, Inc. (VECO) for the supply of 606 GWh and 635 GWh for a five-year period, respectively.

Competition

The Company's geothermal steam competes against other major energy sources used for the production of electricity, particularly coal, natural gas and oil. Of these, coal and oil are imported.

For the supply of geothermal energy, the only other company operating in the Philippines is Unocal Philippines Inc., which was recently acquired by Chevron and is now named Chevron Philippines Geothermal Holdings.

With the Government's commitment to the privatization of the majority of the NPC-owned power generation facilities and the establishment of the Wholesale Electricity Spot Market (WESM), the Company will be exposed to a diversified base of Independent Power Producer (IPP) off takers (at some point in the future).

Additionally, non-Philippine companies that are providing geothermal consultancy services in the Asia-Pacific region are West Japan Engineering Consultancy, GeothermEx and Sinclair Knight Merz Engineering Consultancy.

Dependence on one major customer

The Company's steam and electricity revenues are derived from existing long term supply agreements with NPC.

Concessions and royalty payments

The five geothermal service contract areas where the Company's geothermal steam fields are located are:

1. Leyte Geothermal Production Field (expiring on 2031)
2. Southern Negros Geothermal Production Field (expiring on 2031)
3. Bacman Geothermal Production Field in Luzon (expiring on 2031)
4. Mindanao Geothermal Production Field (expiring on 2017)
5. Northern Negros Geothermal Production Field (expiring on 2024)

KEY PERFORMANCE INDICATORS

The top five (5) key performance indicators are set forth below:

Ratio	March 31, 2007	March 31, 2006
Current Ratio	1.53	0.77
Debt-to-Equity Ratio	1.07	2.74
Net Debt-to-Equity Ratio	0.85	2.55
Return on Assets	0.02	0.03
Return on Equity	0.05	0.17

Current Ratio – Total current assets divided by total current liabilities.

This ratio is a rough indication of a company's ability to pay its short-term obligations. Generally, the higher the current ratio, the greater is the "cushion" between current obligations and a company's ability to pay them.

Debt Equity Ratio – Total interest-bearing debts divided by stockholders' equity.

This ratio expresses the relationship between capital contributed by creditors and that contributed by owners. It expresses the degree of protection provided by the owners for the creditors. The higher the ratio, the greater the risk being assumed by creditors. A lower ratio generally indicates greater long-term financial safety.

Net-Debt-to-Equity Ratio – Total interest-bearing debts less cash & cash equivalents divided by stockholders' equity.

This measures the company's financial leverage and stability. A negative net debt-to-equity ratio means that the total of cash and cash equivalents exceeds interest bearing liabilities.

Return on Assets – Net Income divided by total assets (average).

This ratio is an indicator how profitable a company is relative to its total assets. This also gives an idea as to how efficient management is at using its assets to generate earnings.

Return on Equity – Net income divided by average total stockholder's equity.

This ratio reveals how much profit a company earned in comparison to the total amount of shareholder equity found on the balance sheet. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. For the most part, the higher a company's return on equity compared to its industry, the better.

OPERATING REVENUES AND EXPENSES

FINANCIAL HIGHLIGHTS

For the Quarter ended March 31, 2007:

- PNOC EDC posted a recurring net income of ₱1,304.3 million, 5% higher than the amount posted for the same period in 2006, due to lower peso value of its foreign-currency denominated transactions with the appreciation of the peso against the US dollar, particularly the payment for BOT fees, payments of interest and principal amortization on foreign loans.
- Cash and cash equivalents are at a record high of ₱6,376.4 million, 133% higher than the March 31, 2006 level.
- Year-on-year, total capital expenditures increased by ₱99.6 million.
- Net income decreased by ₱741.1 million, or 33%, to ₱1,502.9 million compared to the same period in 2006 primarily due to the decrease in foreign exchange gains from ₱1,242.8 million to ₱290.2 million in 2007.

RESULTS OF OPERATIONS

The following table details the results of operations for PNOC EDC for the first quarter of 2007 and first quarter of 2006.

Results of Operations (In millions of pesos)	YTD Mar. 31, 2007	YTD Mar. 31, 2006	YoY Change
Net Sales	5,093.9	5,286.8	-4%
Cost of Sales	2,374.8	2,468.4	-4%
Gross Profit	2,719.1	2,818.4	-4%
Other Operating Income	125.9	197.9	-36%
Operating Expenses	354.8	378.9	-6%
Other Operating Expenses	28.8	8.4	244%
Income from Operations	2,461.4	2,629.0	-6%
Finance Costs	470.5	441.7	7%
Foreign Exchange Gain	290.1	1,242.8	-77%
Income Before Income Tax	2,281.0	3,430.1	-33%
Provision for Income Tax	778.1	1,186.1	-34%
Net Income	1,502.9	2,244.0	-33%
EBITDA	2,943.4	3,044.5	-3%
Recurring Net Income	1,304.3	1,244.2	5%

YTD March 31, 2007 vs. YTD March 31, 2006

Net Sales

Net sales for the period ended March 31, 2007 decreased by ₱192.8 million, or 4%, to ₱5,094.0 million from ₱5,286.8 million during the same period in 2006 primarily due to the decrease in both the average price/KWh and billed volume for electricity sales.

