

COVER SHEET

P W - 1 0 2

M A N I L A E L E C T R I C C O M P A N Y

Company's Full Name

L O P E Z B U I L D I N G , O R T I G A S

A V E N U E , P A S I G C I T Y

(Business Address: No. Street City/ Town / Province)

Atty. William S. Pamintuan

Contact Person

632 8014

Company Tel. No.

SEC FORM

LAST TUESDAY OF
MAY IN EACH YEAR

1 2

Month

3 1

Day

Fiscal Year

17 - A

FORM TYPE

0 5

Month

2 7

Day

N/A

Secondary License Type, If Applicable

Dept. Requiring this Doc.
Number/Section.

N/A

Amended Articles

Total Amount of
Borrowings

46,409 as at
December 31,
2013

Total No. of Stockholders

₱33,591
Million

Domestic

N/A

Foreign

To be accomplished by SEC Personnel Concerned

File Number

LCU

Document I. D.

Cashier

STAMPS

TABLE OF CONTENTS

	<u>Page No.</u>
PART I – BUSINESS AND GENERAL INFORMATION	1
Item 1. Business	1
Item 2. Properties	19
Item 3. Legal Proceedings	20
Item 4. Submission of Matters to a Vote of Security Holders	31
PART II – OPERATIONAL AND FINANCIAL INFORMATION	31
Item 5. Market for Issuer’s Common Equity and Related Stockholders Matters	31
Item 6. Management’s Discussion and Analysis or Plan of Operation	33
Item 7. Financial Statements	79
Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	80
PART III – CONTROL AND COMPENSATION INFORMATION	80
Item 9. Directors and Executive Officers of the Issuer	80
Item 10. Executive Compensation	93
Item 11. Security Ownership of Certain Beneficial Owners and Management	94
Item 12. Certain Relationships and Related Transactions	97
PART IV – CORPORATE GOVERNANCE	98
Item 13. Corporate Governance	98
PART V – EXHIBITS AND SCHEDULES	99
Item 14. Exhibits and Reports	99
SIGNATURES	108
INDEX TO FINANCIAL STATEMENTS AND SUPPLEMENTARY SCHEDULES	110

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-A

ANNUAL REPORT PURSUANT TO SECTION 17
OF THE SECURITIES REGULATION CODE AND SECTION 141
OF THE CORPORATION CODE OF THE PHILIPPINES

1. For the fiscal year ended **DECEMBER 31, 2013**
2. SEC Identification Number **PW-102** 3. BIR Tax Identification No. **000-101-528-000**
4. Exact name of issuer as specified in its charter **MANILA ELECTRIC COMPANY**
5. **REPUBLIC OF THE PHILIPPINES** 6. (SEC Use Only)
Province, Country or other jurisdiction Industry Classification Code:
of incorporation or organization
7. **LOPEZ BUILDING, ORTIGAS AVENUE, PASIG CITY** **0300**
Address of principal office Postal Code
8. **(+632) 631-5567**
Issuer's telephone number, including area code
9. **NOT APPLICABLE**
Former name, former address, and former fiscal year, if changed since last report.
10. Securities registered pursuant to Sections 8 and 12 of the SRC, or Sec. 4 and 8 of the
RSA

Title of Each Class	Number of Shares of Common Stock Outstanding
---------------------	---

Common Stock	1,127,098,705
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Amount of Debt Outstanding
₱33,591 million

11. Are any or all of these securities listed on a Stock Exchange?

Yes [/] No []

If yes, state the name of such stock exchange and the classes of securities listed therein:

PHILIPPINE STOCK EXCHANGE

12. Check whether the issuer:

(a) has filed all reports required to be filed by Section 17 of the SRC and SRC Rule 17.1 thereunder or Section 11 of the RSA and RSA Rule 11(a)-1 thereunder, and Sections 26 and 141 of The Corporation Code of the Philippines during the preceding twelve (12) months (or for such shorter period that the registrant was required to file such reports);

Yes [/] No []

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

Yes [/] No []

13. State the aggregate market value of the voting stock held by non-affiliates of the registrant. The aggregate market value shall be computed by reference to the price at which the stock was sold, or the average bid and asked prices of such stock, as of a specified date within sixty (60) days prior to the date of filing. If a determination as to whether a particular person or entity is an affiliate cannot be made without involving unreasonable effort and expense, the aggregate market value of the common stock held by non-affiliates may be calculated on the basis of assumptions reasonable under the circumstances, provided the assumptions are set forth in this Form.

The aggregate market value of voting stock held by non-affiliates of the registrant as of March 31, 2014:

Shares: 148,609,576

Closing Price: ₱284.00

Aggregate: ₱42,205 Million

PART I – BUSINESS AND GENERAL INFORMATION

Item 1. Business

1) Business Development

The name of the issuer is Manila Electric Company, also known as *MERALCO* or “the *Company*”, was duly organized on May 7, 1919 under the laws of the Republic of the Philippines. *MERALCO*, is a private distribution utility or *DU*, which holds a congressional franchise under Republic Act or *RA* No. 9209 effective June 28, 2003. *RA* No. 9209 grants *MERALCO* a 25-year franchise valid through June 28, 2028 to construct, operate, and maintain the electric distribution system in the cities and municipalities of Bulacan, Cavite, Metro Manila, and Rizal and certain cities, municipalities, and barangays in the provinces of Batangas, Laguna, Pampanga, and Quezon. On October 20, 2008, the Energy Regulatory Commission or *ERC*, granted *MERALCO* a consolidated Certificate of Public Convenience and Necessity for the operation of electric service within its franchise coverage, effective until the end of *MERALCO*'s congressional franchise.

MERALCO has a unit for its participation in retail electricity supply or *RES*. The *MERALCO* local *RES*, otherwise known as *MPower*, is a business unit within *MERALCO*.

MERALCO also organized several subsidiaries to provide unregulated electricity-related or other value-added services, which contributed to the efficiency and profitability of the core business. These subsidiaries also provide services to third parties.

The following are the subsidiaries of *MERALCO*, all of them incorporated in the Philippines except for Lighthouse Overseas Insurance Company, Limited or *LOIL* and *MPG Asia Limited*. *MERALCO* and its subsidiaries are herein referred to as “*MERALCO Group*”.

Meralco Industrial Engineering Services Corporation or *MIESCOR*, is 99%-owned by *MERALCO* with the remaining 1% owned by the *MIESCOR* Provident Fund. It was incorporated on December 5, 1973 and is a holder of the highest contractor license Category AAA since 1982. *MIESCOR* is engaged in engineering, construction and maintenance activities for the electric power industry, industrial plants, water resources and telecommunications companies.

In 2013, *MIESCOR* completed several major projects sourced through competitive bids with *MERALCO*, government agencies and other third parties.

