

**POWER SECTOR ASSETS AND LIABILITIES MANAGEMENT CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
(In Philippine Peso)

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**1. GENERAL INFORMATION**

The need for reforms in the entire power industry became evident when the power crisis started in 1989 and continued well into the 1990s. Series of laws were then enacted that instituted reforms in the industry. The latest law, and one that embodies the most extensive reforms, was Republic Act No. 9136, known as the Electric Power Industry Reform Act of 2001 or “EPIRA”, enacted on 26 June 2001. The major aspects of the reforms embodied in the EPIRA include: 1) restructuring of the entire power industry to introduce competition in the generation sector; 2) change from government to private ownership; and 3) introduction of a stable regulatory framework for the electricity sector.

**National Power Corporation (NPC)**

From NPC’s creation in 1936 up to the late 1980’s the generation of power and its transmission through the nationwide transmission Grid (the Grid) in the country was vertically integrated, centrally controlled and managed, and wholly-owned by the NPC. Created as a non-stock government corporation, NPC was tasked to undertake the development of hydraulic power and the production of power, subject to existing rights, from Philippine water resources reserved for its use and all other sources, to meet the needs of industrial development and of rural electrification.

In 1971, NPC’s operations were decentralized to its regional centers in Luzon, Visayas and Mindanao. In 1988 and under its Small Island Grid Power Development Program, NPC took over the operation of generating facilities formerly managed by rural electric cooperatives in small islands and installed additional generation plants to make power rates affordable in these remote rural areas. In 1992, the Small Power Utilities and Barge Management Group was formed to handle this operation. This group later became the Small Power Utilities Group (SPUG). A subsequent reorganization was implemented in 1993 brought on by the enactment of the Electric Power Crisis Act of 1993. Five (5) regional profit centers were devolved and functional groups were created in preparation for the planned privatization of the corporation. The said law also liberalized the power industry by allowing more private sector participation in the generation of electricity. NPC, however, retained exclusive ownership and operation of the Grid and continued to own and operate its existing plants and develop new plants.

## *Independent Power Producers (IPPs)*

In 1987, President Corazon Aquino promulgated Executive Order No. 215 to authorize private sector participation in electricity generation to augment the country's power capacity. This resulted in the first investments by IPPs in generation plants. The Electric Power Crisis Act of 1993, brought on by the power crisis that began in 1989, encouraged increased private capital infusion to power generation, and authorized the increase in the return on rate base from 8% to 12%. Due to the incentives under this statute, more private capital was invested on the construction of IPPs, undertaken in partnership with NPC. These undertakings were formed under different BOT (Build-Operate-Transfer) schemes such as:

### IPP-Owned

#### 1. Build-Operate-Transfer (BOT)

Under this contract, the private sector will build a power plant and operate it for a specified cooperation period (to recover capital/operating cost with reasonable return on investment) and, thereafter, transfer ownership to NPC. In return, NPC commits to pay fixed capacity, operation and maintenance (O&M) and variable energy fees.

#### 2. Build-Operate-Own (BOO)

A project proponent is authorized to finance, construct, own, operate and maintain the power plant as well as recover its investment and operating and maintenance cost plus a reasonable return thereon.

#### 3. Energy Conversion Agreement (ECA)

Under this agreement, NPC shall provide fuel supply during the cooperation period.

#### 4. Power Purchase Agreement (PPA) or Electric Power Supply Agreement (EPSA)

The power plant is built, owned and operated by an IPP. NPC enters into a contract to purchase the power generated by the plant at a guaranteed price for a certain period. These are also known as "Insurance capacity plants," which were encouraged by NPC during the years the country is under power crisis to guarantee availability of power in case some of NPC'S based load plants break down.

## 5. Gas Sale and Purchase Agreement (GSPA)

Under this scheme, NPC commits to purchase the natural gas output of the plant. This contractual arrangement is unique to the Ilijan Natural Gas Plant.

IPP contracts may also be classified as BOT-ECA, BOT-PPA, BOO-ECA or BOO-PPA, BOT-EP SA, etc.

### NPC Owned

## 6. Build-Transfer-Operate (BTO)

Under this scheme, NPC obtains a loan for the project and for the private contractor builder, which builds the power plant on a turnkey basis. The private contractor builder turns over the plant to NPC, the owner, upon completion of the project and operates the power plant under an operation and maintenance (O&M) contract with NPC. NPC guarantees purchase of power generated by the plant for the duration of the cooperation period. NPC enters into BTO contracts if it does not want to expand its operation in a particular place, or when the technology for running the plant is new and is better left to the private sector.

## 7. Rehabilitate-Operate-Maintain-Manage (ROMM)

The scheme applies to existing NPC-owned plants that require massive rehabilitation to be able to operate at its rated capacity. NPC enters into a ROMM agreement with a private company, which puts in the needed investment to either replace or repair aging or inefficient equipment, and thereafter operate and maintain the power plant for a certain period. In turn, NPC purchases the power generated by the power plant. The Operate-Manage-Repair (OMR) scheme is a similar contractual arrangement.

## 8. Build-Rehabilitate-Operate-Transfer (BROT)

This scheme is a combination of BOT and ROM where the proponent builds additional power plants and conducts massive rehabilitation of existing NPC power plants. At the end of the cooperation period, the project proponent will transfer the ownership of the power plants to NPC.

## 9. Electricity Supply, Operation and Maintenance (ESOM)

This is a combination of the EPSA scheme and an operation and maintenance agreement with the proponent.

As of December 2008, the existing IPPs are:

Plant Name	Contract Type
<i>NPC-owned</i>	
Caliraya	BROT-PPA
Botocan	BROT-PPA
Kalayaan 1-2 Units	BROT-PPA
Malaya TPP 1 & 2	ROM-ECA
Limay Combined Cycle "A" & "B"	BTO-OMR
Naga Coal I & II (CTPP/Salcon)	ROMM-ECA
Naga Diesel (CDPP 1/Salcon)	ROMM-ECA
Naga GT Land-based (LBGT/Salcon)	ROMM-ECA
Power Barge 117	BTO-ESOM
Power Barge 118	BTO-ESOM
<i>IPP-owned</i>	
Hydro Electric Development Corp	BOO-EPSA
NMHC	BOO-EPSA
Bakun A/C HEP (HEDCOR)	BOT-PPA
Casecnan (NIA)	BOT-PPA
Kalayaan 3 & 4 Units	BROT-PPA
San Roque Multi-Purpose	BOT-PPA
Enron-Subic II	BOT-ECA
Bauang La Union	BOT-ECA
Pagbilao Coal Units 1 & 2	BOT-ECA
Sual Coal FTTP	BOT-ECA
Ilijan Nat Gas	BOT-ECA, GSPA
Leyte A & B	BOO-PPA
Zamboanga Diesel	BOO-ECA
General Santos Diesel	BOO-ECA
Mt. Apo GPP I & II	BOO-PPA
Mindanao Coal (Steag)	BOT

### **Restructuring of the Electric Power Industry**

The EPIRA restructured the power industry by organizing it into four (4) sectors: generation, transmission, distribution and supply. The structural reforms resulted in the following:

- a) Two government-owned and controlled corporations (GOCCs), Power Sector Assets and Liabilities Management Corporation (PSALM) and National Transmission Corporation (TransCo) were created. PSALM takes over the generation and other disposable assets of NPC and manages its financial obligations, while TransCo takes over the transmission functions of NPC;
- b) NPC was retained as a GOCC performing the missionary electrification function through the SPUG;
- c) The distribution and supply sectors were separated to promote retail competition and open access was introduced;
- d) The sale of sub-transmission assets to distribution utilities (DUs) was mandated;
- e) A wholesale trading market for electricity was established;
- f) The end-user rates and retail distribution rates were unbundled according to specific electricity services provided by industry participants;
- g) A universal charge was imposed as part of electricity tariffs;
- h) The Department of Energy (DOE) was given the added role of supervising the restructuring of the electricity industry;
- i) The Energy Regulatory Board (ERB) was abolished and the Energy Regulatory Commission (ERC) was created in its stead;
- j) The National Electrification Administration (NEA) was given the additional mandate of preparing electric cooperatives to operate and compete under a deregulated electricity market;
- k) Electric cooperatives (ECs) were given the option to convert into either a stock cooperative under the Cooperatives Development Act or a stock corporation under the Corporation Code; and
- l) The Joint Congressional Power Commission (JCPC) was created to monitor and ensure the proper implementation of the EPIRA, determine inherent weaknesses in the law and recommend necessary remedial legislation or executive measures.

### **Power Sector Assets and Liabilities Management Corporation (PSALM)**

PSALM was created under the EPIRA to take ownership of all the existing generation assets, independent power producer (IPP) contracts, real estate and all other disposable assets, and to assume all liabilities and obligations of NPC. The principal purpose of PSALM is to manage the orderly sale, disposition and privatization of NPC's assets with the objective of liquidating in an optimal manner all of NPC's financial obligations and stranded contract costs. To strengthen the financial viability of electric cooperatives, PSALM was also tasked to assume all outstanding financial obligations of electric cooperatives to NEA and other government agencies incurred for the purpose of financing the Rural Electrification Program.

PSALM shall exist for a period of twenty-five (25) years from the effectivity of the EPIRA, unless otherwise provided by law, and all assets and liabilities of the Corporation outstanding upon the expiration of its term of existence shall revert to and be assumed by the National Government.

Included in PSALM's mandate is the collection, administration and application of NPC's portion of the universal charge. The universal charge refers to the charge, if any, imposed on all electricity end-users for the following purposes:

- a) Recovery of the stranded debts and stranded contract costs of NPC as well as the qualified stranded contract costs of distribution utilities resulting from the restructuring of the industry. The *stranded debts* of NPC refer to any unpaid obligations which have not been liquidated by the proceeds from the sale and privatization of its assets. *Stranded contract costs* of NPC or distribution utility is the excess of the contracted cost of electricity under eligible contracts over the actual selling price of the contracted energy output of such contracts in the market. Such contracts should have been approved by the Energy Regulatory Board as of December 31, 2000;
- b) Missionary electrification, which refers to the provision by NPC-SPUG of power generation and its associated power delivery systems in areas that are not connected to the transmission system;
- c) Equalization of taxes and royalties applied to indigenous or renewable sources of energy vis-à-vis imported energy fuels;
- d) An environmental charge equivalent to one-fourth of one centavo per kilowatt-hour (P0.0025k/Wh), which shall accrue to an environmental fund to be used solely for watershed rehabilitation and management. Said fund shall be managed by NPC; and
- e) A charge to account for all forms of cross-subsidies for a period not exceeding three (3) years.

The universal charge (UC) is a non-bypassable charge which is passed on and collected from all end-users on a monthly basis by the distribution utilities. The collections by the distribution utilities and TransCo in any given month shall be remitted to PSALM on or before the fifteenth (15<sup>th</sup>) of the succeeding month. Any end-user or self-generating entity not connected to a distribution utility shall remit its corresponding UC directly to TransCo.

## **Asset – Debt Accounts Transfer/Separation of Books**

The transfer of NPC's assets and liabilities was not fully implemented due primarily to the difficulty of immediately obtaining universal consent of NPC creditors to the transfer and the long process of completing the conditions precedent to the transfer. Without creditors' consent, transfers cannot be effectively made without violating the provisions of loan covenants that prohibit the conveyance of the assets financed through the loans. Thus, NPC assets and liabilities remained in the books of NPC.

Notwithstanding this impediment, PSALM began the privatization process by seeking specific consents from creditors for each plant that is to be privatized. Pending the completion of the conditions precedent to transfer, PSALM recognized an obligation to NPC corresponding to the proceeds of the assets sold. Likewise, PSALM began servicing the foreign obligations of NPC from the proceeds of the assets sold and booked it as a receivable from NPC.

The asset transfer from NPC to PSALM began in 2007 with the transfer of the 360 MW Magat Hydro Electric Power Plant, having obtained the specific consent of the creditors and backed by the Deed of Transfer and the Transfer Certificate of Title for the plant.

### Bases

To carry out PSALM's mandate of ownership of assets and assumption of obligations of NPC and the separation of books of NPC and TransCo, the Deeds of Transfer between NPC and PSALM, and between NPC and TransCo, were executed in December 2001. Both Deeds provide that the assignment, transfer and conveyance of the assets and obligations of the executing parties shall become effective upon the fulfillment of certain conditions precedent or the waiver thereof by the appropriate party(ies).

To make the Deeds effective, the respective Boards of PSALM and NPC approved and confirmed the waiver of the conditions precedent under PSALM Board Resolution No. 07-80 dated 14 November 2007 and NPC Board Resolution No. 2007-66 of even date, while the TransCo Board approved and confirmed the waiver of the conditions precedent per Board Resolution No. TC 2008-013 on 09 May 2008.

The Implementing Guidelines for the Asset-Debt Accounts Transfer and Separation of NPC/TransCo Books of Accounts drafted by PSALM/NPC/TransCo were approved for implementation by the PSALM Board on 20 June 2008 per PSALM Board Resolution No. 2008-0620-007 and by the joint PSALM/NPC Boards on 19 July 2008 as stated in PSALM/NPC Board Resolution No. 2008-0719-004.