Sales of Electricity

Sales of electricity decreased by ₱206.9 million, or 5%, to ₱3,759.7 million in the first quarter of 2007 from ₱3,966.6 million during the same period in 2006 on account of the following:

- ₱0.1168/KWh decrease in average price due to lower inflation factor as influenced by the appreciation of Peso against the US dollar (₱146 million)
- 14.2 GWh decline in Leyte BOT's lower sales volume owing to the reduction of nominated energy to within NPC's financial capacity for the Leyte BOT (₱45 million)
- Billing in the first quarter of 2006 of the 2005 inflation adjustments while none in the same quarter of 2007 for the 2006 inflation adjustments owing to the unavailability of the final indices from the National Statistics Office (₱16 million)

Sales of Steam

Sales of steam increased by ₱16.8 million, or 1%, to ₱1,208 million in the first quarter of 2007 from ₱1,191.2 million during the same period in 2006. The increase came primarily from the ₱0.0233/KWh average hike in average price due to higher inflation factor, partly reduced by the 1.6 GWh drop in sales volume in the first quarter of 2007 due to the decrease in dependable capacity of Palinpinon 2 (Okoy module) from 20 MW to 19.01 MW based on the result of the test conducted in May 2006.

Sales of Drilling Services

Sales of drilling services decreased by ₱2.7 million, or 2%, to ₱126.3 million in the first quarter from ₱129 million during the same period in 2006. The sales generated during the period pertain only to the Separable Portion No. 1 or mobilization charges billed in March 2007 for the new drilling service contract with the Lihir Management Company in Papua, New Guinea. The contract started only on March 12, 2007 (spud-in date). Comparably, the sales generated for the same period in 2006 represented drilling operations for a full quarter as part of a drilling service contract which started on August 22, 2005 and ended in June 2006.

Cost of Sales

Cost of sales decreased by ₱93.5 million, or 4%, in the first quarter of 2007 to ₱2,374.9 million from ₱2,468.4 million for the same period in 2006. The favorable variance was largely contributed by this period's lower BOT fees (₱177 million) due to the completion of the BOT contract for Upper Mahiao power plant in June 2006 and the appreciation of the Peso against the US dollar during the first quarter of 2007 as compared to the same period in 2006.

This was partly offset by this period's insurance premiums and business taxes for the real properties in Leyte including the Upper Mahiao power plant turned over to the Company by the BOT contractor in June 2006 (₱87 million). None was paid for the same period in 2006.

Other Operating Income

Other operating income decreased by ₱71.9 million, or 36%, in the first quarter of 2007 to ₱126 million from ₱197.9 million during the same period in 2006. The decrease was primarily attributed to higher interest income on investment/placement funds during the first quarter of 2006.

Operating Expenses

Operating expenses decreased by ₱24.1 million, or 6%, in the first quarter of 2007 to ₱354.8 million from ₱378.9 million during the same period in 2006. The favorable variance was brought about mainly by this period's lower accrual of retirement benefits based on the result of the latest actuarial study conducted in December 2006.

Other Operating Expenses

Other operating expenses increased by ₱20.5 million, or 244%, in the first quarter of 2007 to ₱28.9 million from ₱8.4 million during the same period in 2006, mainly due to this period's payment of the prior year's real property tax to Kananga, Leyte.

Finance Costs

Finance costs increased by ₱28.8 million, or 7%, to ₱470.5 million in the first quarter of 2007 from ₱441.7 million during the same period in 2006. This increase was brought about by this period's higher accrual of guarantee fees, by ₱107.1 million, particularly for the Miyazawa loans. However, this was reduced by the period's ₱71.6 million drop in interest charges on account of the full settlement of loans from JP Morgan, BOTM and ING in October 2006, December 2006 and February 2007, respectively.

Foreign Exchange Loss (Gain)

Foreign exchange gains dropped by ₱952.7 million, or 77%, to ₱290.2 million in the first quarter of 2007 from ₱1,242.8 million for the same period in 2006 primarily due to lower appreciation of the Peso against the US dollar (3/31/07: 1.7% vs., 3/31/06: 3.6%) based on the closing rates in the 1st quarter of 2006 and 2007.

Provision for (Benefit from) Income Tax

Current taxes increased by ₱220.7 million or 51%, to ₱655.5 million in the first quarter of 2007 from ₱434.9 million during the same period in 2006 caused primarily by the decrease in BOT fees and the realized foreign exchange gain on full settlement of the term loan from ING in February 2007.

Deferred taxes decreased by ₱628.6 million, or 84%, to ₱122.7 million in the first quarter of 2007 from ₱751.2 million during the same period in 2006 mainly due to lower unrealized foreign exchange gain on realignment of long-term foreign loans in the first quarter of 2007 as compared to the same period in 2006.

Net Income

As a result of all the foregoing, net income decreased by ₱741.1 million, or 33%, to ₱1,502.9 million in the first quarter of 2007 from ₱2,244.0 million during the same period in 2006, primarily due to lower foreign exchange gains. In the first quarter of 2007, net income represented 30% of total revenue compared to 42% of total revenue during the same period in 2006.

CAPITAL AND LIQUIDITY RESOURCES

As of and for the quarter ended (in millions of pesos)	Q1 2007	Q1 2006	YoY change
Balance Sheet Data			
Total Assets	71,299.5	67,151.8	6%
Total Debt	41,977.4	53,129.2	-2%
Total Stockholders' Equity	29,322.1	14,022.6	109%

The Company's assets as of March 31, 2007 amounted to ₱71,299.5 million, 6% higher compared to the ₱67,151.8 million level as of March 31, 2006.