Corporate Information Solutions, Inc. or *CIS*, is a wholly owned subsidiary of *MERALCO*, and was incorporated in 1974 to provide information technology services and integrated business solutions to enterprise clients. In 1997, *CIS* introduced the bills payment business as a separate business segment.

In 2006, *CIS* spun off its bills payment collection business to a subsidiary, *CIS Bayad Center, Inc.* or *CIS Bayad Center*. *CIS Bayad Center* has a network of bills payment collection center nationwide, which operates under the brand name “Bayad Center.” *CIS Bayad Center* is the country's leading outsourced over-the-counter payment collection. *CIS Bayad Center* accepts payments for 162 biller brands through its more than 2,000-strong, strategically-located branches nationwide, and US-based online payment facility. *Bayad Center* also offers remittance cash pick-up, electronic wallet services (i.e. vehicle insurance processing), prepaid loading, service applications acceptance, and remittance payout.

CIS Bayad Center provides outsources tellering services through its wholly owned subsidiary, Customer Frontline Solutions, Inc. or *CFS*. *CFS* provides personnel to man the collection operations of *MERALCO* and third party utility billers.

Meralco Energy, Inc. or *MEI*, operates under the trade name *MSERV*. It is a wholly-owned subsidiary of *MERALCO*, which was incorporated in June 2000. *MServ* aims to be the country's premier Energy Services Company or *ESCO* through its two flagship services: Strategic Loadside Outsourcing or *SLO*, and Energy Efficiency or *EE* Solutions.

SLO offers customers the opportunity to outsource their load side electricity requirements. This allows customers to focus on their respective core businesses knowing that all their electrical concerns are being handled by a *MERALCO* company. Under *MServ's* *SLO* services are the 1) design, procurement, and installation of right-sized electrical facilities; 2) *MERALCO* managed services; and 3) power quality and power factor services. The company provides "Best in Class" service levels such as guaranteed continuous power, 24-hours replacement of critical equipment, and 24/7 technical support.

MServ's EE solutions provide customers with energy-saving alternatives. *MServ* can diagnose a customer's energy usage habits, and recommend different solutions that can help optimize their consumption. These solutions include 1) lighting efficiency services; 2) Heating, Ventilation, and Air Conditioning or *HVAC*, Efficiency Services; and 3) e-vehicle service leasing.

MServ has been responsible for the design, installation, oOperation, and maintenance of electrical facilities of industrial buildings, state-of-the-art data centers, large commercial centers, and even high-profile event arenas, among many others. *MServ* has also been trusted by dozens of companies in different industries, from manufacturing to universities to government agencies, for their emergency electrical concerns. Through their services and expertise, *MServ* aims to provide their customers with the most cost-efficient, effective, and reliable energy solutions.

e-Meralco Ventures, Inc. or e-MVI, is a wholly-owned subsidiary of *MERALCO* established on June 22, 2000. Through an indirectly wholly owned subsidiary, Radius Telecoms, Inc. or *Radius*, it holds a telecommunications franchise issued by the National Telecommunications Commission to construct, install, establish, operate and maintain for commercial purposes and in the public interest, the business of providing basic and enhanced telecommunications services in the Philippines and between the Philippines and other countries and territories. *Radius* is a wholly owned subsidiary of Paragon Vertical, Inc. or *Paragon*.

Radius operates and maintains approximately 2,000 kilometers of fiber-optic cables and telecommunications infrastructure. Through such facilities, it provides data connectivity solutions, high capacity services, and managed services to local and international carriers, internet service providers, data centers, and corporate clients in select industries. The Carrier Ethernet service of *Radius* is certified by Metro Ethernet Forum, an international organization of Carrier Ethernet users, as fully compliant with global standards.

Meralco Financial Services Corporation or *Finserve*, was incorporated on March 19, 2002 as a wholly-owned subsidiary of *MERALCO*.

Finserve owns and operates “The Strip” Mall and holds real property for lease.

Clark Electric Distribution Corporation or **CEDC**, organized on February 19, 1997 is 65%-owned by *MERALCO* and 35%-owned by J Ten Equities, Inc., the holding company of Angeles Electric Corporation. It is a private *DU* which holds a franchise issued by Clark Development Corporation for the exclusive distribution of electricity within the Clark Economic Zone or *CEZ*.

CEDC is now on its Third Regulatory Year of the Second Regulatory Period of the ERC-approved Annual Revenue Requirement under the Performance-Based Regulations for the Regulatory Period October 1, 2011 to September 30, 2015.

Republic Surety and Insurance Company, Inc. or **RSIC**, is a professional non-life insurance company, which *MERALCO* acquired in 2007 as a wholly owned subsidiary to align with *MERALCO*’s recognition of a disciplined approach in managing its risk exposures.

RSIC continues to renew an insurance program that provides coverage to *MERALCO*’s transmission and distribution assets.

Lighthouse Overseas Insurance Company, Limited or **LOIL**, is a wholly owned subsidiary and captive reinsurer of *MERALCO*. *LOIL* was incorporated in Bermuda on August 24, 2007. It is registered as a Class 1 insurer under The Bermuda Insurance Act 1978 and Related Regulations and received its license to operate in the territory in March 2008.

LOIL, together with *RSIC* serves as the vehicle to reinsure *MERALCO*’s major catastrophic risk exposure.

MERALCO PowerGen Corporation or **MGen**, is a wholly owned subsidiary of *MERALCO*. *MERALCO*’s strategic decision to re-enter into power generation is through *MGen*.

On July 22, 2011, *MGen* signed a Shareholders’ Agreement with Therma Power Inc. or *TPI*, and Taiwan Cogeneration International Corporation – Philippine Branch or *TCIC*, whereby *MGen* acquired a 47% plus two (2) share-interest in Redondo Peninsula Energy, Inc. or *RP Energy*. *TPI* and *TCIC* each own equal interest in 25% less one (1) share of *RP Energy*. The remaining 3% is held by the Meralco Pension Fund. *RP Energy* continues to undertake development of a 2x300 MW Circulating Fluidized Bed or *CFB*, coal-fired power generation plant in the Subic Freeport Zone through the continuous land development while awaiting for the Supreme Court of the Philippines or *Supreme Court* decision on a Motion for Reconsideration filed related to a Writ of *Kalikasan* case. Please refer to **OTHER QUANTITATIVE AND QUALITATIVE DISCLOSURES** under Item 6 of this Form 17A for a detailed discussion of the case.

In March 2013, *MGen* acquired an effective 28% equity in PacificLight Power Pte Ltd. or *PacificLight Power*, in Jurong Island, Singapore.

In October 2013, *MGen* signed a Share Sale and Purchase Agreement or *SSPA*, and Shareholders’ Agreement or *SHA*, with First Metro Investment Corporation or *First Metro*, for the acquisition of a 20% share in Global Business Power Corporation or *GBPC*, at ₱7.15 billion.