The legality of the asset-debt transfer was affirmed with the issuance by the Office of the Government Corporate Counsel of Opinion No. 247, Series of 2008, dated 21 October 2008, which states that the clear intent of the EPIRA is the transfer of ownership of the assets of NPC to PSALM.

### Scope and Limitations

The asset-debt accounts transfer covers the transfer to PSALM of the balances of the asset and debt accounts of NPC (except SPUG's) as of 31 December 2008, and to record in TransCo's own separate books its asset and debt accounts, except the long-term loans which were assumed by PSALM.

The account balances transferred were the amounts as reflected in NPC books and did not consider thorough analyses and substantiation. As such, the account balances added to PSALM's books may not be entirely correct. Some accounts, particularly those pertaining to reciprocal transactions between NPC and PSALM, may have not been fully eliminated.

The tasks of validation, confirmation, and accounts' disposition will form the succeeding phase of the asset-debt accounts transfer. Meanwhile, to the extent that resources (time, personnel, availability of documents) allow it, PSALM made some initial account validations which resulted in some P19.535 billion (as of 31 December 2008 and excluding those of TransCo) various account balances being retained in NPC books for validation/confirmation.

### Process

Technical working groups (TWGs) from the three agencies drafted the Implementing Guidelines for the Asset-Debt Accounts Transfer and Separation of NPC/TransCo Books of Accounts. These guidelines were approved by the PSALM Board on 20 June 2008 per PSALM Board Resolution No. 2008-0620-007 and the joint PSALM/NPC Boards on 19 July 2008 per PSALM/NPC Board Resolution No. 2008-0719-004. The TWGs likewise addressed issues specific to the process, and set the cut-off date for the transfer of NPC's accounts to both PSALM and TransCo at 30 September 2008. This date set the cut-off for the following:

- Close-out of all January to September 2008 nominal accounts of NPC (except those for Small Power Utilities Group or SPUG) to its Retained Earnings.

- Transfer by NPC and receipt/recording by TransCo of TransCo's real accounts in its own set of books (excluding some ₱1.848 billion accounts retained in NPC books for validation/confirmation). The difference between the amounts for the assets and liabilities was closed by NPC to its reciprocal account with TransCo, and TransCo, to Equity from PSALM account. PSALM, on the other hand, recognized TransCo as its subsidiary and set up its Investment in TransCo account and credited the same amount to the Capital from Asset-Debt Transfer account.
- Transfer by NPC and receipt/recording by PSALM of the generation-related real accounts in PSALM's books (excluding the ₱19.535 billion accounts retained in NPC books for validation/confirmation). The difference between the amounts for the assets and liabilities was closed by NPC to its Retained Earnings account and PSALM to its Capital from Asset-Debt Transfer account.

#### October to December 2008 Transactions

While the cut-off date was set at 30 September 2008 and the implementation was done in October 2008, full implementation of the asset-debt accounts transfer was effected on 31 December 2008.

The October to December 2008 main grid operations were still processed and recorded in NPC and reflected in its income statement. The 4<sup>th</sup> quarter nominal accounts were then closed to NPC Retained Earnings, with the net effect of the transactions, in both asset and liability accounts, taken up as adjustment to PSALM's Capital from Asset-Debt Transfer account.

#### December 31, 2008 Balances Transferred

Asset transferred to PSALM	
Electric plants under capital lease, net	456,777,856,390
Current assets	101,008,390,595
Utility plant, net	77,103,244,049
Investment and other assets	64,081,241,964
Deferred charges	16,350,152,971
Net assets transferred to TransCo	<u>115,693,280,923</u>
Total assets	831,014,166,892
Liabilities assumed by PSALM	
Lease obligation	451,694,256,752
Long-term debts, net of current portion	280,930,814,340
Current liabilities	150,873,950,481
Deferred credits	21,356,158,403
Total liabilities	<u>904,855,179,975</u>
Capital from asset-debt transfer	<u>(73,841,013,083)</u>

With the transfer of the account balances, NPC was left with the SPUG-related accounts and some generation and transmission-related accounts which were retained for further validation/confirmation. SPUG has an asset base of ₱12.081 billion while the retained accounts total ₱21.383 billion.

### Trust Accounts

Part of the accounts retained in NPC books is the inventory (₱16.132 billion as of 31 December 2008) which, for proper accountability, was established as trust account together with the December 31 cash balances (₱6.523 billion) and net receivables from NPC officers and employees (₱62 million). PSALM treats the trust account as an asset and by NPC as a liability.

### Separate TransCo Books from NPC

The October to December 2008 transmission operations were recorded in TransCo's own books. Full year 2008 operations were, however, reported by TransCo. Also, with the separation of TransCo from NPC and the recognition of PSALM's equity in TransCo, the parent-subsidary relationship of PSALM and TransCo is effected beginning 01 October 2008. As such, TransCo will be consolidated with PSALM's financial statements. PSALM investment in TransCo is accounted for at cost.

### Further Actions

The asset-debt accounts transfer opened a new set of activities for the agencies involved. For PSALM, these include, among others, the following:

- Confirmation of fixed assets transferred from NPC through one or a combination of the following: (i) conduct of inventory to confirm physical existence, (ii) titling to substantiate ownership, and (iii) revaluation to ascertain the assets' fair value;
- Further analyses and validations of other accounts transferred from NPC to determine if the balances present fairly the amounts they purport to represent; and
- PSALM will take the lead in the recommendation to the Commission on Audit (COA) for disposition of the accounts retained at NPC (the balances after analyses and appropriate adjustments).

## **NPC-Transferred Generation Assets**

Generation assets transferred by NPC to PSALM include the following:

### Lands

Angat HEPP	Botocan HEPP (CBK-IMPISA)
Mak-Ban GPP	Ilijan Gas Pipeline
Mak-Ban GPP Ormat	Naga CTPP 1 (Cebu CTPP)
Tiwi GPP	Power Barge 117 (Nasipit) -
Masinloc CFTPP	Upper Agno HEPP
Batangas CFTPP	Pantabangan-Masiway HEPP
Panay DPP	Barit-Cauayan HEPP
Bohol DPP	Loboc HEPP
Agus HEPP 1,2,4,5,6,7	Talomo HEPP
Pulangui HEPP 4	Agusan HEPP
Sual CFTPP	Manila TPP 1 & 2
Buang First Private Power Corp	Sucac TPP 1,2,3,4
San Roque Power Corp	Bataan TPP 1 & 2
Luzon HEPP (Bakun 1)	Bataan GT
ABB Bataan Combined Cycle 1 & 2	Malaya GT
Malaya TPP 1 - Land	Talavera DPP (Cebu DPP 2)
Kalayaan HEPP (CBK-IMPISA)	Aplaya DPP
Caliraya HEPP (CBK-IMPISA)	Gen. Santos DPP

### Generation Plants

#### *Operating*

Angat HEPP	Panay DPP 1
Amlan HEPP	Panay DPP 3
Mak-Ban GPP 1,2,3,4,5,6, Ormat, 7,8,9,10	Bohol DPP
Tiwi GPP 1,2,3,4,5,6	Power Barge 101
Bac-Man GPP 1	Power Barge 102
Bac-Man GPP 2 (Cauayan)	Power Barge 103
Bac-Man GPP 2 (Botong)	Power Barge 104
Tongonan (Leyte) GPP	Agus HEPP 1,2,4,5,6,7
Palinpinon GPP 1	Pulangui HEPP 4
Palinpinon GPP 2 (Nasuji)	Iligan DPP 1
Palinpinon GPP 2 (Okoy)	Talomo HEPP
Palinpinon GPP 2 (Sogongon)	Agusan HEPP
Batangas CFTPP 1	Upper Agno HEPP
Batangas CFTPP 2	Masinloc CFTPP

*Decommissioned*

Manila TPP 1 & 2	Aplaya DPP
Sucac TPP 1,2,3,4	Gen. Santos DPP
Sucac GT LB	Iligan DPP 2
Bataan TPP 1 & 2	Navotas GT 1 (Energy) U1, U2, U3
Bataan GT	Navotas GT 2 (Tileman)
Malaya GT	Naga GT LB 1
Cebu DPP 2	Naga GT LB 2

Independent Power Producers (IPPs)

Bataan CC DPP 1 & 2	Naga DPP 1
Malaya TPP 1 & 2	Naga CFTPP 1 & 2
Kalayaan HEPP	Power Barge 117
Caliraya HEPP	Power Barge 118
Botocan HEPP	

**Operation and Maintenance Agreement (OMA)**

Pursuant to the Implementing Rules and Regulations (IRR) of the EPIRA, PSALM has the power to operate the generation assets, directly or through NPC, prior to privatization of such assets.

The Operation and Maintenance Agreement signed on 17 February 2009 between PSALM and NPC provides for the continued orderly operation and maintenance of the transferred generation and other disposable assets and the provision of necessary corporate services from transfer date until the turn-over of such assets to PSALM. NPC shall also provide preservation services to all decommissioned plants and mothballed plants in accordance with the agreed performance standards to prevent the deterioration of serviceable equipment and systems prior to disposal. Furthermore, NPC shall continue to discharge its duties and obligations under existing IPP contracts. NPC shall turn over the IPP plants under IPP contracts to PSALM after the termination / expiration of the IPP contracts, with PSALM having the option to include these plants in the OMA.

NPC shall prepare the budget it needs for each year to perform its obligations under the OMA and submit the O&M Budget to PSALM for review and approval. Upon approval, PSALM shall release the funding in accordance with the O&M Budget subject to existing accounting and auditing rules and regulations. NPC shall regularly submit to PSALM

reports on the performance of the generation and other assets and the use of the funds.

Using the privatization proceeds and income from the operation of the generation and other assets, PSALM shall be responsible in servicing outstanding obligations of NPC arising from: (1) loans, issuances of bonds, securities and other instruments of indebtedness; and (2) IPP contracts.

### **IPP Administrator (IPPA)**

PSALM was mandated under the EPIRA to competitively select and appoint qualified independent entities called Independent Power Producer Administrators (IPPAs) to administer and manage the contracted energy output of NPC/PSALM IPP contracts. The IPPAs are qualified private sector independent entities that will administer and manage the contracted energy from the ECAs and PPAs that NPC entered into with the IPPs. The IPPAs will be appointed through public bidding to be conducted by PSALM.

Since the Wholesale Electricity Spot Market (WESM) commenced operation in 2006, PSALM has been effectively acting as the interim IPPA by bidding the NPC/PSALM IPPs' energy output into the WESM on a day-by-day basis. PSALM initially split the IPPs into four (4) groups, and set up four (4) trading teams to manage them; this has subsequently been reduced to three (3) teams. The total MW capacity of the portfolios of the trading teams has increased, but is still below the 30% of the Luzon Grid capacity threshold established in the EPIRA.

To ensure that more perspectives are taken into account as PSALM finalizes the terms of reference and bidding rules for the selection of IPPAs, series of consultations were conducted in February, March and October 2008 with the Philippine Independent Power Producers Association (PIPPA), potential investors, plant managers of independent power producers (IPPs), distribution utilities, and members of financial institutions. The results of the studies commissioned by DOE were further studied by PSALM and its advisors, taking into consideration the feedback gathered from the consultations and the assessment made on market revenues and fuel costs of IPPAs based on the result of PSALM's trading operations since June 2006. The final scheme adopted is the use of a back to back contract between PSALM and the appointed IPPA that mirrors the applicable provisions of the original agreements between the IPP and NPC.

The first wave of the appointment of IPPAs covers the management and control of contracted energy of the Sual and Pagbilao Coal-Fired Thermal

Power Plants, as approved by the Joint PSALM-NPC Boards on 07 November 2008. The choice of the Sual and Pagbilao plants was based on their having the least complex ECAs, which will result in relieving the government the burden of procuring fuel (coal and oil) using the ownership approach. This should bring private sector efficiency in procurement activities resulting in lower fuel costs for the IPP plants.

The combined contracted capacities of the Sual and Pagbilao plants is 1,700 MW, constituting around 40% of the required contracted capacities that need to be privatized.

The IPPA process gives successful bidders a way to enter the Wholesale Electricity Spot Market (WESM) for a very low capital outlay. The Sual and Pagbilao structure, for example, enables bidders to pay the monthly fees, both for the opportunity to trade, and the payments for the physical assets, out of cashflow. Thus, no upfront financing is required.

This is a unique way to enter the WESM. The assets are relatively new, high quality plants that were built and are well maintained by some of the best IPP developers in the world. The IPPAs will have most of the benefits of being owners of generating stations, such as controlling the fuel and its dispatch, trading, and contracting of the plant, but without maintenance cost or capital upgrades.

Also, many of the risks of owning a plant are explicitly managed through the contract. If there is an extended outage, for example, there is up to a 90% discount on the monthly fees, while PSALM continues to bear Force Majeure risks.

The IPPA will be selected through an open and competitive bidding process using the two (2) envelope system. The 1<sup>st</sup> envelope will contain the legal documentation and the 2<sup>nd</sup> envelope is to contain the financial bid.