Highlights of selected balance sheet accounts follows:

In Million Pesos

	March 31, 2007	December 31, 2006	% Change vs. Dec. 31, 2006	March 31, 2006	% Change vs. March 31, 2006
Cash and cash equivalents	6,376.4	9,999.2	-36%	2,732.8	133%
Investment in available-for-sale securities	1,231.0	1,278.6	-4%	2,692.6	-54%
Other current assets	2,026.2	1,885.5	7%	631.8	221%
Property and equipment, net	14,619.1	14,594.5	0.2%	12,422.1	18%
Power plant, net	2,343.0	2,373.6	-1%	-	n/a
BOT Power plant, net	17,423.2	17,637.8	-1%	20,626.2	-16%
Exploratory and development costs	5,739.9	5,524.5	4%	4,992.0	15%
Deferred tax assets	2,307.2	2,429.8	-5%	3,546.8	-35%
Other non-current assets, net	1,363.4	1,602.4	-15%	2,120.2	-36%
Income tax payable	973.5	507.9	92%	858.8	13%
Royalty fee payable – plus current portion	2,108.7	2,218.5	-5%	2,341.6	-10%
BOT lease obligations – plus current portion	2,039.5	3,179.6	-36%	6,107.8	-67%
Long-term debt – plus current portion	31,333.1	35,697.7	-12%	38,430.9	-18%
Capital Stock	21,278.1	21,278.1	-	10,000.0	113%
Retained Earnings	7,939.1	6,436.2	23%	3,897.3	104%

Cash and cash equivalents

Cash and cash equivalents in March 31, 2007 dropped by ₱3,62.7 million (36%) from end December 2006 level primarily due to the prepayment of the loan from ING bank coupled with the amortization payments made for BOT lease obligations and other outstanding loans.

Cash and cash equivalents for the first quarter of 2007 was higher by ₱3,643.6 million from prior year's level mainly due to the proceeds of the IPO and of the retail treasury bonds that matured on December 31, 2006.

Investment in available-for-sale securities

Investment in available-for-sale securities as of March 31, 2007 was reduced by ₱1,461.6 million as compared to the same level posted for 2006 as portion of peso investments in certain retail treasury bonds matured in December 2006. The proceeds were placed in short-term placement in various banks.

Other current assets

Other current assets for the first quarter of 2007 increased by ₱140.7 million (7%) from December 31, 2006 level mainly due to the payment of insurance for the Upper Mahiao power plant which was turned over to the Company in June 2006.

Compared to the same period in 2006, other current assets grew by ₱1,394.4 million (221%) mainly because of the recognition as prepaid tax of the ₱711.2 million balance of the tax credit certificate issued by the BIR in 2006 coupled with the unamortized portion of prepaid insurance for the Upper Mahiao power plant.

Property and equipment, net

Net property and equipment as of March 31, 2007 surged by ₱2,197 million from a year ago level primarily due to the capital expenditures for the Northern Negros Geothermal Project power plant.

Power plant, net

Power plant, as of March 31, 2007, pertains to the net book value of the Upper Mahiao power plant which was reclassified as company-owned power plant to distinguish it from the power plants still under the BOT contracts, i.e., BOT power plants, net.

BOT power plants, net

The ₱214.6 million depreciation charges for the first quarter of 2007 accounted for the decrease in BOT power plant from the December 31, 2006 recorded balance.

Net BOT power plants balance in March 31, 2007 was lower than the recorded balance last year primarily due to the reclassification of the book value of the Upper Mahiao Plant in 2006.

Exploratory and development costs

Exploratory and development costs as of March 31, 2007 went up by ₱215.4 million from the December 31, 2006 level mainly due to higher development costs in Leyte and Northern Negros.

Compared to the end-balance for the same period last year, exploratory and development costs for the first quarter of 2007 grew by ₱747.9 million mainly due to higher steam field development costs, particularly in Northern Negros and Leyte.

Deferred tax assets

Deferred tax assets went down by ₱122.6 million as of end-March 2007 compared to the December 31, 2006 balance mainly due to the appreciation of the peso against the US dollar.

Compared to end-March 2006 balance, deferred tax asset was lower by ₱1,234.6 million mainly due to the following:

- Decrease in unrealized foreign exchange loss on realignment of long-term foreign loans due to the appreciation of the peso against the US dollar and Yen currencies coupled with prepayment and regular principal amortization of foreign loans – ₱914 million.
- Decrease in foreign exchange loss on BOT lease obligations through amortization under the BIR reporting - P170 million.
- Decrease in allowance for doubtful accounts because of the BIR's issuance of tax credit certificate for the Company's claim for VAT refund, partly offset by the additional overdue receivables from NPC– ₱155 million.

Other non-current assets, net

Other non-current assets in the first quarter of 2007 declined by ₱239 million from end-December 2006 balance essentially due to the Company's payment of the deferred royalty fees for Palinpinon I (DOE share) covering the period 2001 – 2004. The payment is recognized as an addition to other trade receivables from NPC and a reduction from other non-current assets since royalty fees for Palinpinon I are reimbursable from NPC pursuant to the Steam Sales Agreement for the project.

Other non-current assets as of March 31, 2007 was lower by ₱756.6 million l mainly because the end-March 2006 balance included recognition of the ₱457.5 million JBIC's releases to Kanematsu Corporation as part of the Company's loan drawdown for the Northern Negros project. As of the end of the reporting period, this was already recognized under property and equipment due to project completion in February 2007.

Income tax payable

Income tax payable during the first quarter of 2007 surged by ₱465.6 million (92%) as compared to end-December 2006 due to the higher taxable base for non-steam operations owing to the drop in BOT fees coupled with the realized foreign exchange gain on the full settlement of the term loan from ING in February 2007.

Income tax payable as of March 31, 2007 was higher by ₱114.6 million than the reported balance for the same period last year, primarily due to the taxability of the realized foreign exchange gain on the full settlement of the term-loan from ING.