In late 2013, *MGen* signed a Joint Development Agreement and Shareholders' Agreement with New Growth B.V., a wholly owned subsidiary of EGCo of Thailand, paving the way for the start of development activities for a 460MW coal-fired power generation facility in Mauban, Quezon Province. The facility will be the country's first power plant to use supercritical technology.

2) Business of Issuer

The principal business of *MERALCO* is the distribution and sale of electric energy through its distribution network facilities in its franchise area. Its market is categorized into four (4) classes. Following are the percentage contribution to sales of each customer segment based on kWh-sales:

	2013	2012	2011
Residential	30.03%	29.84%	30.55%
Commercial	39.03%	38.90%	39.31%
Industrial	30.56%	30.86%	29.68%
Streetlights	0.38%	0.40%	0.46%
TOTAL	100.00%	100.00%	100.00%

MERALCO sources the electricity it distributes from different power suppliers as follows:

	2013	2012	2011
National Power Corporation or <i>NPC</i>	0.24%	0.86%	3.44%
First Gas Power Corporation or <i>FGPC – Sta. Rita Power Plant</i> and FGP Corp. or <i>FGP – San Lorenzo Power Plant</i>	28.96%	31.38%	36.98%
Quezon Power (Phils.) Ltd.	7.95%	8.39%	9.87%
Philippine Electricity Market Corporation or <i>PEMC</i> , – Wholesale Electricity Spot Market or <i>WESM</i>	6.13%	6.42%	7.31%
AES Corporation or Masinloc Power Partners Co., Ltd. or <i>AES-Masinloc</i>	8.40%	6.45%	5.88%
Therma Luzon, Inc. or <i>TLI – Pagbilao Coal Plant</i>	7.91%	8.38%	6.92%
South Premier Power Corporation or <i>SPPC – Ilijan Power Plant</i>	20.52%	23.42%	20.88%
Aboitiz Power Renewables, Inc. or <i>APRI – Makban Geothermal Plant</i>	1.04%	5.94%	2.23%
San Miguel Energy Corporation or <i>SMEC – Sual Coal-fired Plant</i>	9.23%	4.07%	3.25%
Sem-Calaca Power Corporation or <i>Sem– Calaca</i>	8.11%	4.51%	2.87%
Others	1.51%	0.18%	0.37%
TOTAL	100.00%	100.00%	100.00%

The franchise area of *MERALCO* is a total of 9,337 square kilometers, covering 34 cities and 77 municipalities. This includes Metro Manila, industrial estates, and suburban and urban areas of the adjacent provinces.

Government Approval of Principal Products or Services

On June 9, 2003, then President Gloria Macapagal-Arroyo signed into law Republic Act or RA No. 9209, otherwise known as the **“An Act Granting the Manila Electric Company A Franchise To Construct, Operate and Maintain A Distribution System for the Conveyance of Electric Power to the End-Users in the Cities/Municipalities of Metro Manila, Bulacan, Cavite and Rizal and Certain Cities/Municipalities/Barangays in Batangas, Laguna, Quezon and Pampanga”**, which took effect on June 28, 2003.

MERALCO is involved in the distribution and supply of electricity and is subject to the rate-making regulations and regulatory policies of the *ERC*. *MERALCO*'s billings to customers are itemized or “unbundled” into a number of bill components that reflect the various costs incurred in providing electric service.

The adjustment of each bill component is governed by mechanisms promulgated and enforced by the *ERC*, mainly: (i) the “Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities”, which govern the recovery of pass-through costs, including over- or under-recoveries of the bill components, namely: (a) generation charge, (b) transmission charge, (c) system loss or *SL* charge, (d) lifeline subsidy, and (e) local franchise or *LFT*, and (f) business tax; and (ii) the “Rules for the Setting of Distribution Wheeling Rates” or *RDWR*, as modified by *ERC* Resolution No. 20, Series of 2008, which govern the determination of *MERALCO*'s distribution, supply, and metering charges.

Effects of Existing and of Probable Governmental Regulations on the Business

Supreme Court or Supreme Court, Decision on Unbundling Rate Case

On May 30, 2003, the Energy Regulatory Commission or *ERC*, issued an Order approving *MERALCO*'s unbundled tariffs that resulted in a total increase of ₱0.17 per kWh over the May 2003 tariff levels. However, on August 4, 2003, certain consumer and civil society groups filed a Petition for Review with the Court of Appeals or *CA*, on the *ERC*'s ruling. On July 22, 2004, the *CA* set aside the *ERC*'s ruling on *MERALCO* rate unbundling and remanded the case back to the *ERC*. Further, the *CA* opined that the *ERC* should have asked the Commission on Audit or *COA*, to audit the books of *MERALCO*. The *ERC* and *MERALCO* subsequently filed separate motions asking the *CA* to reconsider its decision. On January 24, 2005, as a result of the denial by the *CA* of the motions, the *ERC* and *MERALCO* elevated the case to the *Supreme Court*.

In an En Banc Decision promulgated on December 6, 2006, the *Supreme Court* set aside and reversed the *CA* ruling saying that a *COA* audit was not a prerequisite for the determination of a utility's rates. However, while the *Supreme Court* affirmed the *ERC*'s authority in rate-fixing, the *Supreme Court* directed the *ERC* to request the *COA* to undertake a complete audit of the books, records and accounts of *MERALCO*. On January 15, 2007, in compliance with the directive of the *Supreme Court*, the *ERC* requested the *COA* to conduct an audit of the books, records and accounts of *MERALCO* using calendar year 2004 and 2007 as test years.

The *COA* audit, which began in September 2008, was completed in August 2009.

On February 17, 2010, the *ERC* issued its Order directing *MERALCO* and all intervenors in the case to submit within 15 days from receipt their respective comments on the *COA*'s “Report No. 2009-01 Rate Audit Unbundled Charges.”

On July 1, 2011, the *ERC* maintained and affirmed its findings and conclusions in its Order dated March 20, 2003. The *ERC* stated that the *COA* recommendation to apply disallowances under *PBR* to rate unbundling violates the principle against retroactive rate-making. An intervenor group filed its motion for reconsideration. On September 5, 2011, *MERALCO* filed its comment to the intervenor's motion for reconsideration.

On February 4, 2013, the *ERC* denied the intervenor's motion for reconsideration. A petition for Review of the *ERC*'s order was filed by an intervenor group with the *CA*. *MERALCO* is awaiting further action of the *CA* on this matter.

Transition to Performance-Based Regulation or *PBR*

Rate-setting under *PBR* is governed by the *RDWR*. The *PBR* scheme sets tariffs based on the *DU*'s asset base, and the required operating and capital expenditures once every *RP*, to meet a level of operational performance and service level approved by the *ERC*. The *PBR* also employs a mechanism that penalizes or rewards a *DU* depending on its network and service performance.

MERALCO was among the Group A entrants to the *PBR*, together with Dagupan Electric Corporation and Cagayan Electric and Power Company, Inc.