Among the tasks that the appointed IPPAs will handle are:

- Unfettered ability to trade the IPP energy output in the WESM.
- Unfettered ability to procure their fuel requirements (coal plants only).
- Guaranteed revenues for the first few years through the assignment of Transition Supply Contracts (TSCs) (thermal plants only).
- Freedom to enter into bilateral contracts and seek other markets for the balance of their contracted capacities and energy.
- Freedom to enter into other forms of financial hedging instruments if desired to manage their position in and exposure to the market.

## **Wholesale Electricity Spot Market (WESM)**

The commercial operation of the WESM (26 June 2006) is one of the pre-conditions to retail competition and open access. Other conditions as required in the Implementing Rules and Regulations (IRR) of the EPIRA are the: (i) approval of the unbundling of the transmission and distribution charges; (ii) initial implementation of the Cross Subsidy Removal System; (iii) privatization of 70% of the total capacity of NPC plants in Luzon and the Visayas; and (iv) transfer of the management and control of at least 70% of the total energy output of power plants under contract with IPPs.

The WESM is initially a market for energy. Eventually, with the approval of the ERC, there will be a market for ancillary services for regulation, contingency reserve and dispatchable reserves.

Electricity is offered and traded in a 24 hour by 7 days market. There are hourly prices published and used as basis for settlements. Prices in the spot market are volatile ranging from zero prices during off peak hours to as high as twelve pesos during peak hours. Distribution Utilities (DUs), Electric Cooperatives (ECs) and Suppliers/Aggregators can source their electricity requirements from the spot market or through Transition Supply Contracts (TSCs) with NPC. There is a provision in the EPIRA where DUs must source at least 10% of its requirements from the spot market.

In parallel to the spot market, DUs, ECs and Suppliers can enter into Transition Supply Contracts (TSCs) with NPC. These contracts can have predetermined rates such as the NPC Grid Rate or Time of Use (TOU) rates (plus other charges as approved by the ERC) that eliminate the volatility if one will source from the spot market.

On the demand side of the spot market, MERALCO is the biggest customer of the WESM. There are electric cooperatives such as Camarines Sur Electric Cooperative (CASURECO) and Ilocos Norte Electric Cooperative (INEC) which have registered as market participants in the WESM.

## **National Transmission Corporation (TransCo)**

The creation of TransCo under the EPIRA as a GOCC that will take ownership of the transmission assets of NPC and assume responsibility for the planning, construction and centralized operation and maintenance of its high voltage transmission facilities (the Grid), including grid interconnections and ancillary services, was meant to separate the power transmission system from the power generation system. TransCo was also mandated to privatize sub-transmission assets transferred from NPC by selling these assets to qualified distribution utilities. As provided in the

EPIRA, TransCo is wholly-owned by PSALM and, like the generation assets, is also subject to privatization.

TransCo started operations as a functional unit in charge of transmission functions of NPC. TransCo started independent operations in March 2003, although its operations continued to be carried in NPC's books of accounts. On 31 December 2008, TransCo's books were separated from the books of NPC.

Based on the government's Privatization Plan, PSALM shall privatize the transmission assets by way of the award of a Concession to a qualified bidder in an open and competitive bidding process.

The concession contract was awarded to the consortium of Monte Oro Grid Corporation, Inc. as the winning bidder in the fourth round of bidding for the TransCo concession contract held on 12 December 2007. The consortium, composed of Monte Oro Grid Resources Corp., Calaca High Power Corp. and State Grid Corp. of China, won with their bid price of US\$3.95 billion. The consortium established the National Grid Corporation of the Philippines (NGCP) as the "Concessionaire."

On 28 February 2008, the Concession Agreement became effective. Republic Act No. 9511 (The TransCo Franchise Law) was enacted on 01 December 2008 and became effective on 20 December 2008. The operation and management of the transmission business by NGCP commenced on 15 January 2009, upon receipt by PSALM of 25% of the concession fee as upfront payment (Commencement Fee). The balance of the concession fee will be paid by the Concessionaire with interest in semi-annual installments for 20 years.

### **Taxes**

Unlike the NPC whose Charter provides that NPC shall be exempt from direct and indirect taxes, the EPIRA (the law that created PSALM) does not contain a provision that exempts PSALM, as an entity, from taxation.

While PSALM as an entity is not per se tax-free, there are certain transactions of PSALM which are exempt from taxation. The tax treatment of PSALM's transactions is set forth in BIR Ruling No. 020-02 dated 13 May 2002, the pertinent provisions of which are summarized as follows:

- a) Income of PSALM arises from the exercise of essential government function and, thus, exempt from tax.

Under Section 32(B)(7)(b) of the Tax Code of 1997, income derived from the exercise of any essential government function accruing to the Government of the Philippines is excluded from gross income. The defined activities of PSALM under Section 50 of EPIRA are essentially governmental functions.

- b) Gain from the sale by PSALM of the generation facilities to qualified buyers is not subject to income tax.

Such income is considered income from the exercise of essential government function and thus, exempt from income tax pursuant to Sec. 32(B)(7)(b) of the Tax Code.

- c) Privatization of assets by PSALM is not subject to VAT.

The sale or disposition by PSALM of NPC assets is completely not related with the original business of NPC as a power generation company, which function is now being assumed by PSALM, and neither is it incidental thereto. Moreover, the disposition or sale of NPC assets are isolated transactions, therefore, not subject to VAT (BIR Ruling No. 113-98 dated 23 July 1998).

- d) The collection of universal charge by PSALM will not be considered as taxable income nor will it form part of its gross receipts for VAT purposes.

The universal charge received by PSALM is not subject to income tax since it is not in the nature of income as defined in Sec. 32(A) of the Tax Code and Section 36, Revenue Regulations No. 2, otherwise known as the Income Tax Regulations.

- e) Interest arising from NPC loans transferred to PSALM is exempt from income tax.

The exemption in the NPC Charter is granted not to NPC but on the loans, credits and indebtedness as well as on the payment of principal, interest and other charges ( Section 8 of RA No. 6395, NPC Charter).

- f) Interest income from loans entered into by PSALM shall be taxable, unless they are in connection with loans extended by (i) foreign governments, (ii) financing institutions owned or controlled or enjoying financing from foreign governments, and (iii) international or regional financial institutions established by foreign governments (Sec. 32(B)(7) (a), 1997 Tax Code).

- g) Interest income arising from foreign commercial loans is exempt from income tax pursuant to any of the tax treaties that the Philippines has with other country.

Under certain tax treaties, interest arising from commercial loans may be exempt from income tax, subject to compliance of the conditions provided in the treaty.

In 2005, RA 9337 or the R-VAT law was enacted. RA 9337 imposed 12% Value-added tax (VAT) on the sale of electricity, except for the sale of electricity sourced from renewable resources such as but not limited to biomass, solar, wind, hydropower, geothermal, ocean energy and other emerging energy resources, which is subject to zero 0% rate VAT. Thus, the sale by PSALM of generated power shall be subject to VAT at 12% or 0% rate as may be applicable.

## **KEY ACCOMPLISHMENTS**

In pursuit of its mandate set forth in the EPIRA, PSALM accomplished the following in 2008:

### **I. Asset Management**

#### Privatization of Generation Assets

In 2008 PSALM successfully bid out six (6) generation plants, most of which were sold in packaged combinations, like the Tiwi-Makban Geothermal Plants with a combined capacity of 747.5 MW and the Panay I & III and Bohol Diesel Plants with a combined capacity of 168.5 MW, while the 0.8 MW Amlan Hydroelectric Plant was sold solo. The Tiwi-Makban Plants were sold to AP Renewables, Inc., the Panay I & III and Bohol Plants were sold to SPC Power Corporation, and the Amlan Plant was sold to ICS Renewables, Inc.

The privatization of the six plants generated US\$455.48 million in expected proceeds. As of 31 December 2008, a total of eighteen (18) generation plants with a total capacity of 2,772.33 MW have been sold with a total bid price of US\$ 3.059 billion.

The successful bidding of the six generation plants brings the privatization level from 49% in 2007 to 73% in 2008, which partly satisfies the requirements for Open Access and Retail Competition.

Late in January 2009, the winning bidder for the 600 MW Calaca Coal-Fired Thermal Power Plant, Emerald Energy Corporation, terminated the Asset Purchase Agreement for the plant due to what it observed as the

“deterioration” of the plant’s condition since the bid date. The bidding was held last 6 October 2007 on an “as is, where is” basis. With the failed sale of the Calaca Plant, the level of privatization achieved will drop to 57%. Despite this turn of events, PSALM remains committed to achieving its goal of 100% privatization of the generation assets. Last 8 July 2009, PSALM has awarded the sale of Calaca to DMCI Holdings, Inc. as the winning negotiating party.

### Decommissioned Plants

On 25 April 2008 PSALM negotiated with Gagasan Steel Inc. the sale of one decommissioned plant, the 200 MW Manila Thermal Power Plant, following three rounds of failed biddings, for US\$2.506 million. Gagasan Steel Inc. was the only bidder who passed the technical qualifications in the third round of bidding but its bid fell short of the reserve price. The sale does not include the underlying land.

### Transmission Assets

The transmission assets were privatized by way of the award of a Concession contract to the National Grid Corporation of the Philippines. The Concession commenced on 15 January 2009, upon payment of 25% of the Concession Fee as Commencement Fee.

## **II. Liability Management**

### Loan Repayment

In 20 June 2007, PSALM secured Board approval of the Liability Management Program Phase-1(LMP-1). The LMP-1 aims to prepay US\$2.4 billion of NPC debt utilizing the privatization proceeds and the refinancing proceeds to achieve the following objectives: (i) liquidate debt from the privatization proceeds; (ii) manage liquidity risks and improve the debt service coverage ratio (DSCR) for the years 2009-2011; (iii) reduce foreign currency exposure of NPC debt from 90.75% to at least 50%; and, (iv) realize foreign exchange mark-to-market gains from 2004 to 2007.

Since NPC’s revenues are in peso and almost 88% of its debts are in foreign currency, forex losses incurred during the years after the Asian financial crisis significantly accounted for the increase in the cost of debt. Re-denominating NPC’s foreign denominated debts through this prepayment program effectively reduces the volatility of NPC/PSALM’s cash flows brought about by forex rate fluctuations.

The prepayment program of PSALM was targeted for full implementation within the years 2008-2009 to take advantage of the peso’s strong

showing beginning the second half of 2007. From March to September 2008, a total of US\$1.3 billion of NPC's mostly yen-denominated obligations have been prepaid:

- *March 2008:* Three yen-denominated loans of NPC with the Japan Bank for International Cooperation-OECF (JBIC-OECF) worth ¥16.887 billion, or around US\$174 million, were prepaid. These loans were extended to NPC in 1995 and 1997 to finance a number of transmission projects.
- *June 2008:* PSALM prepaid ¥49.5 billion, or around US\$458.5 million, OECF (Overseas Economic Cooperation Fund) relent loans to NPC by the national government and ¥27.2 billion, or around US\$263 million, representing Tranche B of the Miyazawa yen-denominated loans extended in 1999 by the Japanese government to NPC to finance a number of transmission projects.
- *August & September 2008:* PSALM prepaid US\$403 million of NPC's debt. The amount represents the loans extended by the Asian Development Bank and the Japan Bank for International Cooperation (JBIC) to NPC for the Masinloc Coal-Fired Thermal Project.

The loan prepayments helped reduce the country's debt burden, improved PSALM/NPC's liability profile by reducing NPC's aggregate debts from US\$7.01 billion as of end 2007 to US\$5.8 billion as of September 2008, and decreased its exposure to foreign currency risks, especially to the volatility of the Yen, with the 4% reduction in NPC's foreign debts. It likewise enabled PSALM/NPC to save a total of US\$371.57 million on interest and guarantee fee payments and on foreign exchange currency by prepaying the loans at a lower USD-JPY exchange rate. The prepayments also rendered unnecessary the condition precedent of creditor consent to the prepaid loans in the privatization of the remaining NPC generation assets and of TransCo.

However, towards the last quarter of 2008, PSALM decided to terminate the prepayment program under LMP-1 and reserved the cash in light of the credit crisis. Furthermore, NPC's cash position posted a shortfall in the last quarter of 2008, requiring PSALM to utilize privatization proceeds for debt servicing. Additionally, NPC's shortfall prompted PSALM to avail of a six-month ₱ 20 billion loan facility on 11 December 2008 with the Land Bank of the Philippines and the Development Bank of the Philippines.

As a consequence of the bankruptcy of Lehman Brothers Holdings, Inc. (LBHI), the primary credit support provider of Lehman Brothers Special

Financing, Inc. (LBSFI), on 15 September 2008, the Joint NPC/PSALM Boards authorized the termination proceedings with LBSFI, one of the counterparties of NPC/PSALM in the US\$ 300 million principal-only-swap (POS) transaction executed on 18 July 2007. Furthermore, the Joint Board authorized the execution and negotiation of a replacement swap that mirrors the terminated LBSFI POS. Consequently, on 7 November 2008, a US\$ 100 million replacement swap was successfully executed with a prepayment option executable on 15 November 2009.