Royalty fee payable (inclusive of current portion)

Royalty fee payable balance as of March 31, 2007 was lower by ₱232.9 million and ₱109.8 million than the comparable end-December 2006 and March 31, 2006, respectively,

attributable mainly to the settlement of royalty fees for Palinpinon I (DOE share) covering the period 2001 – 2004 .

BOT lease obligations (inclusive of current portion)

BOT lease obligations as of March 31, 2007 went down by ₱1,140.1 million from the December 31, 2006 balance mainly due to the regular monthly payments made by PNOC-EDC.

BOT lease obligations was reduced by ₱4,068.3 million from last year's same period level primarily due to the full payment of the Upper Mahiao BOT power plant in July 2006 and the continuing monthly payments in the first quarter of 2007 for the geothermal power plants of Malitbog, Mahanagdong and Mindanao.

Long-term debt (inclusive of current portion)

Long-term debt decreased by ₱4,364.6 million compared to December 2006 level primarily due to the prepayment of the term loan from ING bank in February 2007.

Long-term debt dropped by ₱7,097.8 million from end balance a year ago traceable mainly to the full settlement of loans from BOTM and JP Morgan Chase in the last quarter of 2006, prepayment of the term-loan from ING bank in February 2007 and the continuous amortization payments for other loans.

Capital Stock

The increase in capital stock of P5,000 million in December 31, 2006 from the March 31, 2006 level was mainly due to the increase in the authorized and subscribed capital stock to 15 billion shares with par value of P1.00 per share as approved by the Board of Director's on September 19, 2006 and by the Securities and Exchange Commission on October 9, 2006.

The IPO in December 2006 generated an additional paid-in-capital of ₱6,278.1 million out of the 3 billion primary shares offered to the public.

Retained Earnings

The ₱1,502.9 million earnings for the first quarter of 2007 accounted for the increase in retained earnings from the December 2006 level.

Retained earnings went up by ₱4,041.8 million from the reported balance a year ago primarily due to the ₱4,538.9 million net income from second to fourth quarters of 2006 and the ₱1,502.9 million first quarter's net income in 2007, which were reduced by the ₱2,000 million stock dividend to PNOC in September 2006.

Cash Flow (March 31, 2007 vs. March 31, 2006)

Net cash inflows from operating activities for the first quarter of ₱1,478.8 million was higher than the ₱360.3 million for March 2006 due to the payment of the 2004 and 2005 income taxes amounting to ₱1,663.6 million in the first quarter of 2006. This was the result of the BIR's final approval for the Company to use the finance lease method in treating BOT transactions for income tax computation.

Net cash used in financing activities for the reporting period of ₱4,801.2 million was higher than the net cash used in financing activities of ₱1,876.8 million during the same period last year caused mainly by the full payment of the long-term loan obtained from ING.

FOREIGN EXCHANGE AND INTEREST RATE EXPOSURE

Out of the ₱30,576.3 million long-term foreign loans, 70% is yen-denominated.

To partially mitigate foreign exchange risk, the Company is hedging its JPY12.0 Miyazawa I loan through a JPY/USD Accumulating Forward structure (principal amount only). The loan is due for bullet payment on June 1, 2009 and is equivalent to 23% of the ₱21,488.1 million total yen-denominated liabilities and represents 16% of the total long-term foreign loans.

The hedging of the loan was approved by the Board of Directors last March 20, 2007. However, final Board approval will have to be obtained by Management as soon as the necessary approval from the Department of Finance and the Monetary Board of the Bangko Sentral ng Pilipinas are obtained.

OTHER MATTERS

CASH DIVIDEND

On April 17, 2007, the Board of Directors approved a cash dividend of ₱0.099 per share to stockholders of record as of May 15, 2007 payable on June 6, 2007.

MAJOR STOCKHOLDERS

As of March 31, 2007, the total number of stockholders was 1,010 and the stock price was ₱6.10.

List of Top 20 Stockholders as of March 31, 2007

Rank	Name	Nationality	No. of Shares	%
1	Philippine National Oil Company	Filipino	8,999,999,991	60.00
2	PCD Nominee Corporation	Foreign	5,253,856,354	35.03
3	PCD Nominee Corporation	Filipino	724,790,646	4.83
4	Domingo U. Lim	Filipino	2,000,000	0.01
5	ALG Holdings Corporation	Filipino	700,000	0.00
6	Manuel S. Ogena	Filipino	600,001	0.00
7	The Insular Life Assurance Co., Ltd.	Filipino	600,000	0.00
8	Rosalind Camara	Filipino	531,000	0.00
9	Peter &/or Annabelle C. Mar	Filipino	400,000	0.00
10	Marcelino M. Tongco	Filipino	330,001	0.00
11	Northwest Insurance & Surety Co. Inc.	Filipino	300,000	0.00
12	Hans T. Sy	Filipino	300,000	0.00
13	Edgar V.	Filipino	250,000	0.00

Rank	Name	Nationality	No. of Shares	%
	Cadungog			
14	Catherine L. Tan	Filipino	250,000	0.00
15	Miguel T. Tan	Filipino	250,000	0.00
16	Engracio A. Sanchez	Filipino	220,000	0.00
17	Agnes C. de Jesus	Filipino	200,001	0.00
18	Asuncion J. Espina	Filipino	200,001	0.00
19	Danilo M. Capapas	Filipino	200,000	0.00
20	Daniel D. Tagaza	Filipino	200,000	0.00