As part of the *PBR*, *MERALCO* implemented payouts to customers for instances where its performance was beyond the guaranteed service levels or *GSL*.

Rate filings and settings are done on a *RP* basis. One *RP* consists of four Regulatory Years or *RYs*. A *RY* for *MERALCO* begins on July 1 and ends on June 30 of the following year. As at December 31, 2013, *MERALCO* is operating in the second half of the third *RY* of the third *RP*. The third *RP* is from July 1, 2011 to June 30, 2015.

CEDC was among the four Group D entrants to the *PBR*. Similar to *MERALCO*, it is subject to operational performance and service level requirements approved by the *ERC*. The second *RP* of *CEDC* began on October 1, 2011 and ends on September 30, 2015.

MAP for RY 2008 and RY 2009

On January 11 and April 1, 2008, *MERALCO* filed separate applications for the approval of its proposed translation of the *MAPs* for *RY 2008* and *RY 2009*, respectively, into different rate schedules for its various customer segments. A portion of the distribution charge under-recoveries as a result of the delay in the implementation of *PBR* was incorporated in the proposed *MAP* for *RY 2009*.

In April 2009, the *ERC* approved the implementation of *MERALCO*'s average distribution rate for *RY 2009* of ₱1.2227 per kWh effective billing period of May 2009. This rate is inclusive of under-recoveries for calendar year 2007 of ₱0.1285 per kWh.

On May 28, 2009, certain electricity consumer groups filed a petition with the *CA* questioning the Decision and Order of the *ERC* on *MERALCO*'s rate translation application for *RY 2008* and *RY 2009*. In a decision dated January 27, 2010, the *CA* denied the Petition. Consequently, the consumer groups brought the case to the *SC*. Comments and responses were filed by both parties with a Manifestation filed by *MERALCO* on January 26, 2011. As at March 17, 2014, the *SC* has yet to render its decision on this case.

MAP for RY 2012

On June 21, 2011, *MERALCO* filed its application for the approval of its *MAP* for RY 2012 and its translation into rate tariffs by customer category. On October 6, 2011, the *ERC* provisionally approved the *MAP* for RY 2012 of ₱1.6012 per kWh and the rate translation per customer class was reflected commencing with the October 2011 customer bills. As at March 17, 2014, hearings for the final approval of the application have been completed and all parties have submitted their respective memoranda. The application is pending approval by the *ERC*.

MAP for RY 2013

On June 11, 2012, the *ERC* provisionally approved the *MAP* for RY 2013 of ₱1.6303 per kWh which was reflected starting with the July 2012 customer bills. Hearings on this case have been completed and *MERALCO* is awaiting the final decision of the *ERC*.

MAP for RY 2014

On June 10, 2013, the *ERC* provisionally approved the *MAP* for RY 2014 of ₱1.6474 per kWh and the rate translation per customer class.

CEDC entry into PBR

In compliance with the *ERC*'s *PBR* rate setting mechanism, *CEDC* filed a reset application for the approval of its *ARR* and *PIS* with the *ERC*. *CEDC* filed its revised application on November 3, 2010, which underwent a series of hearings and public consultations in 2011. The *ERC* issued *CEDC*'s Final Determination on August 5, 2011. Subsequently, *CEDC* filed with the *ERC* its application for RY 2012 Rate Translation into different customer classes.

On April 10, 2012, the *ERC* approved with modification, *CEDC*'s application for the approval of the translation into distribution rates of different customer classes for the first RY of the approved *ARR* under the *PBR* for the RP October 1, 2011 to September 30, 2015. *CEDC* implemented the approved distribution, supply and metering charges of ₱0.8527 per kWh and the new customer segments in its June 2012 billing.

On August 30, 2012, *CEDC* filed its application for the approval of its *MAP* for RY 2013. The *ERC*, on December 17, 2012, approved a *MAP* of ₱0.8953 per kWh. The revised rates based on the approved *MAP* 2013 were implemented by *CEDC* starting January 2013.

Under-recoveries in Pass-Through Costs

Applications for the Recovery of Generation Costs and System Loss or SL, Charges

MERALCO filed separate applications for the full recovery of generation costs, including value-added tax, or *VAT*, incurred for the supply months of August 2006 to May 2007 or total under-recoveries of ₱12,679 million for generation charges and ₱1,295 million for *SL* charges.

The separate applications for the full recovery of generation charges have been approved by the *ERC* in its decisions released on January 18, 2008, September 3, 2008 and August 16, 2010.

With respect to the ₱1,295 million *SL* charge under-recoveries, the *ERC* ordered *MERALCO* to file a separate application for the recovery of *SL* adjustments after the *ERC* confirms the transmission rate to be used in the calculation of the *SL* rate in accordance with the *SL* rate formula of the Automatic Generation Rate Adjustments Guidelines. *MERALCO* has filed the application for recovery of the ₱1,295 million *SL* charge under-recoveries with the *ERC*. This was included in the Consolidated Application to confirm under/over recoveries in generation, transmission, *SL* and lifeline charges filed on March 31, 2011 with the *ERC*. Hearings were completed on October 25, 2011. On December 12, 2011, *MERALCO* filed for the admission of its Supplemental Application. An expository hearing was conducted on February 1, 2012. As at March 17, 2014 the case is awaiting the final resolution of the *ERC*.

Inter-Class Subsidies and Lifeline Subsidies

MERALCO filed separate applications to recover inter-class cross subsidies (on November 14, 2007) and lifeline subsidies (on February 19, 2008).

In a decision dated November 16, 2009, the *ERC* authorized *MERALCO* to recover the inter-class cross subsidy under-recoveries covering the period June 2003 to October 2006 amounting to ₱1,049 million and total lifeline subsidy under-recoveries covering the period June 2003 to December 2007 amounting to ₱856 million.

In December 2009, *MERALCO* implemented the decisions of the *ERC* on the inter-class cross and lifeline subsidies. As at December 31, 2012, the total billed inter-class cross subsidies and lifeline subsidies amounted to ₱963 million and ₱638 million, respectively. The unbilled balance of inter-class cross subsidies is ₱86 million and is expected to be recovered within the next 3 months from January 1, 2013. The balance of lifeline subsidies is ₱218 million and will be billed within the next 13 months from January 1, 2013.

Consolidated Applications for the Confirmation of Over/Under Recoveries of Pass-through Charges

On August 12, 2009, the *ERC* issued Resolution No. 16, Series of 2009, adopting the ***“Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities.”*** These rules govern the recovery of pass-through costs, including over- or under-recoveries with respect to the following bill components: generation charge, transmission charge, *SL* charge, lifeline and interclass rate subsidies, *LFT* and business tax. On October 18, 2010, the *ERC* promulgated *ERC* Resolution No. 21, Series of 2010, amending the system loss true-up formula contained in *ERC* Resolution No. 16, Series of 2009, and setting March 31, 2011 (covering adjustments implemented until the billing month of December 2010) and March 31, 2014 (covering adjustments from January 2011 to December 2013) as the new deadlines for *DUs* in Luzon to file their respective applications. Subsequent filings shall be made every three years thereafter.