### Debt Servicing

With the implementation of the final asset and debt accounts transfer from NPC to PSALM in October 2008, PSALM assumed the payment of principal and interest of NPC's regular debt service. In addition, PSALM also paid NPC's IPP obligations beginning the second half of 2008 due to NPC's cash flow deficit for the period.

### Management of Privatization Proceeds

With the winning bid price of US\$3.95 billion for the TransCo concession, privatization efforts are expected to yield US\$7.111 billion.

PSALM started receiving privatization proceeds from the sale of NPC generating plants in January 2005. As of 31 December 2008, actual dollar proceeds collected amounted to US\$1.901 billion while peso privatization proceeds collected totaled ₱172.9 million.

On 20 June 2007, the joint Boards of PSALM and NPC under Board Resolution No. 07-29, approved the utilization of the privatization proceeds to liquidate principal and interest obligations of NPC as they fall due. This was amended last 4 October 2007 by Board Resolution No. 07-61, which granted authority to PSALM Management to utilize the privatization proceeds to:

- Prepay NPC's principal obligations,
- Settle NPC's principal and interest obligations as they become due only after NPC shows deficit in its cash flow after utilization of its own internally generated cash,
- Manage NPC's liabilities with the objectives of reducing interest cost and liquidity risk in 2009-2011 and hedging foreign exchange risks at terms and conditions advantageous to the government, and
- Pay other financial obligations of NPC.

From 22 August 2007 to 31 December 2008, a total of US\$1.871 billion dollar proceeds and ₱2.303 billion peso proceeds were utilized to cover

mostly the financial obligations of NPC such as its maturing obligations, IPP obligations and the prepayment of more expensive Yen-denominated obligations, as well as other privatization-related expenditures.

As of 31 December 2008, the balance of dollar proceeds is US\$30.118 million while the balance of the peso proceeds is ₱805.667 million.

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## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### **Basis of Preparation of Financial Statements**

The financial statements are prepared on a historical cost basis and transactions are recorded using the accrual basis of accounting. The assets transferred from NPC were recorded at their carrying amounts (balances as reflected in NPC books) as of the transfer date of 31 December 2008.

The preparation of the financial statements in accordance with Philippine Accounting Standards requires the Company to make estimates and assumptions that affect the reported amounts of resources, liabilities, income and expenses and the disclosures of contingent resources and liabilities. Future events may occur which can cause the assumptions used in arriving at the estimates to change. The effects of any change in estimates are reflected in the financial statements as they become reasonably probable.

Estimates and judgments are continually evaluated and are based on historical experiences and other factors including expectations of future events that are believed to be reasonable under the circumstances.

Due to the asset-debt transfer from NPC to PSALM, comparative figures in the financial statements show significant variances.

### **Cash Equivalents**

Cash equivalents consist of short-term placements/time deposits which are highly liquid investments with a maturity of three months or less from the date of acquisition and which are subject to insignificant risk of changes in value.

### **Inventories**

Inventories are valued at cost using the moving-average method and consist only of office supplies.

### **Non-Current Assets Held for Sale**

Non-current assets held for sale consist of generation plants in service and decommissioned plants that are scheduled for privatization in 2009. The account also include those plants that have been previously bid out but whose sale were not consummated by end of 2008, either because the bidding was declared a failure or because the winning bidder failed to close the sale, but which are still intended to be sold in 2009.

Under Philippine Financial Reporting Standard (PFRS) 5, *Non-current Assets Held for Sale*, a non-current asset is classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale that should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell, the carrying amount being the amount reflected in the NPC books at the date of transfer.

### **Build-Operate-Transfer (BOT) Plants**

Total capacity fees for the duration of the cooperation period are capitalized and recognized as asset under BOT Electric Plants under Capital Lease account. A liability corresponding to the capital recovery fees is set up under BOT Lease Obligation. BOT assets are amortized over 20 years, except for Hopewell Pagbilao which is amortized over 29 years.

### **Property, Plant and Equipment and Depreciation**

#### *NPC-transferred assets*

Property, plant, and equipment transferred from NPC include electrification, power and energy structures and referred to as utility plants. The last external revaluation of these plants was of the 1996 asset prices. These structures are carried in PSALM's books at their carrying amounts as of the transfer date of 31 December 2008. While these assets were carried in NPC books, regular annual maintenance, repairs and minor replacements were charged to expense as they were incurred,

whereas major maintenance, which was done on periodic three-to five-year intervals, was deferred, amortized and charged to operations over the number of years interval. Rehabilitation expenditures that would result in improvement of the plant's efficiency beyond five years were capitalized and transferred to plant cost upon completion of work orders.

Depreciation was charged from the date of acquisition of the fixed assets or after the completion of works and computed on a straight-line basis. Depletion which shows the periodic provision for the depletion of extractable natural resources such as steam, natural gas, etc. was also computed on a straight-line basis. Three-month depreciation was recognized on NPC transferred assets.

Transferred utility plants	Remaining life ranging from 2 to 20 years
Transferred non-utility plants	Remaining life ranging from 0 to 4 years

*PSALM-acquired*

Property and equipment consisting of computers, office furniture and fixtures, vehicles and communication equipment are stated at cost less accumulated depreciation and any impairment in value. The stated cost comprises its purchase price and directly attributable costs of bringing the asset to working condition for its intended use. Generally, tangible assets that are expected to be used for more than one year are considered as capital assets. Expenditures for repairs and maintenance are charged to expense as incurred.

Depreciation is computed on a straight-line basis over the useful lives of the assets as follows:

Furniture, fixtures and equipment	5 – 10 years
Transportation equipment	7 years
Computers and accessories	5 years

Residual value equivalent to ten percent (10%) of the acquisition cost is deducted before dividing the same by the estimated useful life.

The carrying values of property and equipment are reviewed for impairment when changes in circumstances indicate that the carrying value may not be recoverable or may have diminished. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount and impairment losses are recognized in the statement of income and expenses.

### **Assumed REP Loans**

Loans by Electric cooperatives (ECs) from the National Electrification Administration (NEA) which were incurred for the purpose of financing the Rural Electrification Program and which were assumed by PSALM were charged to a deferred asset account "Assumed Rural Electrification Program Loans" and subjected to amortization. This deferred asset account increases as PSALM assumes additional loans of ECs from other government agencies (OGA) and local government units (LGUs). The amortization expense is computed based on a straight-line, 10-year amortization of the total assumed NEA loans and a straight-line amortization of the OGA and LGU loans over the remaining balance of the 10-year period, beginning from the year the OGA and LGU loans were assumed.

### **Taxes**

Taxes for current and prior periods are, to the extent unpaid, recognized as a liability. If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess payment is recognized as an asset.

### **Bonds Payable**

Bonds payable are presented net of unamortized discount and are revalued at year-end to reflect Philippine peso exchange rate prevailing as of the balance sheet date.

### **Revenue Recognition**

Revenue/gain from sale of the generation plants is recognized upon perfection of sale, when PSALM receives the full payment, or the upfront cash payment, in case of installment sale. Other revenues are recognized when it is probable that future economic benefits will be received and such future benefits can be measured reliably.

### **Foreign Currency Transactions**

The accounting records of the Company are maintained in Philippine pesos. Transactions denominated in foreign currencies are translated into Philippine pesos at exchange rates prevailing on the transaction dates in accordance with PAS 21, *The Effects of Changes in Foreign Exchange Rates*, which requires that foreign currency transactions shall be recorded on initial recognition in the functional currency by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of transaction.

The Company translates its foreign currency-denominated deposits and loans at year-end rates in accordance with PAS 21, which requires foreign currency monetary items to be translated at balance sheet date using the closing rate. The resulting gains and losses from the exchange differences are recognized in the statement of income and expenses.

Year-end foreign currency exchange rates follow:

	<b>2008</b>	2007
Philippine Peso (₱) : US Dollar (\$)	<b>47.4850</b>	41.4010
Philippine Peso (₱) : Japanese Yen (¥)	<b>0.5221</b>	0.3642
Philippine Peso (₱) : Korean Won (KRW)	<b>0.0357</b>	0.0441
Philippine Peso (₱) : Euro (EUR)	<b>66.2463</b>	60.5572

### **3. CASH AND CASH EQUIVALENTS**

This account consists of the following:

	<b>2008</b>	2007
Cash on hand and in banks	<b>8,517,775,380</b>	39,112,204
Cash equivalents – Privatization proceeds	<b>3,260,352,693</b>	21,926,498,398
– Others	<b>3,460,970,071</b>	7,475,385,012
	<b>15,239,098,144</b>	29,440,995,614

The increase in *Cash on hand and in banks* was due largely to the ₱8 billion balance of the ₱20 billion bridge financing secured from the Land Bank of the Philippines (LBP) and the Development Bank of the Philippines (DBP).

*Cash equivalents* include the short-term placement of the proceeds from the sale of generation plants with the Bangko Sentral ng Pilipinas (BSP), LBP and DBP and short-term time deposits of regular funds.

### **4. POWER RECEIVABLES**

This account is composed of receivables from the following entities:

	Total	Current	Non-current
Utilities	55,201,243,406		
Cooperatives	13,195,757,481		
Industries	6,015,997,774		
Government	5,269,117,790		
PEMC	8,520,353,500		

Others	2,296,920,188		
	90,499,390,139		
Refunds	(20,969,621,752)		
	69,529,768,387	68,483,094,289	1,046,674,098
Allowance for bad debts	(10,981,380,518)	(10,459,396,853)	(521,983,665)
	58,548,387,869	58,023,697,436	524,690,433

*Power receivables* consist of the trade collectibles for the power generation charges, including ancillary service charges, universal charges and restructured power receivables, net of refunds to power customers as a result of ERC decisions.

*Refunds* are billing adjustments (in the form of reduction in future power bills) arising from the ERC Orders.

The recognition of the refunds was based on the following Deferred Accounting Adjustments (DAAs), which were approved by the ERC in accordance with the existing Generation Rate Adjustment Mechanism (GRAM) and Incremental Currency Exchange Rate Adjustment (ICERA) Guidelines dated February 24, 2003:

**SUMMARY OF ERC ORDERS/DECISIONS**

ERC Case No.	Filings	Period Covered/Test Period	Date Applied	Date of ERC Approval	Status	Amount in Pesos
<b>GRAM</b>						
<b>LUZON</b>						
2008-031 RC	9th GRAM	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	(6,109,623,368)
2008-042 RC	10th GRAM	January 2007 to December 2007 January 2008 to April 2008	29-Jul-08	15-Dec-08	P.A.	(4,182,302,185) (378,653,796)
2008-053 RC	11th GRAM	May 2008 to June 2008	25-Sep-08	15-Dec-08	P.A.	1,398,841,914
2008-063 RC	12th GRAM	July 2008 to September 2008	16-Dec-08	19-Jan-09	P.A.	2,905,422,964
<b>VISAYAS</b>						
2008-031 RC	9th GRAM	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	537,507,535
<b>MINDANAO</b>						
2008-031 RC	9th GRAM	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	2,709,234,892
<b>ICERA</b>						
<b>LUZON</b>						
2008-032 RC	8th ICERA	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	(1,981,640,116)
2008-043 RC	9th ICERA	January 2007 to December 2007 January 2008 to April 2008	29-Jul-08	15-Dec-08	P.A.	(9,390,808,305) (2,955,459,834)
2008-054 RC	10th ICERA	May 2008 to June 2008	25-Sep-08	15-Dec-08	P.A.	(1,839,170,751)
2008-064 RC	11th ICERA	July 2008 to September 2008	16-Dec-08	19-Jan-09	P.A.	(939,063,474)
<b>VISAYAS</b>						
2008-032 RC	8th ICERA	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	427,801,687
<b>MINDANAO</b>						
2008-032 RC	8th ICERA	July 2006 to December 2006	3-Jun-08	15-Dec-08	Decision	(16,920,093)

In the Order dated 15 December 2008 for the 10<sup>th</sup> GRAM and 9<sup>th</sup> ICERA, the ERC effectively amended the 9<sup>th</sup> GRAM and 8<sup>th</sup> ICERA Decisions when it revised the recoverable amount for the Luzon Grid as follows:

	From	To
9 <sup>th</sup> GRAM	(6,109,623,368)	(8,313,052,371)
8 <sup>th</sup> ICERA	(1,981,640,116)	(1,594,328,682)

A Motion for Reconsideration was filed with the ERC to reconsider its position and to issue an Order containing the revised GRAM and ICERA DAA balances.

The approved amount (whether a refund or a recovery) is being monitored on a monthly basis by multiplying the approved rate per kWh by the sales volume for the month. The monthly resulting amounts are tracked until its total equals the approved amount. As of June 2009, the remaining balance of the amount approved for refund is ₱8.811 billion: GRAM, ₱0.693 million and ICERA ₱8.118 billion.

*Power receivables - utilities* consist substantially of receivables from Meralco of ₱36.079 billion representing penalty on below contracted demand/energy for the period covering 2001 to 2004 which Meralco deducted from its power bill payments to NPC. This resulted in a dispute between the parties. In February 2002, the parties entered into negotiation to settle the dispute and on July 2003, signed a Settlement Agreement. The Agreement is still pending with Energy Regulatory Commission for its approval.