BOARD OF DIRECTORS

As of March 31, 2007, the members of Board of Directors of PNOC EDC are as follows:

Antonio M. Cailao	Chairman
Paul A. Aquino	Director
Benjamin F. Tugonon	Director
Danilo-Luis M. Mariano	Director
Ernesto Amatong	Director
Benito Q. Bengzon	Director
Nicasio P. Rodriguez, Jr.	Director
Ralph A. Salazar	Director
Asuncion Jimenez Espina	Director

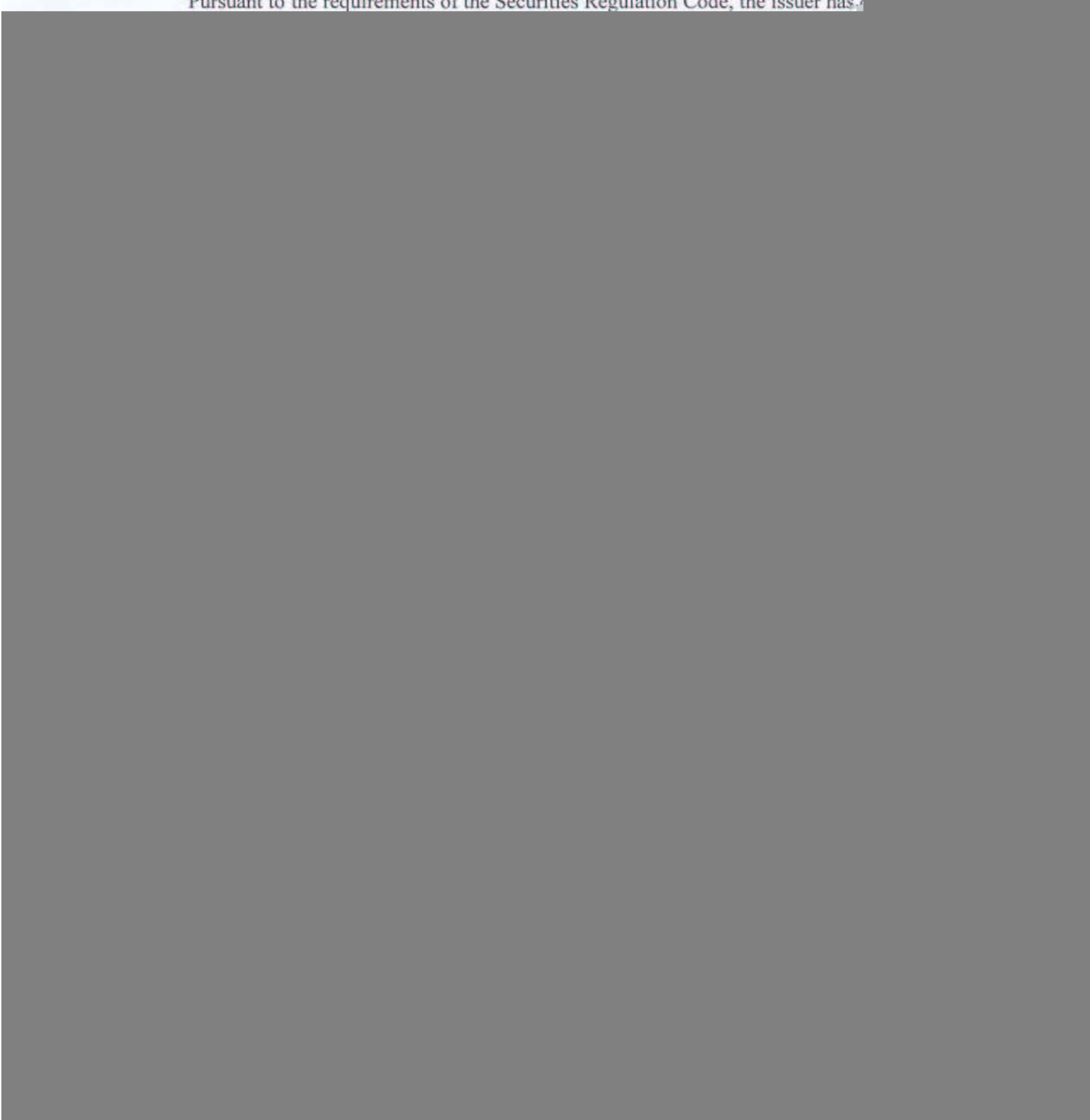
KEY OFFICERS

As of March 31, 2007, the key officers of PNOC EDC are as follows:

Name	Position
Paul A. Aquino	President and Chief Executive Officer
Ester R. Guerzon	Vice President for Corporate Services
Agnes C. de Jesus	Vice President for Environmental and External Relations
Marcelino M. Tongco	Vice President for Operations
Manuel S. Ogena	Vice President for Technical Services
Danilo C. Catigtig	Vice President for Power Generation
Fenina O.T. Rodriguez	Treasurer
Roberto V. San Jose	Corporate Secretary
Ana Maria A. Katigbak-Lim	Assistant Corporate Secretary
Michael R. Rodriguez	Sr. Manager, Internal Audit
Francis M. Dolor	Sr. Manager, Planning and Control
Michael A. Medado	Sr. Manager, Human Resources & Legal
Elvira L. Punsalan	Sr. Manager, Supply, Procurement and Materials Management Division
Mario L. Taguines	Sr. Manager, Engineering, Procurement and Design
Francisco A. Palafox	Sr. Manager, Power and Sales
Gino P. de la Cruz	Resident Manager, NNGPF
Ellsworth R. Lucero	Resident Manager, MGPF
Dwight A. Maxino	Resident Manager, SNGPF
Manuel C. Paete	Resident Manager, LGPF
Liberato S. Virata	Resident Manager, BGPF