On March 31, 2011, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries accumulated from June 2003 to December. Hearings

were conducted and completed by October 25, 2011. On December 8, 2011, *MERALCO* filed an Omnibus Motion praying, among other things, for the admission of the Supplemental Application. In an Order dated December 12, 2011, the *ERC* granted *MERALCO*'s Omnibus Motion and admitted its Supplemental Application. Accordingly, hearings on the Supplemental Application were conducted where *MERALCO* presented additional evidence. *MERALCO* already filed its Formal Offer of Evidence or *FOE*, on September 13, 2012. The consolidated filing included (i) net generation charge under-recoveries of ₱1,000 million, (ii) net transmission charge over-recoveries of ₱111 million, (iii) net lifeline subsidy under-recoveries of ₱9 million and (iv) net *SL* over-recoveries of ₱425 million, excluding any applicable carrying charges.

On July 6, 2012, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries for the calendar year 2011. The consolidated filing includes net generation charge under-recoveries of ₱1,826 million, transmission charge under-recoveries of ₱253 million, net lifeline subsidy under-recoveries of ₱39 million and *SL* over-recoveries of ₱445 million, excluding any applicable carrying charges. Hearings on the application have been terminated and *MERALCO* has submitted its *FOE* on January 25, 2013. As at March 17, 2014, the application is pending approval by the *ERC*.

Deferred PPA

On October 14, 2009, the *ERC* released its findings on *MERALCO*'s implementation of the collection of the approved pass-through cost under-recoveries in 2004. *ERC* directed *MERALCO* to refund ₱268 million of deferred *PPA* transmission line costs related to Quezon Power (Philippines) Limited Company or *QPPL* and deferred accounting adjustments or *DAA* incurred to customers, along with ₱184 million in carrying charges, or an equivalent of ₱0.0169 per kWh. *MERALCO* implemented the refund beginning November 2009 until September 2010. However, the *ERC* has yet to rule on *MERALCO*'s deferred *PPA* under-recoveries of ₱106 million, which does not represent the transmission line fee. As at March 17, 2014, *MERALCO* has filed a Motion for Reconsideration, which is pending decision by the *ERC*.

Application for the Recovery of Local Franchise Taxes or LFT

On March 25, 2011, *MERALCO* filed with the *ERC* an Application for recovery of *LFT* paid but are not yet billed to customers for the period beginning first quarter of 1993 up to the second quarter of 2004 for five provinces, namely: Bulacan, Batangas, Cavite, Laguna and Rizal; and 14 cities, namely: San Jose Del Monte, Batangas, San Pablo, Tagaytay, Lucena, Mandaluyong, Marikina, Quezon, Caloocan, Pasay, Las Piñas, Manila, Pasig and Calamba. The *LFT* is recognized as a legitimate and reasonable *DU* expense in the *ERC*'s Unbundling decision.

In a Decision dated February 27, 2012, the *ERC* released its Order approving with modifications *MERALCO*'s application. The *ERC* approved recovery of *LFT* amounting to ₱1,571 million plus carrying charges of ₱730 million. As directed by the *ERC*, the recovery was reflected as a separate item in the *MERALCO* billing statement to its customers beginning April 2012. As at December 31, 2013, a total of ₱856 million *LFT* and carrying charges have been billed to affected customers.

Revision of SL Caps

On December 8, 2008, the *ERC* promulgated a resolution providing for a lower maximum rate of *SL* (technical and non-technical) that a utility can pass on to its customers. The revised *SL* cap is 8.5% for private utilities, effective January 2010 billing. This is one percentage point lower than the *SL* cap of 9.5% provided under *RA No. 7832*. The actual volume of electricity used by *MERALCO* (administrative loss) is treated as part of the operation and maintenance expense beginning July 2011. The manner by which the utility is rewarded for their efforts in *SL* reduction is addressed by the *ERC* in the *PIS* under *PBR*.

On December 8, 2009, *MERALCO* filed a Petition to amend the said Resolution with an urgent prayer for the immediate suspension of the implementation of the new *SL* cap of 8.5% starting January 2010. The proposed amendment is aimed at making the Resolution consistent with the provisions of *RA No. 9136* and *RA No. 7832*, by increasing the *SL* cap to not less than 9%. The hearing on the Petition was conducted on November 18, 2010. Thereafter, *MERALCO* was directed to submit its *FOE*.

The Petition is awaiting the resolution by the *ERC* as at March 17, 2014.

Benefit Sharing Scheme to Lower SL

Last January 26, 2011, *MERALCO*, together with Private Electric Power Operators Association Inc. or *PEPOA*, and Philippine Rural Electric Cooperative Association or *PHILRECA*, filed a joint petition with the *ERC* to initiate rule-making praying that a resolution be issued adopting the “***Proposed Guidelines for the Implementation of an Incentive Scheme to Lower the System Losses of Private Distribution Utilities and Electric Cooperatives to Level Below the System Loss Cap, for the Benefit of End-Users***”. This was aimed at encouraging the *DUs* to reduce *SL* level below the cap set by the *ERC* and benefit the end-users through lower *SL* charge rates. Public hearings were conducted and completed on June 15, 2011 under *ERC* Case No. 2011-002 RM. The new set of rules will introduce a new bill component “System Loss Savings” to show how much the customers’ savings are as a result of the *DU*’s lowering of its *SL* rate.

On December 11, 2012, the *ERC* posted on its website the second draft of the “***Rules to Govern the Implementation of a Benefit Sharing to Lower the System Losses of Electric Distribution Utilities***”. The salient points of *ERC* draft rules include calculation of *SL* charge using the prevailing *SL* cap or the lowest consecutive five (5)-year average *SL*, whichever is lower, and an equitable sharing (50-50) of incentives between the customer and the *DU* on the savings, which is the difference between the lower of this *SL* level and the *DU*’s actual *SL*. Any *SL* reward from the *PIS* under the *RDWR* for private *DUs* or the “Rules Setting the Electric Cooperatives’ Wheeling Rate” or *RSEC-WR*, shall be offset from the rewards the *DU* will receive from this Benefit-Sharing scheme, except when the net benefit from this scheme is less than the *PIS* rewards of the *DU*, in which case the *DU* will retain the rewards under the *PIS* and forego its share under this Benefit-Sharing Scheme. The foregone share of the *DU* shall be added to the End-user share correspondingly. The implementation of this scheme is dependent on the release of the final set of rules by the *ERC*.