Under the Settlement Agreement, Meralco agrees to pay the NPC the amount of ₱27.515 billion, while NPC agrees to credit Meralco for ₱7.465 billion. The amount will be paid by Meralco over a five to six-year period to minimize the impact to consumers as purchased power cost is a pass-through to customers.

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## 5. ASSET SALE RECEIVABLE

*Asset sale receivable* represents the balance of the sales price of US\$ 129 million (₱6.338 billion) on the sale of the 112 MW Pantabangan-Masiway Hydro-electric Power Plant complex to the First Generation Hydro Power Corporation (First Gen). The sales price is payable by First Gen as follows: 40% cash upfront and the 60% balance payable in 14 equal semi-annual payments with an interest of 12% per annum starting 17 May 2007. Amounts falling due in May and November of the succeeding year are presented separately in the current assets. Details follow:

	2008	2007
Asset sale receivable	<b>2,910,259,468</b>	2,932,714,104
Less non-current portion	<b>2,455,420,854</b>	2,537,383,432
Current portion	<b>454,838,614</b>	395,330,672

## 6. OTHER RECEIVABLES

The following comprise this account:

	2008	2007
Due from NGAs	50,414,311,729	38,945,811
Due from GOCCs	9,624,513,512	5,197,223,472
Interest receivable	6,136,906,306	106,154,283
Due from officers & employees	963,964	2,259,339
Other receivables, net	2,633,078,031	-
	<b>68,809,773,542</b>	<b>5,344,582,905</b>

*Due from the national government agencies* (NGAs) includes claims from the following:

	2008	2007
San Roque Multi-purpose Project	24,237,729,197	-
Bureau of Internal Revenue	22,018,482,651	38,945,811
National government	4,077,091,491	-
Department of National Defense	22,712,634	-
Others	58,295,756	-
	<b>50,414,311,729</b>	<b>38,945,811</b>

### San Roque Multi-Purpose Project

The P24.237 billion advanced by NPC to the San Roque Multi-Purpose Project (SRMP) arose from the Memorandum of Agreement (MOA) in 1998 by and between the Department of Finance (DOF), Department of Budget and Management (DBM), Department of Environment and Natural Resources (DENR), Department of Public Works and Highways (DPWH), National Irrigation Administration (NIA), and NPC.

San Roque is a power project of NPC approved by the National Economic Development Authority (NEDA) as one of the projects for development by the Government. San Roque is located in San Manuel, at the lower Agno River in Pangasinan. The project was bid out by NPC on a Build-Operate-Transfer (BOT) basis which gave rise to a Power Purchase Agreement (PPA) between NPC and the Consortium (Marubeni Corporation, Sithe Philippine Holdings, Ltd., and Italian Thai Development Public Company, Limited). As signatory to this PPA, NPC becomes responsible for the disbursement of the cost of the non-power component of the Project estimated at \$400 million.

SRMP is the non-power component of the project. It is a project serving several purposes: (i) annual generation of 1000 GWh energy; (ii) irrigation

of about 87,000 hectares service areas in Pangasinan; (iii) flood forecasting and control; and (iv) water quality and environmental protection. As the project encompasses several functional areas, its implementation was a multi-agency effort with NPC tasked to lead in the project development. To ensure that the agencies meet their obligations in the implementation of the project and the terms of the PPA, the agencies entered into the MOA.

The MOA provided, among others, that:

1. DOF shall (i) secure the financing of the \$400 million for disbursement to the Consortium through NPC, (ii) ensure the timely transfer of the \$400 million fund to NPC, and (iii) ensure that the advances to be made by NPC for SMRP non-power component shall not be offset against any receivables of the Government from NPC;
2. NIA, DENR, DPWH shall (i) include SRMP as a priority project in their programs, (ii) cause the inclusion in their annual budget, over and above its ceiling, their share in the \$400 million non-power cost, (iii) give authority to DBM and BTr to remit funds directly to NPC's account; (iv) coordinate with NPC and the Consortium in the implementation of Project matters under their jurisdiction;
3. DBM shall ensure the inclusion of each agency's contribution to SRMP, as defined in the MOA, in the agencies' respective annual budgets from 1999 to 2000;
4. NPC shall, among others, disburse to the Consortium the \$400 million non-power component funding in accordance with the schedule.

Certain amendments to the MOA were made in September 1998, major of which follow:

1. NPC to borrow for the \$400 million non-power component of the Project, with repayments to NPC made over the same debt service period as the said loan;
2. DOF shall secure the full government guarantee for the NPC financing of the \$400 million non-power cost component of SRMP;
3. Longer spread of the agency's budget allocation for the contribution to the \$400 million non-power component (from years 1999 to 2000 to years 1999 to 2014)

## Bureau of Internal Revenue

This account pertains to input tax of ₱11.151 billion and taxes paid under protest of ₱10.867 billion value added tax on sale of generation plants and final withholding taxes on interest expense paid to foreign creditors.

## National Government

The ₱4.077 billion represents NPC's advances for the preservation and maintenance of the mothballed Bataan Nuclear Power Plant.

*Due from government-owned and controlled corporations (GOCCs)* pertains mainly to PSALM's advances to NPC for regular debt service and settlement of IPP obligations which, together with the other receivable sub-accounts under this account, are still subject to reconciliation with NPC.

*Interest receivable* represents interest income accruing on short-term placements/time deposits with authorized government depository banks.

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## **7. NON-CURRENT ASSETS HELD FOR SALE**

This account represents the generation plants with a total carrying amount of ₱46.667 billion scheduled for privatization in 2009, including those that will be offered for sale again in view of their unsuccessful privatization in 2008. PSALM is set to dispose of the following generation plants, two of which represent packaged combinations – the Iligan I & II Diesel Power Plants and the Navotas I & II Gas Turbine Plants.

<i>Generating Plants</i>	Bid Schedule
ABB Bataan Combined Cycle 1 & 2	April 09
Power Barge 118 (Maco)	May 09
Iligan DPP (Alsons Tomen 1 & 2)	1 <sup>st</sup> sem 09
Naga Gas Turbine Land-based 1 & 2	April 09
Power Barge 117 (Nasipit)	April 09
Palinpinon GPP	June 09
Tongonan (Leyte) GPP	June 09
Bacon-Manito GPP	June 09
Angat HEPP	Sep 09
Hopewell Plant Energy (Navotas) 1 & 2	June 09
Batangas CFTPP 1 & 2	2009
<i>Decommissioned Plants</i>	
Talavera DPP (Cebu DPP 2)	Negotiated Jan 09

Bataan TPP 1 & 2	Feb 09
Aplaya DPP	May 09
Gen. Santos DPP	May 09
Sucat TPP 1, 2, 3, 4	Aug 09

The bidding process for the Iligan 1 & 2 Diesel Power Plants was suspended by the PSALM Board on 23 March 2009 due to concerns over the legitimacy of the title over the assets that NPC can transfer to PSALM and which PSALM can subsequently privatize.

The Iligan 1 & 2 Diesel Power Plants were former Build-Operate-Transfer (BOT) plants owned by the Northern Mindanao Power Corporation (NMPC). Part of the BOT agreements for both plants, known then as NMPC 1 and NMPC 2 plants, provided that NPC shall be responsible for the payment of all real estate taxes and assessments, rates and other charges in respect of the site and the buildings and improvements. NPC complied by paying the real property taxes assessed by the Iligan City Government on NMPC 1 & 2 until the first quarter of 2003.

After the turn-over of NMPC on August 1, 2003, NPC contested the Iligan City Treasurer's assessment on NMPC 1 & 2 on the ground that the machineries and equipment of NMPC 1 & 2, which are actually, directly and exclusively used by NPC for power generation, should have been exempted from real property taxes pursuant to Section 234 (c) of the Local Government Code. NPC likewise sought the reassessment of the lands, buildings and other improvements of NMPC 1 & 2 which were erroneously assessed by the City of Iligan at 35% instead of at 10% as Special Classes of Real Property pursuant to Section 216 and 218 (d) of the Local Government Code.

The City Treasurer denied NPC's protest on the ground that NMPC 1 & 2 are not owned by NPC but by NMPC, which is a private entity. On 8 March 2004, NPC appealed to the Local Board of Assessment Appeals (LBAA), which denied the appeal in its decision dated 2 June 2004. NPC appealed the LBAA decision to the Central Board of Assessment Appeals (CBAA) on 9 July 2004, which appeal was dismissed per its decision dated 20 December 2006.

On 8 February 2006, NMPC 2 was turned-over to NPC.

On 2 April 2007, the City Government issued the warrants of levy for the two plants and sold both plants at auction. On 25 April 2007, because there was no bidder for the assets, title to the assets passed to the City Government. On 7 May 2007, the CBAA, acting on NPC's motion for reconsideration, issued a cease and desist order to the City Government.

The City Government filed a motion for reconsideration, to which NPC filed its opposition. Both motions are still pending with the CBAA.

To settle the issue on the correct tax liability of NPC and to avoid continuously litigating over the legality of the auction of the two plants by the City Government, NPC proposed a Memorandum of Agreement (MOA) on 12 December 2007. On 18 February 2008, the draft MOA was rejected by the City Government, which reiterated its claim for the unpaid RPT notwithstanding the turn-over of the two Iligan plants from NMPC to NPC.

NPC has contested the auction sale of the two plants before the Regional Trial Court. In January 2009, NPC again failed to reach a settlement with the City Government. Under these circumstances, bidding out the Iligan power plants would make PSALM vulnerable to legal action by the City Government and the bidders; hence, the PSALM Board decided to suspend the process.

To date, four of the generating and four of the decommissioned plants have been marketed by PSALM thru negotiated sale, as shown in Note 26.

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## 8. OTHER CURRENT ASSETS

This account consists of the following:

	2008	2007
Cash and cash equivalents	6,522,821,772	-
Materials, supplies, & equipment	16,132,352,415	-
Due from officers & employees	62,029,760	-
Assets in trust with NPC	22,717,203,947	-
Guaranty/court deposits and cash advances	707,764,552	1,750,987
Prepaid rent & inventory	5,718,658	5,304,917
	<b>23,430,687,157</b>	7,055,904

*Assets in trust with NPC* represent current assets held by NPC as part of its working capital as “Operator” under the Operations and Management Agreement with PSALM.

*Guaranty deposits* include the marginal and guaranty deposits for Letters of Credit and for the Nomura bonds issuances.

## 9. PROPERTY, PLANT AND EQUIPMENT

*Property, plant and equipment* account consists of PSALM-acquired and NPC-transferred property, plant and equipment as follows:

PSALM –acquired:

	Furniture, Fixtures/ Equipment	Transportation Equipment	Total
<i>COST</i>			
1 January 2008	135,291,350	13,154,968	148,446,318
Additions/Adjustments	8,135,594	-	8,135,594
31 Dec 2008	143,426,944	13,154,968	156,581,911
<i>ACCUM DEPRECIATION</i>			
1 January 2008	71,889,540	5,144,859	77,034,399
Provision/Adjustment	12,149,767	1,743,103	13,892,870
31 December 2008	84,039,307	6,887,962	90,927,269
<b>Carrying amount</b>			
<b>31 December 2008</b>	<b>59,387,637</b>	<b>6,267,006</b>	<b>65,654,643</b>
Carrying amount			
31 December 2007	63,401,810	8,010,109	71,411,919

NPC—transferred assets:

*Utility Plants*  
(In million pesos)

	Land / Landholdings	Hydraulic Production Plant	Steam Production Plant	Other Production Plant	Transmission Plant	Other Utility Plant	Total
<i>Cost</i>							
1 January 2008	-	-	-	-	-	-	-
Transfers from NPC	6,701	18,872	4,284	382	1,048	1,512	32,799
31 December 2008	6,701	18,872	4,284	382	1,048	1,512	32,799
<i>Accumulated Depreciation</i>							
1 January 2008	-	-	-	-	-	-	-
Depreciation, Oct-Dec 2008	-	275	193	50	22	4	544
31 December 2008	-	275	193	50	22	4	544
<b>Carrying amount</b>							
<b>31 December 2008</b>	<b>6,701</b>	<b>18,597</b>	<b>4,091</b>	<b>332</b>	<b>1,026</b>	<b>1,508</b>	<b>32,255</b>

### Non-utility plants

	Land / Landholdings	Non-Utility Plants	Total
<i>Cost</i>			
1 January 2008	-	-	-
Transfers from NPC	207,435,345	385,594,404	593,029,749
31 December 2008	207,435,345	385,594,404	593,029,749
<i>Accumulated Depreciation</i>			
1 January 2008	-	-	-
Depreciation, Oct-Dec 2008	-	312,969,000	312,969,000
31 December 2008	-	312,969,000	312,969,000
<b>Carrying Amount</b>			
<b>31 December 2008</b>	<b>207,435,345</b>	<b>72,625,404</b>	<b>280,060,749</b>