SIGNATURES

Pursuant to the requirements of the Securities Regulation Code, the issuer has filed



Annex I

PNOC ENERGY DEVELOPMENT CORPORATION

(A Subsidiary of the Philippine National Oil Company)

Financial Statements

March 31, 2007 and 2006

(Unaudited)

PNOC ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)

BALANCE SHEETS

In Philippine Peso

	March 31		Dec. 31
	2007 (Unaudited)	2006 (Unaudited)	2006 (Audited)
ASSETS			
Current Assets			
Cash and cash equivalents	6,376,444,757	2,732,852,928	9,999,202,227
Cash - restricted	20,476,270	-	33,212,957
Trade and other receivables, net	4,529,477,810	4,249,201,951	4,378,239,217
Parts and supplies inventories	1,182,425,349	1,003,144,689	1,160,998,435
Due from affiliated companies	5,584,448	2,987,387	4,785,103
Investment in available-for-sale securities	1,231,005,967	2,692,646,495	1,278,631,449
Other current assets	2,026,231,160	631,812,908	1,885,512,228
Total Current Assets	15,371,645,761	11,312,646,359	18,740,581,616
Non-Current Assets			
Investments at cost	45,000,000	45,062,500	45,000,000
Property and equipment, net	14,619,111,484	12,422,104,759	14,594,476,289
Production wells, net	11,800,537,412	11,801,067,301	11,905,737,284
Power plant, net	2,343,004,008	-	2,373,564,909
BOT power plants, net	17,423,194,049	20,626,240,620	17,637,817,500
Exploratory and development costs	5,739,866,667	4,992,017,323	5,524,511,412
Investment property, net	278,778,912	279,561,395	278,921,181
Deferred tax assets	2,307,183,714	3,546,827,859	2,429,844,439
Other non-current assets, net	1,363,367,728	2,120,231,138	1,602,404,960
Total Non-Current Assets	55,920,043,974	55,833,112,895	56,392,277,974
Non-Current Assets Held for Sale	7,828,474	5,999,124	7,720,559
TOTAL ASSETS	71,299,518,209	67,151,758,378	75,140,580,149
LIABILITIES AND EQUITY			
LIABILITIES			
Current Liabilities			
Trade and other payables	4,044,214,567	3,969,095,479	4,091,156,339
Income tax payable	973,462,654	858,822,785	507,932,215
Due to PNOC	359,308,936	370,544,071	350,844,177
Royalty fee payable	524,424,026	623,397,214	524,644,631
BOT lease obligations	1,786,640,780	4,423,183,586	2,766,401,494
Long-term debt	2,326,071,039	4,455,217,050	3,171,351,515
Total Current Liabilities	10,014,122,002	14,700,260,185	11,412,330,371
Non-Current Liabilities			
Royalty fee payable, net of current portion	1,584,256,268	1,595,125,120	1,816,945,624
BOT lease obligations, net of current portion	252,899,004	1,684,608,397	413,180,565
Long-term debt, net of current portion	29,007,057,798	33,975,678,449	32,526,343,253
Retirement benefit obligation	869,569,338	954,602,057	869,569,338
Other long-term liabilities	249,534,622	218,890,102	256,432,845
Total Non-Current Liabilities	31,963,317,030	38,428,904,125	35,882,471,625
TOTAL LIABILITIES	41,977,439,032	53,129,164,310	47,294,801,996
EQUITY	29,322,079,177	14,022,594,068	27,845,778,153
TOTAL LIABILITIES AND EQUITY	71,299,518,209	67,151,758,378	75,140,580,149

See accompanying Notes to Unaudited Financial Statements.

PNOC ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
UNAUDITED STATEMENTS OF INCOME
In Philippine Peso

	Three-month period ended	
	March 31	
	2007	2006
Net Sales	5,093,951,424	5,286,802,566
Cost of Sales	(2,374,859,045)	(2,468,415,079)
Gross Profit	2,719,092,379	2,818,387,487
Other Operating Income	125,999,120	197,855,778
Operating Expenses	(354,782,878)	(378,914,489)
Other Operating Expenses	(28,882,561)	(8,386,907)
Inome from Operations	2,461,426,060	2,628,941,869
Finance Costs	(470,524,614)	(441,718,151)
Foreign Exchange Gain (Loss)	290,154,553	1,242,844,870
Income Before Income Tax	2,281,055,999	3,430,068,588
(Provision for) Benefit from Income Tax		
Current tax	(655,530,439)	(434,868,181)
Deferred tax	(122,660,725)	(751,223,198)
Net Income	1,502,864,835	2,243,977,209
<i>See accompanying Notes to Unaudited Financial Statements.</i>		
Earnings Per Share (EPS)		
Basic/Diluted	0.100	0.224

PNOG ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
UNAUDITED STATEMENTS OF CHANGES IN EQUITY
In Philippine Peso

	Capital Stock (Note 25)	Additional Paid-in Capital (Note 25)	Fair Value and Other Reserves (Note 27)	Appropriated Retained Earnings (Note 26)	Unappropriated Retained Earnings (Deficit)	Total Equity
Balance, December 31, 2006	15,000,000,000	6,278,075,648	131,462,811	1,653,315,043	4,782,924,651	27,845,778,153
Net Income					1,502,864,835	1,502,864,835
Unrealized Holding Gain on Available-for-						
Sale Investments			(26,563,811)			(26,563,811)
Balance, March 31, 2007	15,000,000,000	6,278,075,648	104,899,000	1,653,315,043	6,285,789,486	29,322,079,177
Balance, December 31, 2005	10,000,000,000	-	110,309,139	1,653,315,043		11,763,624,182
Net Income					2,243,977,209	2,243,977,209
Unrealized Holding Gain on Available-for-						
Sale Investments			14,992,677			14,992,677
Balance, March 31, 2006	10,000,000,000	-	125,301,816	1,653,315,043	2,243,977,209	14,022,594,068

See accompanying Notes to Unaudited Financial Statements.