Retail Competition

On February 24, 2012, the Department of Energy or *DOE* issued Department Circular No. DC 2012-02-0002 designating the *PEMC* as the Central Registration Body or *CRB*, under the Retail Competition and Open Access or *RCOA*. The *CRB* is tasked to

develop market infrastructure, systems and processes capable of supporting *RCOA* registration, customer switching and information exchange among industry participants.

On May 9, 2012, the *DOE* issued Department Circular No. DC2012-05-0005, prescribing the general policies for the implementation of *RCOA*. The circular provides the overall direction *DOE* intends to take in developing the policy framework for *RCOA* implementation.

On September 27, 2012, the *DOE* and the *ERC* issued a joint statement setting the initial *RCOA* implementation on December 26, 2012. The joint statement clarified that the *RCOA* commencement is on a phase-in and partial implementation of the program, with the first six (6) months of *RCOA* implementation (December 26, 2012 – June 25, 2013) allotted as the Transition Period to allow all concerned parties to undertake their respective preparations to operationalize the mechanism for *RCOA*. An initial *RCOA* Commercial Operation using an interim information technology or *IT* system will start on June 26, 2013.

On December 17, 2012, the *ERC* issued Resolution No. 16 series of 2012 adopting the Transitory Rules for the implementation of *RCOA*. The resolution provides the detailed responsibilities of industry participants during the *RCOA* transition period.

On January 9, 2013, the *DOE* issued Department Circular, "Promulgating the Retail Rules for the Integration of Retail Competition and Open Access in the Wholesale Electricity Spot Market", to provide rules for the integration of retail competition in the operations and governance processes of the WESM, the management of the transactions of Suppliers and Contestable Customers, and the operations of the Central Registration Body.

On March 26, 2013, *PEMC* began the *RCOA* Trial Operations Program, a nine-week test period participated in by the various entities and service providers of *RCOA*.

On May 6, 2013, the *DOE* issued Department Circular, "Enjoining all Generation Companies, Distribution Utilities, Suppliers and Local Suppliers to Ensure an Effective and Successful Transition towards the Implementation of Retail Competition and Open Access", which required generation companies, suppliers and *DUs* to disclose their supply portfolio and capacity allocation to determine the available energy supply for Contestable Customer in the market. *MERALCO* submitted its first compliance to said Circular on June 7, 2013.

On June 19, 2013, the *ERC* issued a resolution adopting the Supplemental Rules to the Transitory Rules for the implementation of *RCOA*. The resolution seeks to prevent contestable customers who have yet to execute a Retail Supply Contract or *RSC*, with a *RES* from being disconnected or transferred to *SOLR* service upon the commencement of initial commercial operations of *RCOA*. Qualified contestable customers who fail to enter into a *RSC* with a *RES* shall be deemed to stay with their current *DU* until December 26, 2013 or until such time that it is able to find a *RES* provided that they inform the *DU*.

In accordance with the *ERC*'s "Transitory Rules for the Initial Implementation of Open Access and Retail Competition", commercial operations of *RCOA* began on June 26, 2013.

Nineteen *RESs* were licensed by the *ERC* to provide competitive retail supply service to eligible contestable customers. As at December 31, 2013, 287 customers have opted for contestability and are now being supplied by competitive retail electricity suppliers.

On September 4, 2013, the *ERC* conducted a public consultation on its proposed amendments to the *RES Licensing Rules*, for which *MERALCO* submitted comments and participated in the public consultation.

As at December 31, 2013, there are about 782 contestable customers in *MERALCO*'s franchise area and 287 have already switched to their respective *RESs*.

Philippine Export Processing Zone Authority or *PEZA* – *ERC* Jurisdiction

On September 13, 2007, *PEZA* issued “Guidelines in the Registration of Electric Power Generation Facilities/Utilities/Entities Operating inside the Ecozones” and “Guidelines for the Supply of Electric Power in Ecozones” or *Guidelines*. These *Guidelines*, effectively give *PEZA* franchising and regulatory powers in Economic zones or *Ecozones*, operating within the legislative franchise areas of *DUs*, which are under the legislatively authorized regulatory jurisdiction of the *ERC*. The *Guidelines* are the subject of an injunction case filed by the *DUs* at the Regional Trial Court – Pasig Branch or *RTC-Pasig*.

In support of the government's objective of providing lower cost to Ecozone locators, *MERALCO* entered into a Memorandum of Agreement or *MOA*, with *NPC* on September 17, 2007 for the provision of special Ecozone rates to high load factor *PEZA*-accredited industries. The *ERC* authorized the immediate implementation of the Ecozone Rate Program or *ERP*. The *ERP* was initially scheduled to expire by December 25, 2011 but has been extended twice and was terminated as at December 25, 2012.

In January 2013, *MERALCO* entered into a tripartite agreement with *PEZA* and Trans-Asia Oil and Energy Development Corporation for the sale of power to *CEZ* and its locators beginning February 27, 2013.

As an alternative to the Ecozone rate program, *MERALCO* filed an application for the implementation of Peak/Off-Peak or *POP*, Program (formerly known as *MERALCO* Time-Of-Use or *TOU*). On December 17, 2012, the Commission provisionally approved the application and *MERALCO* started implementing the program on February 1, 2013.

Sucat-Araneta-Balintawak Transmission Line

The Sucat-Araneta-Balintawak transmission line is a two-part transmission line, which completed the 230kV-line loop within Metro Manila. The two main parts are the Araneta to Balintawak leg and the Sucat to Araneta leg, which cuts through Dasmariñas Village, Makati City.

On March 10, 2000, certain residents along Tamarind Road, Dasmariñas Village, Makati City or plaintiffs, filed a case against *NPC* with the Regional Trial Court – Makati Branch or *RTC-Makati*, enjoining *NPC* from further installing high voltage cables near the plaintiffs' homes and from energizing and transmitting high voltage electric current through said cables because of the alleged health risks and danger posed by the same. Following its initial status quo Order issued on March 13, 2000, *RTC-Makati* granted on April 3, 2000 the preliminary injunction sought for by the plaintiffs. The decision was affirmed by the *SC* on March 23, 2006, which effectively reversing a decision of the *CA* to the contrary. The *RTC-Makati* subsequently issued a writ of execution based on the order of the *SC*. *MERALCO*, in its capacity as an intervenor, was constrained to file an Omnibus Motion to maintain status quo because of the significant effect of a de-energization of the Sucat-Araneta line to the public and economy. Shutdown of the 230-kV line will result in

widespread and rotating brownouts within *MERALCO*'s franchise area with certain power plants unable to run at their full capacities.

On September 8, 2009, the *RTC-Makati* granted the motions for intervention filed by intervenors *MERALCO* and *NGCP* and dissolved the Writ of Preliminary Injunction issued, upon the posting of the respective counter bonds by defendant *NPC*, intervenors *MERALCO* and *NGCP*, subject to the condition that *NPC* and intervenors pay all damages, which the plaintiffs may incur as a result of the Writ of Preliminary Injunction.