## 10. BOT ELECTRIC PLANTS UNDER CAPITAL LEASE

This account represents the total computed capacity fees of Build-Operate-Transfer (BOT) projects for the duration of the cooperation period, as follows:

Plant	Total capacity fees	Accumulated Depreciation	Net
Pagbilao I (350 Mw)	71,839,467,000	31,054,742,775	40,784,724,225
Pagbilao II (350 Mw)	71,839,467,000	30,632,327,419	41,207,139,581
Ilijan Nat Gas (1200 Mw)	107,387,216,364	28,157,390,011	79,229,826,353
CBK-Kalayaan 2 Unit 3 (177.5 Mw)	17,387,881,744	2,209,709,972	15,178,171,772
CBK-Kalayaan 2 Unit 4 (177.5 Mw)	17,387,881,744	2,209,709,972	15,178,171,772
Enron Subic (108 Mw)	12,883,027,751	8,673,356,606	4,209,671,145
Bauang (FFPC) (215 Mw)	16,190,349,336	11,535,623,902	4,654,725,434
Sn Roque Multi-Purpose Plant (345 Mw)	92,954,875,257	13,168,607,328	79,786,267,929
Sual I (500 Mw)	96,734,389,479	35,656,503,993	61,077,885,486
Sual II (500 Mw)	96,734,389,479	35,656,503,994	61,077,885,485
Bakun I (35 Mw)	24,500,769,930	9,494,048,348	15,006,721,582
Bakun II (35 Mw)	24,500,769,930	10,106,567,596	14,394,202,334
STEAG/Mindanao Coal Fired I (100 Mw)	13,738,656,531	1,252,210,641	12,486,445,890
STEAG/Mindanao Coal Fired 2 (100 Mw)	13,660,516,256	1,154,498,854	12,506,017,402
	<b>677,739,657,801</b>	<b>220,961,801,411</b>	<b>456,777,856,390</b>

The 108 MW Enron Subic Diesel Power Plant was formally turned over by NPC/PSALM to the Subic Bay Metropolitan Authority (SBMA) effective 23 February 2009 upon the expiration of the BOT Agreement between Subic Power Corporation and NPC and the Ground Lease Agreement (GLA) between NPC and SBMA.

The turn-over was in conformity with Opinion No. 238 s. 2008 dated 16 October 2008 issued by the Office of the Government Corporate Counsel (OGCC) which provided, among others, that:

- Ownership of the Subic Power Station will be transferred from ENRON to NPC at the end of the cooperation period under the BOT Agreement, and from NPC to SBMA at the termination of the GLA.
- The Subic Power Station is not subject to privatization under the EPIRA since it is not “disposable” property of NPC within the ambit of the law.

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#### **11. INVESTMENT IN TRANSCO**

This account represents the difference between the NPC assets and liabilities transferred to TransCo upon its separation from NPC and which represents PSALM’s equity investment in TransCo. As provided for in the EPIRA, TransCo is wholly-owned by PSALM which assumed the foreign loan obligations related to the transmission assets.

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#### **12. INVESTMENT IN BONDS**

This account represents PSALM’s investment in bonds issued by NPC as part of an On-Lending Agreement in 2002. Upon the completion of the asset-debt accounts transfer from NPC, this account and the corresponding liability in NPC’s books were closed.

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#### **13. ASSUMED RURAL ELECTRIFICATION PROGRAM (REP) LOANS**

Section 60 of the EPIRA provides that all outstanding financial obligations of the electric cooperatives (ECs) to NEA and other government agencies incurred for the purpose of financing the REP shall be assumed by PSALM in accordance with the program approved by the President of the Philippines within one (1) year from the effectivity of the Act which shall be implemented and completed within three (3) years from the effectivity of the Act. Section 2, Rule 31 of the Implementing Rules and Regulations of EPIRA states that the assumption covers all outstanding REP-related financial obligations of the ECs as of 26 June 2001.

The Act also provides that ERC shall ensure a reduction in the rates of ECs commensurate with the resulting savings due to the removal of the amortization payments of their loans. However, any EC which shall

transfer ownership or control of its assets, franchise or operations within five years shall repay PSALM the total debts including accrued interests thereon.

To carry out the aforementioned objective and that of Executive Order (EO) No. 119, Restructuring Program for Electric Cooperatives, PSALM and NEA entered into a Memorandum of Agreement (MOA) on 3 October 2003 to lay down the operational legal framework upon which the financial obligations of ECs to NEA shall be lawfully assumed by PSALM. Article IV of the MOA provides that repayment of the assumed loans shall be for the period of 10 years in accordance with the amortization schedule as may be mutually agreed by the parties.

The condonation was subject to compliance with certain conditions required under Executive Order (EO) No. 119. On 2 September 2006, EO 460 was issued amending EO 119 by giving retroactive effect to the effectivity of the assumption by PSALM of the rural electrification loan obligations of the ECs to NEA and other government agencies.

The total amount of ECs' obligations to NEA assumed by PSALM amounted to ₱17.978 billion. The obligations of ECs to local government units and other government agencies amounted to ₱0.096 billion, putting the total loans assumed to-date by PSALM at ₱18.074 billion. Of this amount, the following remains outstanding:

	<b>2008</b>	2007
Current portion	<b>2,936,245,026</b>	2,614,180,578
Non-current	<b>6,355,711,966</b>	8,400,186,849
<b>Total</b>	<b>9,291,956,992</b>	11,014,367,427

The amounts of ₱7.239 billion and ₱9.049 billion reflected under this account in the non-current assets represent the unamortized balance of the account as of 31 December 2008 and 2007, respectively.

#### **14. OTHER NON-CURRENT ASSETS**

Other non-current assets consist of the following:

	<b>2008</b>	2007
Stored energy	<b>34,685,325,157</b>	-
Deferred taxes and duties	<b>4,127,104,030</b>	-
Other non-current receivables, net	<b>3,060,575,843</b>	-
Universal charge (UC)	<b>1,428,726,949</b>	849,849,019
Various	<b>223,934,720</b>	104,341,345
	<b>43,525,666,699</b>	954,190,364

*Stored energy* represents the difference between the actual gas lifted by NPC versus the contracted volume per the Gas Supply and Purchase Agreement with Shell Philippines Exploration B. V. (SPEX).

*Deferred taxes and duties* pertain to the payments by NPC to BIR for specific taxes and to Bureau of Customs for customs duties for its purchase of petroleum products prior to the implementation of the R-VAT Law in 2005.

*Other non-current receivables* consist substantially of the ₱3.13 billion receivable from Metropolitan Waterworks and Sewerage System (MWSS) which have accumulated since 1992. The amount represents energy and capacity losses incurred by the Angat Hydroelectric Power Plant (AHEPP) due to the implementation of MWSS' Angat Water Supply Optimization Project (AWSOP). The Memorandum of Understanding between NPC and MWSS on 9 February 1990 provides that MWSS shall compensate NPC the energy and capacity losses, if any, which the latter may incur as a result of the operation of the former's Auxiliary Unit No. 5.

*Universal charge* refers to the charge imposed on all electricity end-users for various purposes as enumerated in Note 1. In May 2003, ERC approved the ₱0.0025/kWh for UC-watershed management. The UC for missionary electrification was first approved at ₱0.0168 kWh effective February 2003 and increased to ₱0.0373/kWh effective July 2003.

At year-end, the composition of UC fund is as follows:

	2008	2007
Special Trust Fund (STF)	889,125,235	357,755,392
Receivables	539,601,714	492,093,627
	<b>1,428,726,949</b>	<b>849,849,019</b>

Transactions affecting the UC are as follows (cumulative):

	2008	2007
Remittances by collecting entities (CEs):		
For missionary electrification	9,208,332,051	7,395,782,644
For watershed rehabilitation	620,453,600	499,157,625
Others (no identification of specific purpose)	226,080	2,811,552
	<b>9,829,011,731</b>	<b>7,897,751,821</b>
Interest earnings	122,156,626	103,039,242
	<b>9,951,168,357</b>	<b>8,000,791,063</b>
Disbursements to NPC	<b>(9,062,043,122)</b>	<b>(7,643,035,671)</b>
STF balance	889,125,235	357,755,392
Receivables from CEs	539,005,486	491,595,417
Interest receivable	596,228	498,210
	<b>1,428,726,949</b>	<b>849,849,019</b>

Disbursements to NPC of ₱9.062 billion represent disbursements for missionary electrification of ₱7.820 billion, watershed of ₱0.339 billion, and DAA for ICERA and GRAM of ₱0.903 billion. *Receivables from CEs* pertain to the difference between the reported billings of CEs versus their remittances to PSALM.

The same amount of UC is presented under Other Long-Term Liabilities in Note 18.

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## 15. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Below is the breakdown of the account:

	2008	2007
Accounts payable		
Accounts payable	35,233,150,627	54,384,932
Check vouchers payable	11,551,749,442	-
Fuel payables	3,115,749,093	-
Materials, supplies, equipment payables	860,828,295	-
Other payables	5,100,450,522	43,669,449
Interest payable	9,565,259,208	38,341,155
Guaranty deposits payable	508,695,660	19,722,211
Performance/bidders bonds	231,248,716	2,025,918
Due to officers & employees	58,205,320	51,623,663
	<b>66,225,336,883</b>	<b>209,767,328</b>

*Other payables* for 2008 consist of the following:

Guaranty fees payable	4,183,994,724
Financial assistance/benefits payable	883,482,654
Suppliers and contractors	29,529,332
Various	3,443,822
	<b>5,100,450,522</b>

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## 16. BOT LEASE OBLIGATION

This account pertains to the liability set up for capital cost recovery fees of the BOT power plants during the cooperation period indicated in the BOT contracts.

	2008	2007
Total lease obligation	<b>487,876,887,631</b>	-
Less current portion	<b>36,182,630,879</b>	-
Non-current	<b>451,694,256,752</b>	-

## 17. LONG-TERM LIABILITIES

This account consists of:

	2008	2007
Bonds payable	<b>214,733,927,376</b>	22,412,427,358
Loans payable	<b>86,124,001,305</b>	-
Other long-term liabilities	<b>35,968,531,360</b>	-
	<b>336,826,460,041</b>	-
Less bond discount	<b>(10,794,564,776)</b>	-
Net	<b>326,031,895,265</b>	22,412,427,358
Less current portion	<b>50,252,876,459</b>	-
Long-term	<b>275,779,018,807</b>	22,412,427,358

On a per bank/creditor basis, the amounts in 2008 are summarized as follows:

Deutsche Bank	71,227,500,000
Bank of New York/JP Morgan Chase Manhattan	54,082,775,000
Citibank	39,504,700,000
Bureau of Treasury	38,613,000,000
Department of Energy	28,297,252,592
Land Bank of the Phils./Development Bank of the Phils.	20,000,000,000
International Bank for Reconstruction and Development	14,089,134,555
Eximbank of Japan	12,896,683,445
US Bank	11,305,952,376
Bank of Tokyo-Mitsubishi UFJ	10,859,680,000
Asian Development Bank	10,499,244,261
Kreditanstalt fur Wiederaufbau	8,169,007,897
Overseas Economic Cooperation Fund	4,244,439,155
Japan Bank for International Cooperation	3,816,088,342
National Government	3,322,310,817
Instituto de Credito Oficial	1,244,024,282
Caliraya-Botocan-Kalayaan Power Corporation	1,210,707,950
Natixis/Credit National	1,144,865,889
Artigiancassa MCA	707,348,640
Nordic Investment/Development Fund	625,780,896
Banco de Oro/Development Bank of Phils.	350,000,000
Eximbank of Korea	305,550,909
Erste Bank Osterreichischen	262,324,906
US Agency for International Development	48,088,129

	336,826,460,041
Less bond discount	10,794,564,776
<b>Net</b>	<b>326,031,895,265</b>

Further details of the account follow:

CREDITOR / PROJECT	MATURITIES	INTEREST RATES	CURR	ORIGINAL CURRENCY	PESO	
<b>Asian Development Bank</b>						
1288-PHI	Power Transmission Project	1997 to 2013	Cost of Qualified Borrowings	USD	56,696,913.74	2,692,252,949
1474-PHI	Leyte-Mindanao Interconnection Project	2000 to 2011	Cost of Qualified Borrowings	USD	1,789,737.98	84,985,708
1590-PHI	Power Transmission Reinforcement Project	2002 to 2017	Cost of Qualified Borrowings	USD	30,650,454.80	1,455,436,846
1662-PHI	Power Sector Restructuring Program	2002 to 2013	Cost of Qualified Borrowings	USD	50,000,000.00	2,374,250,000
1984-PHI	Electricity Market & Transmission Development Proj.	2009 to 2022	LIBOR + 0.60%	USD	31,723,887.55	1,506,408,800
SPIA	Special Project Implementation Agreement	1991 to 2026	FIXED at 9.65%	USD	28,459,465.00	1,351,397,696
#624P	Mindanao Power Project	1999 to 2011	FIXED at 7%	USD	455,394.04	21,624,386
985-PHI	15th Power Project	1994 to 2009	Cost of Qualified Borrowings + 0.40%	JPY	1,940,026,578.00	1,012,887,876
<b>International Bank for Reconstruction and Development</b>						
3163-0-PH	Energy Sector Loan	1995 to 2010	Cost of Qualified Borrowings + 0.50%	USD	31,675,000.00	1,504,087,375
3626-PH	Power Transmission Project	1999 to 2013	Cost of Qualified Borrowings + 0.50%	USD	23,204,651.80	1,101,872,891
3700-0-PH	Leyte-Cebu Geothermal	1999 to 2014	Cost of Qualified Borrowings + 0.50%	USD	62,913,221.65	2,987,434,330
3700-A-PH	Leyte-Cebu Geothermal	1999 to 2014	Cost of Qualified Borrowings + 0.50%	USD	6,188,319.70	293,852,237
3746-0-PH	Leyte-Luzon Geothermal	1999 to 2014	Cost of Qualified Borrowings + 0.50%	USD	43,896,446.73	2,084,422,773
3746-A-PH	Leyte-Luzon Geothermal	1999 to 2014	Cost of Qualified Borrowings + 0.50%	USD	5,003,405.83	237,586,726
3996-0	Transmission Grid	2001 to 2016	Cost of Qualified Borrowings + 0.50%	USD	21,217,833.72	1,007,528,834
3997-0	Reinforcement Project	2001 to 2016	LIBOR + 0.50%	USD	67,967,006.15	3,227,413,287
296-PHI	Reinforcement Project	2001 to 2016	Service Charge at 0.75%	USD	4,056,451.29	192,620,590
3996-A-PH	Bataan Thermal 2 Transmission Grid	1982 to 2022	Cost of Qualified Borrowings + 0.50%	JPY	1,825,343,224.00	953,011,697
4887-PH	Reinforcement Project	2001 to 2016	LIBOR + 0.50%	USD	10,514,979.78	499,303,815
<b>Overseas Economic Cooperation Fund (OECF)</b>						
PH-C8	Extra High Voltage Transmission Line Project 1&2	1989 to 2004	FIXED at 3.50%	JPY	5,361,445,783.13	2,799,210,843
PH-009	Cagayan Electrification	2002 to 2012	FIXED at 3.20%	JPY	332,780,752.00	173,744,831
PH-013	Abulog River Hydro Electric Power	2002 to 2012	FIXED at 3.20%	JPY	40,187,026.00	20,981,646
PH-029	Power Plant Barge Project 1	2002 to 2012	FIXED at 3.20%	JPY	425,147,696.00	221,969,612

PH-031	Tongonan Geothermal	2002 to 2012	FIXED at 3.20%	JPY	387,781,829.00	202,460,893
PH-043	Mindanao Transmission Line Project	2002 to 2012	FIXED at 3.20%	JPY	201,105,852.00	104,997,365
PH-048	Extra High Voltage Transmission Line Project 1	2002 to 2012	FIXED at 3.20%	JPY	934,031,902.00	487,658,056
PH-057	Extra High Voltage Transmission Line Project 2	2002 to 2012	FIXED at 3.20%	JPY	130,128,999.00	67,940,350
PH-065	Power Plant Barge Project 2	2002 to 2012	FIXED at 3.20%	JPY	316,942,270.00	165,475,559

#### Japan Bank for International Cooperation

	Electricity Market & Transmission Dev't Project	2009 to 2022	Tokyo Swap Reference Rate + 1.25%	JPY	3,058,467,990.00	1,596,826,138
	Leyte-Cebu Interconnection Uprating Project	2006 to 2015	FIXED at 3.69%	JPY	4,250,645,860.00	2,219,262,204

#### Eximbank of Japan

ESPL	Energy Sector Loan	1995 to 2010	Long-Term Prime Rate	JPY	809,250,283.00	422,509,573
	Leyte-Luzon Interconnection Project	1999 to 2014	Long-Term Prime Rate + 0.20%	JPY	2,098,764,130.00	1,095,764,752
Series A	San Roque Multi-Purpose Project	2004 to 2014	Long-Term Prime Rate + 0.20%	JPY	11,715,464,000.00	6,116,643,755
Series B	San Roque Multi-Purpose Project	2004 to 2014	LIBOR + 0.90%	USD	110,809,000.00	5,261,765,365

#### Kreditanstalt für Wiederaufbau

87652	Sucacat 1&4 Rehabilitation Project	1998 to 2018	FIXED at 6.50%	EUR	11,171,727.65	740,085,620
88651	Various Spare Parts	1999 to 2019	FIXED at 3.50%	EUR	6,039,509.18	400,095,137
91654	Sucacat 2&3 Rehabilitation	2002 to 2032	FIXED at 9.0%	EUR	23,641,113.99	1,566,136,330
	Sucacat 2&3 Rehabilitation (Additional)	2006 to 2036	FIXED at 7.0%	EUR	5,903,376.08	391,076,822
91658	Sucacat/Sta.Mesa/Balintawak Transmission Project	2006 to 2023	FIXED at 9.0%	EUR	13,257,798.49	878,280,096
91658	Sucacat/Sta.Mesa/Balintawak Transmission Project	2006 to 2033	FIXED at 9.0%	EUR	27,837,286.47	1,844,117,231
	Northern Luzon Generation & Transmission Proj.	2010 to 2035	FIXED at 7.50%	EUR	22,804,494.32	1,510,713,372
	Northern Luzon Generation & Transmission Proj.	2006 to 2025	FIXED at 7.50%	EUR	44,117.29	2,922,606
	Energy Sector Loan	2008 to 2035	FIXED at 7.0%	EUR	12,613,243.05	835,580,683

#### Natixis/Credit National

1528	Navotas Gas Turbine	1997 to 2016	FIXED at 5.45%	EUR	7,317,552.80	484,760,798
1543	Sucacat Gas Turbine	1999 to 2019	FIXED at 5.45%	EUR	2,309,602.56	153,002,624
467-OA1	Pielstick for Diesel Power Plant	2000 to 2022	FIXED at 3.0%	EUR	2,121,342.88	140,531,072
467-OB1	Bataan Gas Turbine	1999 to 2020	FIXED at 3.0%	EUR	4,033,170.00	267,182,523
747-OD1	Northern Luzon 230KV Transmission Line	2001 to 2016	FIXED at 3.10%	EUR	1,500,292.62	99,388,872

#### Instituto de Crédito Oficial

	Palawan Backbone Transmission Line	2003 to 2013	FIXED at 2.0%	USD	8,271,428.68	392,768,791
	200MW Mindanao Barge	2003 to 2023	FIXED at 1.25%	USD	17,926,829.33	851,255,491

#### Nordic Investment/Development Fund

PIL95/ 1	Leyte-Cebu HV Interconnection Project	2005 to 2034	Service Charge at 0.75%	EUR	3,851,341.69	255,137,137
	Leyte-Cebu HV Interconnection Project	2000 to 2014	LIBOR + 0.85%	USD	4,055,491.40	192,575,009
	Leyte-Cebu HV Interconnection Project	2000 to 2010	LIBOR + 0.65%	USD	3,750,000.00	178,068,750
<b>Eximbank of Korea</b>						
94- 2063	Transmission & Substation Project in Luzon	2004 to 2018	FIXED at 3.50%	KRW	4,144,850,000.00	147,971,145
	Mindanao Power Transmission	2002 to 2017	FIXED at 3.50%	KRW	4,413,999,000.00	157,579,764
<b>National Government</b>						
	New Money Bond (B) Principal Collateralized Interest Reduction Bond (B)	1997 to 2009	LIBOR + 0.8125%	USD	292,640.00	13,896,010
		2017	FIXED at 6.50%	USD	4,880,000.00	231,726,800
	New Money Bond (B) Principal Collateralized Interest Reduction Bond (A)	1997 to 2009	LIBOR + 0.8125%	USD	1,691,840.00	80,337,022
		2018	FIXED at 6.50%	USD	1,658,000.00	78,730,130
	Principal Collateralized Interest Reduction Bond (B)	2017	FIXED at 6.50%	USD	61,443,000.00	2,917,620,855
<b>Deutsche Bank</b>						
	Leyte Interconnection Project General Funding Requirements	2009	FIXED at 9.75%	USD	100,000,000.00	4,748,500,000
	General Funding Requirements	2011	LIBOR + 4.25%	USD	300,000,000.00	14,245,500,000
	General Funding Requirements	2011	LIBOR + 4.25%	USD	100,000,000.00	4,748,500,000
	General Funding Requirements	2016	FIXED at 6.875%	USD	500,000,000.00	23,742,500,000
	General Funding Requirements	2010	FIXED at 9.875%	USD	125,000,000.00	5,935,625,000
	General Funding Requirements	2010	FIXED at 9.875%	USD	375,000,000.00	17,806,875,000
<b>Citibank</b>						
	General Funding Requirements	2010	FIXED at 9.467%	USD	300,000,000.00	14,245,500,000
	General Funding Requirements	2010	FIXED at 10.09%	USD	400,000,000.00	18,994,000,000
	General Funding Requirements	2015	FIXED at 4.65%	JPY	12,000,000,000.00	6,265,200,000
<b>Bank of Tokyo-Mitsubishi UFJ</b>						
	Various Transmission Projects	2009	FIXED at 3.78%	JPY	20,800,000,000.00	10,859,680,000
<b>Bank of New York/JP Morgan Chase Manhattan</b>						
	General Funding Requirements	2016	FIXED at 8.40%	USD	160,000,000.00	7,597,600,000
	General Funding Requirements	2028	FIXED at 9.625%	USD	300,000,000.00	14,245,500,000
	General Funding Requirements	2020	FIXED at 3.22%	JPY	24,750,000,000.00	12,921,975,000
	General Funding Requirements	2022	FIXED at 3.55%	JPY	37,000,000,000.00	19,317,700,000
<b>US Bank</b>						
	General Funding Requirements	2008 to 2018	FIXED at 5.40%	USD	238,095,238.00	11,305,952,376

<b>Bureau of Treasury</b>						
General Funding Requirements	2009	MART + 0.50%	PhP	3,752,000,000.00	3,752,000,000	
General Funding Requirements	2011	MART + 0.625%	PhP	8,800,000,000.00	8,800,000,000	
General Funding Requirements	2012	FIXED at 9.875%	PhP	11,000,000,000.00	11,000,000,000	
General Funding Requirements	2010	FIXED at 9.125%	PhP	2,061,000,000.00	2,061,000,000	
General Funding Requirements	2012	FIXED at 10.375%	PhP	3,000,000,000.00	3,000,000,000	
General Funding Requirements	2011	FIXED at 5.25%	PhP	3,680,000,000.00	3,680,000,000	
General Funding Requirements	2016	FIXED at 5.875%	PhP	6,320,000,000.00	6,320,000,000	
<b>Caliraya-Botocan-Kalayaan Power Corporation</b>						
General Funding Requirements	2006 to 2016		USD	25,496,640.00	1,210,707,950	
<b>Erste Bank Osterreichischen</b>						
Agus 1 Hydro Electric Power Rehabilitation	2005 to 2013	EUR LIBOR + 0.50%	EUR	3,959,842.37	262,324,906	
<b>Artigiancassa MCA</b>						
Bacon-Manito Geothermal	2001 to 2010	FIXED at 1.50%	USD	14,896,254.19	707,348,640	
<b>US Agency for International Development</b>						
492-H-032 Tiwi Geothermal 1&2	1985 to 2015	FIXED at 3.0%	USD	886,737.93	42,106,751	
492-H-032 Tiwi Geothermal 1&2	2002 to 2012	FIXED at 3.0%	USD	125,963.52	5,981,378	
<b>Banco de Oro/Development Bank of Phils.</b>						
Leyte-Cebu Interconnection Uprating Project.	2006 to 2012	FIXED at 11.32%	PhP	350,000,000.00	350,000,000	
<b>Department of Energy</b>						
Gas Sale and Purchase Agreement			PhP	28,297,252,592.42	28,297,252,592	
<b>Land Bank of the Phils./Development Bank of the Phils</b>						
General Funding (IPP Payment)	2009	FIXED at 8.1654%	PhP	10,000,000,000.00	10,000,000,000	
<b>Land Bank of the Phils./Development Bank of the Phils</b>						
General Funding (IPP Payment)	2009	FIXED at 8.20%	PhP	10,000,000,000.00	10,000,000,000	
<b>Total long-term liabilities</b>					<b>336,826,460,041</b>	

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**18. OTHER LONG-TERM LIABILITIES**

This account consists of the following:

	2008	2007
Universal charge	1,428,726,949	849,849,019
Deferred credits	604,850,732	-
Various	1,412,194	9,961,343
	<b>2,034,989,875</b>	<b>859,810,362</b>

The details of the Universal Charge are in Note 14. *Deferred credits* refer to unearned portion of the rent income from lease of land pertaining to sold plants.