PNOC ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
UNAUDITED STATEMENTS OF CASH FLOWS
In Philippine Peso

	Three-month period ended	
	March 31	
	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	5,111,395,408	5,484,473,685
Cash paid to suppliers and employees	<u>(3,096,543,417)</u>	<u>(3,138,591,613)</u>
Cash Generated from Operations	2,014,851,991	2,345,882,072
Interest expenses paid	(346,092,807)	(321,965,314)
Income taxes paid	<u>(190,000,000)</u>	<u>(1,663,596,538)</u>
Net cash from operating activities	<u>1,478,759,184</u>	<u>360,320,220</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of property and equipment	(185,263,278)	(110,187,787)
Exploratory and development costs	<u>(115,064,755)</u>	<u>(90,550,687)</u>
Net cash used in investing activities	<u>(300,328,033)</u>	<u>(200,738,474)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payment of BOT lease obligations	(795,795,496)	(1,081,910,248)
Payment of long-term debt	(4,005,393,125)	(880,138,278)
Long-term loan drawdowns	-	85,229,463
Net cash from (used in) financing activities	<u>(4,801,188,621)</u>	<u>(1,876,819,063)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>(3,622,757,470)</u>	<u>(1,717,237,317)</u>
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>9,999,202,227</u>	<u>4,450,089,945</u>
CASH AND CASH EQUIVALENTS AT END OF PERIOD	<u>6,376,444,757</u>	<u>2,732,852,628</u>

See accompanying Notes to Unaudited Financial Statements.

PNOG ENERGY DEVELOPMENT CORPORATION
(A Subsidiary of the Philippine National Oil Company)
SELECTED NOTES TO THE FINANCIAL STATEMENTS
March 31, 2007

1. CORPORATE INFORMATION

PNOG Energy Development Corporation (PNOG EDC or the Company) was incorporated and registered with the Philippine Securities and Exchange Commission (SEC) on March 5, 1976.

PNOG EDC is a subsidiary of the Philippine National Oil Company which was created under Presidential Decree No. 334 on November 9, 1973.

Presidential Decree Number 334, otherwise known as the Charter of the Philippine National Oil Company (PNOC), empowered PNOC to undertake exploration, discovery and development of all forms of energy resources, including geothermal services of heat and power. In line with this decree, the Company, being a subsidiary of PNOC, entered into service contracts with the Department of Energy (DOE) in 1981 to develop the geothermal resources in Tongonan, Leyte; Palinpinon, Negros Oriental; and Bacon-Manito in Albay and Sorsogon. New service contracts were signed with the DOE for the development of Mt. Apo in North Cotabato (March 24, 1992), Mt. Labo in Camarines Norte (March 14, 1994), Northern Negros (March 24, 1994), and Mt. Cabalian in Southern Leyte (January 13, 1997). The contracts grant certain rights and privileges to the Company in the form of tax exemptions (except income tax) and other incentives.

The registered office address of the Company is Merritt Road, Ft. Bonifacio, Taguig City, Metro Manila.

The Audit and Governance Committee approved and authorized for issue the Company's financial statements on May 11, 2007.

2. ACCOUNTING POLICIES

The accompanying condensed financial statements have been prepared in accordance with the Philippine Accounting Standard (PAS) 34, *Interim Financial Reporting*. Accordingly, the condensed financial statements do not include all of the information and footnotes required by generally accepted accounting principles in the Philippines (Philippine GAAP) for complete financial statements as set forth in the Philippine Financial Reporting Standards (PFRS).

The accompanying condensed interim financial statements, which have been prepared under the historical cost convention method except for fair market valuation of financial instruments (financial assets, financial liabilities and equity instruments), are presented in Philippine peso because this is the currency of the primary economic environment in which the Company operates.

The same accounting policies and methods of computation as mentioned in the 2006 audited financial statements were followed in the preparation of the accompanying financial statements.

The March 31, 2006 comparative condensed financial statements were restated for certain adjustments to conform to the current period's presentation.

3. CASH AND CASH EQUIVALENTS

This account consists of the following:

	2007	2006
Cash on hand and in banks	12,457,421	603,761,150
Cash equivalents	6,363,987,336	2,129,091,778
	6,376,444,757	2,732,852,928

4. CASH – RESTRICTED

The cash – restricted in March 31, 2007 represents the balance of fixed term deposits and cash in bank with the Land Bank of the Philippines intended for the payment of West-Jec consultancy services advanced by Japan Bank International Cooperation (JBIC) under the OECF 21st Yen Loan.

5. POWER PLANT

This account pertains to the recognition of the Upper Mahiao power plant which was turned-over to PNO C EDC by CE Cebu (BOT contractor) on June 25, 2006 with a cost of ₱3,670,775,022. The plant's accumulated depreciation amounted to ₱1,327,771,014 as of March 31, 2007. Provision for the three-month period in 2007 amounted to ₱30,560,901.