Thereafter, the plaintiffs questioned the *RTC-Makati* order before the CA. As at March 17, 2014, this case remains pending for resolution in the CA.

Moreover, in its Order dated February 5, 2013, the *RTC-Makati* granted plaintiffs' motion and directed the re-raffle of the case to another court after the judicial dispute resolution failed.

Purchase of Subtransmission Assets or STAs

On November 25, 2009, *MERALCO* signed a Contract to Sell with the National Transmission Corporation or *TransCo*, for the sale and purchase of certain subtransmission assets for ₱86 million. On February 25, 2010, the *ERC* approved this Contract to Sell. On June 1, 2012, the *ERC* rendered a decision dated March 6, 2012, approving the sale of the said STAs in favor of *MERALCO* for ₱85 million.

On April 17, 2012, *MERALCO* and *TransCo* filed a joint application for the approval of the Batch 4 contract to sell with the *ERC*. On April 22, 2013, the *ERC* issued a Decision on *MERALCO*'s joint application for the acquisition of the Batch 4 contract to sell. On June 21, 2013, *MERALCO* filed a motion for partial reconsideration regarding the exclusion of certain facilities for acquisition, which has yet to be resolved by the *ERC*.

On December 12, 2011, *MERALCO* signed various agreements for the acquisition of certain sub-transmission assets of *TransCo* within the *MERALCO* franchise area for its sole account, as well as with a consortium with Batangas II Electric Cooperative, Inc., or *BATELEC II* and First Bay Power Corporation or *FBPC*. On September 18, 2012, an amended consortium agreement was executed between *MERALCO* and *FBPC*. On October 17, 2012, *MERALCO* signed two separate amended consortium agreements with *BATELEC II*, and with *FBPC* and *BATELEC II*. These amended consortium agreements superseded the ones signed on December 12, 2011. On December 27 and 28, 2012, the Contract to Sell and Consortium Agreements, respectively, covering these sub-transmission assets were filed with the *ERC* for approval.

Petition for Dispute Resolution

On September 9, 2008, *MERALCO* filed a Petition for Dispute Resolution with the *ERC*, against *PEMC*, *TransCo*, *NPC* and Power Sector Assets and Liabilities Management Corporation or *PSALM* as a result of the congestion in the transmission system of *TransCo* arising from the outages of the San Jose-Tayabas 500kV Line 2 on June 22, 2008, and the 500kV 600 MVA Transformer Bank No.2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The Petition seeks to, among others, direct *PEMC* to adopt the *NPC-TOU* rate or the new price determined through the price substitution methodology of *PEMC* as approved by the *ERC*, as basis for its billing during the period of the congestion and direct *NPC* and *PSALM* to refund the transmission line loss components of the line rentals associated with *NPC/PSALM* bilateral transactions from the start of *WESM* operation on June 26, 2006.

In a Decision dated March 10, 2010, the *ERC* granted *MERALCO*'s petition and ruled that there is double charging of the Transmission Line Cost on *MERALCO* by *NPC* for the Transition Supply Contract or *TSC*, quantities to the extent of 2.98% loss factor, since the start of the *TSC* in November 2006. Thus, *NPC* was directed to refund/collect line rental adjustment to/from *MERALCO*. In the meantime, the *ERC* issued an Order on May 4, 2011 directing *PEMC* to submit an alternative methodology for the segregation of line rental into congestion cost and line losses from the start of the *WESM*. *PEMC* has filed its compliance submitting its alternative methodology

On September 8, 2011, *MERALCO* received a copy of *PEMC*'s compliance to *ERC*'s directive and on November 11, 2011, *MERALCO* filed a counter-proposal which effectively simplifies *PEMC*'s proposal.

On November 11, 2011, *MERALCO* filed its Motion to Implement the Decision dated March 10, 2010 By Immediately Effecting the Refund/Collection of Line Rental Adjustments to Consumers. On December 21, 2011, *PSALM* filed its comment on *MERALCO*'s said Motion. Then, in an Order dated January 24, 2012, the *ERC* directed *PEMC*, *TransCo* and *NPC* to submit their respective comments on *MERALCO*'s motion within five days from receipt.

In an Order of the *ERC* dated June 27, 2012, *MERALCO* was directed to submit its computation of the amount of the double charging of line loss on a per month basis from June 26, 2006 up to the present. On July 4, 2012, *MERALCO* filed its Compliance to the said Order. Thereafter, the *ERC* issued an Order directing the parties to comment on *MERALCO*'s submissions.

In an Order dated March 4, 2013, the *ERC* approved the methodology proposed by *MERALCO* and *PEMC* in computing the double charged amount on line losses by deducting 2.98% from the *NPC-TOU* amount. Accordingly, the *ERC* determined that the computed double charge amount to be collected from *NPC* is ₱5.2 billion, covering the period November 2006 to August 2012 until actual cessation of the collection of the 2.98% line loss charge in the *NPC-TOU* rates imposed on *MERALCO*, while the amount to be collected from the *SGCs* is ₱4.7 billion. Additionally, *MERALCO* was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC* and *Sem-Calaca*, within thirty (30) days from receipt thereof, to recover the line loss collected by them. *MERALCO* filed a motion for clarification with the *ERC* regarding the directives contained in the March 4, 2013 Order. On April 30, 2013 and May 8, 2013, *PSALM* and *NPC*, respectively, filed motions seeking reconsideration of the March 4, 2013 Order.

In an Order dated July 1, 2013, the *ERC* issued the following clarifications/resolutions: 1) *SPPC* should be included as one of the *SGCs* against whom a

petition for dispute resolution should be filed by *MERALCO*; 2) Amount to be refunded by *NPC* is not only ₱5.2 billion but also the subsequent payments it received from *MERALCO* beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates; and Petition to be filed by *MERALCO* against the *SGCs* should not only be for the recovery of the amount of ₱4.7 billion but also the subsequent payments beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates. ; 3) “*SCPC Ilijan*” pertains to *SPPC* instead. Thus, the refundable amount of ₱706 million pertaining to “*SCPC Ilijan*” should be added to *SPPC*’s refundable amount of ₱1.1 billion; 4) Grant the “Motion for Extension” filed by *MERALCO* which was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC*, *Sem-Calaca* and *SPPC*, otherwise, it shall be the one liable to refund the subject amount to its customers; and 5) Deny the respective “Motions for Reconsideration” filed by *NPC* and *PSALM*.

On September 12, 2013, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking approval of its proposal to offset the amount of ₱74 million against some of its monthly remittances to *PSALM*. *PSALM* and *NPC* filed their comments *ad cautelam* on *MERALCO*’s Manifestation and Motion. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion. On November 4, 2013, *MERALCO* filed its Reply. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion.