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**19. DUE TO GOCCs AND NATIONAL GOVERNMENT AGENCIES**

This account consists of the following amounts which are still being reconciled with the concerned agencies:

	2008	2007
Due to GOCCs	11,590,084,446	11,228,144,304
Due to national government agencies	11,825,290,944	25,025,877
	<b>23,415,375,390</b>	<b>11,253,170,181</b>

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**20. CAPITAL FROM ASSET-DEBT TRANSFER**

This account pertains to the difference in the carrying amount of assets transferred from NPC to PSALM and TransCo and (i) the amount of liabilities assumed by PSALM and (ii) the amount of liabilities transferred to TransCo. This includes the balances initially transferred in September 2008, the additional accounts transferred reflecting the October to December 2008 transactions, and the subsequent adjustments related to the asset-debt accounts transfer. Since the fair value or the reserve price, in this case, of any of the assets held for sale is set only on bidding date, the NPC-transferred generating assets were initially recognized in the books of PSALM at their NPC-carrying values as of the transfer date. These carrying values which are lower than the assumed liabilities created the negative balance in the account. An asset appraisal is dispensed with for the assets for privatization since appraised values are not a crucial consideration in establishing minimum acceptable sale prices (reserve price). PSALM has chosen the Discounted Cash Flow Analysis valuation method, which best optimized the value of these assets.

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## 21. INCOME FROM SALE OF ASSETS

PSALM's income is derived mostly from its privatization-related activities as follows:

	2008	2007
Gain on sale of disposed assets	33,429,983,174	20,534,301,372
Privatization participation fees	7,401,796	8,532,279
IPARP data room access & site visit/CD sale	859,692	594,905
Magat purchase price option & accrued rental	-	315,446
	33,438,244,662	20,543,744,002

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## 22. MAINTENANCE AND OTHER OPERATING EXPENSES (MOOE)

In 2008, major expense items comprising MOOE are depreciation (P2.887 billion) and professional services (P118.159 million), which make up 91% and 4%, respectively. Depreciation leaped from a mere P19.576 million in 2007 to P2.887 billion in 2008 due to the transfer of NPC's generation and other disposable assets to PSALM in 1 October 2008.

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## 23. GAIN (LOSS) ON FOREIGN EXCHANGE

As the Company translates its foreign currency transactions/monetary items in accordance with PAS 21, the resulting gains and losses from the exchange differences are recognized in the statement of income and expenses as follows:

	2008	2007
Unrealized forex gain (loss) on translation	(13,102,401,778)	4,563,866,670
Realized forex gain (loss) on foreign currency-related transactions	6,408,988,353	(6,102,942,832)
	(6,693,413,425)	(1,539,076,162)

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## 24. ORGANIZATIONAL DEVELOPMENT AND EFFICIENCY

A highly significant corporate milestone is the initiation by PSALM of an ISO certification program to enhance investor confidence on PSALM and,

at the same time, effect a culture change in the organization and improve management systems. The program was started in March 2008 with the first stage marked by a series of familiarization seminars for six months targeting 80% of the total workforce for a unified understanding and commitment to the program.

Subsequently, teams such as the Documentation and IQA Teams were created to ensure implementation of the program. An external auditor, the Certification International Philippines, Inc., was awarded the contract to determine the readiness of PSALM's Quality Management System for certification. The external audit began in January 2009.

The focus on personnel development was evident with the substantial number and variety of training and development programs held in 2008. A total of thirty-five (35) in-house training and development programs were conducted/facilitated while selected personnel were sent to nineteen (19) local external training programs and to five (5) professional conventions/conferences held within the country.

Employee wellness continues to be given attention. An annual physical and medical examination for all PSALM officers and employees totaling one hundred sixty-two (162) personnel, including contractual personnel, was held last November 2008 as scheduled.

Strong logistic support was provided to the different departments within PSALM through the development and/or implementation of thirteen (13) Information and communications technology programs, systems and capacity building activities.

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## 25. CONTINGENCIES

### Legal Proceedings Involving PSALM

PSALM is involved in various legal and administrative proceedings, including litigation and proceedings related to electricity charges and challenges to certain provisions of the EPIRA. Because of the nature of these proceedings, PSALM cannot predict the ultimate outcomes of these proceedings, some of which may be unfavorable. However, PSALM does not expect the outcomes of these proceedings, either individually or in the aggregate, to have a material adverse effect on its financial position.

On 23 April 2009 and 7 May 2009, respectively, PSALM was impleaded in two separate actions by NPC's employees to enjoin implementation of the Operations and Maintenance Agreement (OMA). The first case, **G.R. 187359 (NECU and NEW vs. NPC and PSALM)**, seeks to enjoin

implementation of the OMA in an effort to collect on a judgment rendered in the employees' favor against NPC for unpaid employment compensation-related claims. The second case, **G.R. No. 187420 (PGEA-NPC vs. NPC, NP Board, PSALM and PSALM Board)**, seeks to enjoin the OMA's implementation based on a claim that it violates the EPIRA. PSALM does not expect these cases to have a material adverse effect on its results of operations or financial condition. PSALM is reviewing these cases independently, and is also coordinating with the Office of the Government Corporate Counsel.

### ***Basic Generation Rates Petition***

The basic power generation rate is based on a return-on-rate-base (RORB) method with time-of-use pricing. The RORB method takes a ratio (calculated as a percentage of investment in facilities and working capital necessary for day to day operations, or "rate base") of rate base to determine the return on rate base that will be considered together with the operating costs in determining the generation charge.

On 16 January 2009, NPC and PSALM jointly filed an application for revised basic generation rates before the Energy Regulatory Commission (ERC), docketed as **ERC Case No. 2009-04 RC** to reflect the impact of the sale, transfer and disposal of NPC's generation assets, as well as to alleviate the current financial difficulties resulting from low power generation rates.

In support of their application, NPC and PSALM prepared an analysis based on the 2007 calendar year to show that NPC's costs have significantly increased from 2002 and 2004. PSALM and NPC filed for basic rate increases of ₱0.8332 per kWh for Luzon, ₱1.3815 per kWh for the Visayas and ₱1.0686 per kWh for Mindanao.

On 16 February 2009, the ERC provisionally authorized increases to the basic electricity rates amounting to ₱0.4682 per kWh for Luzon grid and ₱0.7147 per kWh for Mindanao grid. In a separate order dated 23 March 2009, the ERC provisionally authorized a ₱0.8376 per kWh for the Visayas grid. With these adjustments, the new average basic rates are ₱4.3648 per kWh for Luzon, ₱3.7255 per kWh for the Visayas, and ₱2.8177 per kWh for Mindanao. These provisional rates were effective beginning March 2009.

The provisional rates may still be revised depending on the outcome of ERC hearings that are currently being conducted on the rate application as well as additional evidence to be submitted by applicants and intervenors. These basic rates are further subject to the adjustments described below. Failure to secure the ERC's approval for the new basic

generation rate, as well as for the adjustments described below, will materially and adversely affect PSALM's results of operations and financial condition.

### ***Petition for Basic Rate Adjustment Mechanisms***

The ERC has promulgated two price adjustment mechanisms to the basic rates of electricity under the EPIRA. These adjustment mechanisms are (i) the GRAM and (ii) the ICERA.

The GRAM was approved by the ERC in 2003 to allow for recovery of incremental fuel and purchased power costs resulting from changes in either fuel prices or the cost of power purchased from IPPs.

The ICERA allows for the recovery of incremental costs that are incurred as a result of foreign currency exchange fluctuations. Under current ERC rules, PSALM is required to file applications quarterly for GRAM and ICERA adjustments. These adjustments can cause the basic rate to be increased or decreased, depending on developments in fuel prices, IPP costs and foreign exchange rate fluctuations.

On 14 August 2008, PSALM submitted to the ERC its Proposed Rules for the Automatic Recovery of NPC/PSALM's Generation Assets' Monthly Fuel, Purchased Power and Foreign Exchange-Related Costs. After several consultative processes, the ERC passed Resolution No. 19 dated 3 August 2009 adopting the Rules for Automatic Recovery of Monthly Fuel and Purchased Power Costs and Foreign Exchange-Related Costs. This effectively replaced the existing GRAM and ICERA guidelines, thus eliminating the need for PSALM and NPC to file for cost recoveries every quarter and await a decision from the ERC before passing the costs to customers.

### ***Petition for Recovery of Universal Charge***

The Universal Charge is imposed on every end-user of electricity for specific uses that are enumerated under Section 34 of the EPIRA. The amount for each component of the Universal Charge is determined by the ERC as mandated by Section 32 of the EPIRA. It is also collected from end-users on a monthly basis and remitted to PSALM.

PSALM is mandated under Section 51(d) of the EPIRA to calculate the amount of stranded debts and stranded contract costs of NPC which shall form the basis for ERC in the determination of the Universal Charge.

On 30 June 2009, PSALM filed before the ERC two separate petitions for the recovery of the Universal Charge for Stranded Contract Cost and Stranded Debt.

The first petition seeks to recover NPC's stranded costs portion of the Universal Charge for the Luzon Grid, docketed as **ERC Case No. 2009-046RC**. Stranded Contract Cost refers to the excess of the contracted cost of electricity under eligible IPP contracts of NPC over the actual selling price of the contracted energy output of such contracts in the market. To be eligible for recovery under the UC, such contracts must have been approved by the then Energy Regulatory Board (ERB) as of 31 December 2000. Based on a 5-year recovery period, PSALM proposed to ERC a UC for stranded cost amounting to ₱0.0920 per kWh. The petition is currently under evidentiary hearing before the ERC.

The second petition seeks to recover NPC's stranded debt portion of the Universal Charge for the Luzon, Visayas and Mindanao Grids, docketed as **ERC Case No. 2009-047RC**. Stranded Debt refers to any unpaid financial obligations of NPC which have not been liquidated by the proceeds from the sales and privatization of NPC assets. Financial obligations pertain to net obligations of NPC after deducting the ₱200 billion debt assumed by the National Government (Section 32 of the EPIRA). Based on a 17-year recovery period, PSALM proposed to ERC a ₱0.3049 per kWh UC for Stranded Debt of NPC. The petition is now under evidentiary hearing before the ERC.

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## 26. OTHER SUBSEQUENT EVENTS

The following are the other events subsequent to balance sheet date:

### *Sale/Disposal of assets*

The following plants were sold on the dates indicated:

Plant	Status
Cebu II Diesel Power Plant	Negotiated sale with Taifu Metal Exchange Corporation on 21 January 2009
Bataan Thermal Power Plant	Negotiated sale with Rubenori, Inc. on 14 April 2009
Aplaya & Gen Santos Diesel Power Plants	Negotiated packaged sale with TEC Industries, Inc. on 25 May 2009
Batangas Coal-Fired Thermal Power Plant	Negotiated sale with DMCI Holdings, Inc. on 8 July 2009
Power Barge 117	Negotiated sale with Therma Mobile, Inc. on 31 July 2009
Power Barge 118	Negotiated sale with Therma Marine, Inc. on 31 July 2009

*Operation and Maintenance Service Contract (OMSC)*

Pursuant to its privatization mandate, PSALM schedules the selling of the plants thru open and competitive bidding on dates such that the date of turn-over to the winning bidder/new owner would correspond with the termination of the plants' operation and maintenance agreements with third parties. In some instances, the biddings would not proceed as planned due to various constraints, delaying the turn-over of the plants to the new owner. Pending these plants' privatization and still continue the operation of the plants, prevent their deterioration, and service the power requirements of the public, PSALM entered into Operation and Maintenance Service Contract (OMSC) with third parties.

Plant	Parties	Contract Amount (estimated)	Period
Naga Land-Based Geothermal Turbine	PSALM and SPC Power Corp.	₱ 38.2 million	6 months from effective date
Limay Combined Cycle Power Plant	PSALM and Alstom	₱ 1,028 million	19 Apr 2009 - 18 Jan 2010
Power Barge 117	PSALM and BWSC *	₱ 318.2 million	6 months from effective date
Power Barge 118	PSALM and BWSC *	Agreed rates / hour, engine, barge	6 months from effective date

\* Burmeister & Wain Scandinavian Contractor

*Liability Management Program*

In the transfer of asset-debt accounts from NPC to PSALM, PSALM assumed the loans of NPC. Of these loans, about more than a third of the principal payments are set to mature in 2009, 2010, and 2011. In addition to these cash requirements, IPP operations and generating assets also need funding. To address the resulting cash deficit, the following financing structures were recommended to and approved by the PSALM Board:

- a. Approval on 25 May 2009 of US\$ 1 billion bond issue, in single tranche, to mature in 10 years or 27 May 2019, for general corporate funding requirements including servicing of payments under IPP contracts;
- b. Approval on 31 July 2009 of a program involving the securitization of deferred payments payable by the National Grid Corporation of the Philippines to PSALM over the next 20 years in an amount of up to US\$3.0 billion;
- c. Approval on 26 August 2009 structure of the Liability Management Program Phase II (LMP-II) consisting of:

- Securitization of the TransCo deferred payments (approved on 31 July 2009)
- Peso bonds/credit facility with an aggregate amount of up to P50 billion
- Bond exchange of up to US\$1.34 billion inclusive of new money component of between US\$ 450-700 million
- Financial derivatives transaction – forwards, swaps, and options
- US\$ bond issuance of up to US\$1.0 billion

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**27. AUTHORITY FOR ISSUANCE**

These financial statements have been approved for issue by the PSALM Board of Directors on 28 August 2009.