Meanwhile, the reduction in the cost of BOT Power Plants was mainly due to the reclassification of the cost and accumulated depreciation of Upper Mahiao Power plant to PNO C EDC as a legally-owned power plant. The account BOT Power Plants pertains to the capitalized present value of the stream of future cash payments for capital cost recovery (CCR) fees of the BOT power plants during the ten-year cooperation period discounted at the buy-out rate indicated in the BOT contracts.

6. LONG-TERM DEBT

	2007	2006
Total Dollar-denominated debt	9,088,193,474	16,020,767,381
Total Japanese Yen-denominated debt	21,488,117,181	21,148,764,482
Total Peso-denominated debt	756,818,182	1,261,363,636
	31,333,128,837	38,430,895,499
Current portion	(2,326,071,039)	(4,455,217,050)
Long-term portion	29,007,057,798	33,975,678,449

The Company's foreign-currency denominated long-term debts were translated into Philippine pesos based on the prevailing foreign exchange rates at balance sheet date (USD1=JPY117.924: USD1=PHP48.217 on March 31, 2007 and USD1=JPY117.330: USD1=PHP51.158 on March 31, 2006).

7. EQUITY

a. Capital Stock

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 and other mineral resources. The Company's shares of stocks are 60% owned by PNOC and 40% owned by various investors, both local and foreign.

Details are as follows:

	2007	2006
Common stock		
Authorized & subscribed	15,000,000,000	10,000,000,000
2006 - 15,000,000,000 shares @ ₱1 par value		
2005 - 10,000,000 shares @ ₱1,000 par value		
Additional paid-in capital	6,278,075,648	-
	21,278,075,648	10,000,000,000

As of March 31, 2007, there are 1,010 stockholders of PNOC EDC.

8. EARNINGS PER SHARE (EPS)

The earning's per share amount was computed as follows:

	2007	2006
Net income attributable to common shareholders	1,502,864,835	2,243,977,209
Weighted average numbers of shares for EPS	15,000,000,000	10,000,000,000
Basic/Diluted earnings per share	0.100	0.224

9. Explanatory comments about the seasonality or cyclicity of interim operations

Seasonality or cyclicity of interim operations is not applicable to the Company's type of business because of the nature of its contracts with NPC which includes guaranteed volume under the take-or-pay or the minimum energy off-take provisions.

10. The nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size or incidence

There are no assets, liabilities, equity, net income or cash flows that are unusual because of their nature, size or incidence.

11. The nature and amount of changes in estimates of amounts reported in prior interim periods of the current fiscal year or changes in estimates of amounts reported in prior financial years, if those changes have a material effect in the current interim period.

There are no changes in estimates of amounts in the first quarter of 2007.

12. Issuances, repurchases, and repayments of debt and equity securities

With clearances issued by the Department of Finance and the Bangko Sentral ng Pilipinas, the Company opted to prepay its US\$90 million syndicated loan on February 21, 2007 which was originally due in February 2008. This was to take advantage of the appreciation of the peso against the US dollar. Total estimated savings from foregone interest and guarantee fee amounted to P6.8 million.

Except for the US\$90 million prepayment, there are no issuances, repurchases and repayment of debt and equity securities.

13. Segment revenue and segment results for business segments or geographical segments, whichever is the issuer's primary basis of segment reporting

The Company's reportable segments are as follows:

Electricity generation - represents the production of steam for delivery to the Company-owned Upper Mahiao power plant and to the Build-Operate-Transfer (BOT) power plants which convert steam to electricity for sale by the Company to NPC pursuant to the Power Purchase Agreements (PPAs) entered into by the two parties.

Steam generation - represents the production of geothermal steam for sale to the National Power Corporation (NPC) pursuant to the Steam Sales Agreements (SSAs) entered into by the two parties.

Due to the complexity of disaggregating the operating expenses, assets and liabilities of these segments, which are presently centrally managed, presentation of each segment's financial information will be made by the end of the year.

14. The effect of changes in the composition of the issuer during the interim period, including business combinations, acquisition or disposal of subsidiaries and long-term investments, restructurings, and discontinuing operations

There are no changes in the composition of the registrant during the period.

15. Changes in contingent liabilities or contingent assets since the last annual balance sheet date

There are no material changes in the contingent liabilities or contingent assets since the last annual balance sheet date.

16. Existence of material contingencies and any other events or transactions that are material to an understanding of the current interim period

The Northern Negros Geothermal Project, the first merchant plant of the company, was inaugurated on February 2, 2007. However, this was not yet turned over to PNOC EDC because the power plant was still under reliability testing. Expected commercial operation would be in June 2007.

The two firms which already entered into electricity sales agreements with the Company in 2006 for the project's power generation in 2007 are the Visayan Electric Company, Inc. (VECO) and the Ilo-ilo I Electric Cooperative, Inc. (ILECO), with contracted annual volume of 127.8 GWh and 101 GWh, respectively.

Annex II

PNOC Energy Development Corporation
As of March 31, 2007
(In Million Pesos)

Aging of Accounts Receivable

	Amount
Trade Receivables	
Current	3,845.1
More than 90 days past due	26.1
More than 120 days past due	245.5
Subtotal	4,116.7
Other receivables	412.7
Total Receivables	4,529.4

Breakdown of Liabilities

	2007	2006
A. Current Liabilities		
Accounts Payable	390.4	144.2
Accrued Interest and Other Liabilities	3,653.8	3,824.9
Income Tax Payable	973.5	858.8
Due to Affiliated Companies	524.4	371.5
Total	5,542.1	5,199.4
B. Other long-term liabilities		
Royalty Fee Payable		
Current	359.3	623.4
Non-current	1,584.2	1,595.1
BOT lease obligations		