On October 24, 2013, *MERALCO* received *PSALM*’s Petition for Review on Certiorari with the *CA* (With Urgent *TRO* and/or Writ of Preliminary Mandatory Injunction Applications) questioning the March 4, 2013 and July 1, 2013 Orders of the *ERC*. In a Resolution dated December 29, 2013, the *CA* gave *MERALCO* until December 26, 2013, within which to submit its Comment on the Petition for Review on Certiorari and to show cause why the prayer for the Application for *TRO* and/or Preliminary Injunction should not be granted (“*Comment and Opposition*”). On December 23, 2013, January 5, 2014 and January 15, 2014, *MERALCO* requested for an additional period of ten (10) days each, within which to submit its *Comment and Opposition*.

On February 2, 2014, *MERALCO* filed its Comment to said Petition. As at March 17, 2014, the *CA* has yet to rule on the Petition.

PSALM versus PEMC and MERALCO

Due to the significant increases in *WESM* prices during the 3rd and 4th months of the *WESM* operations, a concern was raised by *MERALCO* with the *PEMC* to investigate whether *WESM* rules were breached or if anti-competitive behavior has occurred.

While resolutions were initially issued by the *PEMC* directing adjustments of *WESM* settlement amounts, a series of exchanges and appeals with the *ERC* ensued. *ERC*’s decision directing the *WESM* settlement price for the 3rd and 4th billing months to be *NPC-TOU* rates, prompted *PSALM* to file a Motion for Reconsideration with the *CA*, which was denied on November 6, 2009. In December 2009, *PSALM* filed a Petition for Review on Certiorari with the *Supreme Court*.

As at March 17, 2014, *PSALM*’s petition for review is pending resolution by the *Supreme Court*.

Petition for Dispute Resolution with NPC on Premium Charges

On June 2, 2009, *MERALCO* filed a Petition for Dispute Resolution against *NPC* and *PSALM* with respect to *NPC*’s imposition of premium charges for the alleged excess energy it supplied to *MERALCO* covering the billing periods May 2005 to June 2006. The

premium charges amounting to ₱315 million during the May-June 2005 billing periods have been paid but are the subject of a protest by *MERALCO*, and premium charges of ₱318 million during the November 2005, February 2006 and April to June 2006 billing periods are being disputed and withheld by *MERALCO*. *MERALCO* believes that there is no basis for the imposition of the premium charges. The hearings on this case have been completed and *MERALCO* is now awaiting the resolution of the *ERC* on the petition.

Supreme Court Temporary Restraining Order on *MERALCO*'s December 2013 Billing Rate Increase

On December 9, 2013, the *ERC* gave clearance to the request of *MERALCO* to implement a staggered collection over three (3) months covering the December 2013 billing month for the increase in generation charge and other bill components such as *VAT*, *LFT*, transmission charge, and *SL* charge, which reflected a total increase of ₱4.15 per *kWh* for a 200-*kWh* residential consumer. The generation costs for the November 2013 supply month increased significantly because of the use of the more expensive liquid fuel by the natural gas-fired power plants that were affected by the Malampaya Gas Field or *Malampaya*, shutdown from November 11 to December 10, 2013. This was compounded by the aberrant spike in the *WESM*, charges on account of the scheduled and extended shutdowns, and the forced outages, of several base load power plants, as well as the non-compliance with *WESM* Rules by certain plants resulting in significant power generation capacities not being offered and dispatched.

The Department of Justice commenced an investigation while the House of Representatives and the Senate conducted separate hearings to determine the underlying reasons for the price increase, including any possible collusion among the power firms. In the meantime, *MERALCO* proceeded with billing its captive customers with the *ERC* approval.

On December 19, 2013, several interest groups filed a Petition against *MERALCO*, *ERC* and the *DOE* before the *SC*, questioning the *ERC* clearance granted to *MERALCO* to charge the ₱4.15 per *kWh* price increase, alleging the lack of hearing and due process. It also sought for the declaration of the unconstitutionality of the *EPIRA*, which essentially declared the generation and supply sectors competitive and open, and not considered public utilities. A similar petition was filed by a consumer group and several private homeowners associations challenging also the legality of the *AGRA* that the *ERC* had promulgated. Both petitions prayed for the issuance of *TRO*, and a Writ of Preliminary Injunction.

On December 23, 2013, the *SC* consolidated the two (2) Petitions and granted the application for *TRO* effective immediately and for a period of sixty (60) days, which effectively enjoined the *ERC* and *MERALCO* from implementing the ₱4.15 per *kWh* price increase. The *SC* also ordered *MERALCO*, *ERC* and *DOE* to file their respective comments to the Petitions and set the hearing for Oral Arguments on January 21, 2014. The *SC* further set two more Oral Arguments on February 4, 2014 and February 11, 2014. After the conclusion of the Oral Arguments, the *SC* ordered all the Parties to the consolidated Petitions to file their respective Memorandum on or before February 26, 2014 after which the Petitions will be deemed submitted for resolution of the *SC*. *MERALCO* complied with said directive and filed its Memorandum on said date.

On February 18, 2014, acting on the motion filed by the Petitioners, the *SC* extended for another period of 60 days or until April 22, 2014, the *TRO* that it originally issued against *MERALCO* and *ERC* last December 23, 2013. The *TRO* was also similarly applied to the generating companies, specifically *MPPCL*, *SMEC*, *SPPC*, *FGPC*, and the *NGCP*, and the *PEMC* (the administrator of *WESM* and market operator) who were all

enjoined from collecting from *MERALCO* the deferred amounts representing the ₱4.15 per *kWh* price increase for the November 2013 supply month.

In the meantime, on January 30, 2014, *MERALCO* filed an Omnibus Motion with Manifestation with the *ERC* for the latter to direct *PEMC* to conduct a re-run or re-calculation of the *WESM* prices for the supply months of November to December 2013. Subsequently, on February 17, 2014, *MERALCO* filed with the *ERC* an Application for the recovery of deferred generation costs for the December 2013 supply month praying that it be allowed to recover the same over a six (6)-month period.

On March 3, 2014, the *ERC* issued an Order voiding the Luzon *WESM* prices given that the prices in *WESM* during the November and December 2013 supply months could not qualify as reasonable, rational and competitive. *PEMC* was given seven (7) days upon receipt of the Order to calculate these regulated prices and implement the same in the revised *WESM* bills of the concerned.

As at March 17, 2014, *MERALCO* is still awaiting decisions of the *Supreme Court* on the *TRO*.

Feed-in-Tariff or *FIT*

Pursuant to *RA* No. 9513, or the Renewable Energy Act of 2008 or *RE Act*, the issued Resolution No. 16, Series of 2010, “Adopting the Feed-in-Tariff Rules”, on July 23, 2010. As defined, the *FIT* system offers a guaranteed payment on a fixed rate per *kWh* for electricity from wind, solar, ocean, hydropower and biomass energy sources under the renewable energy policy.

On May 16, 2011, pursuant to the *FIT* Rules, the National Renewable Energy Board or *NREB* filed its “Petition to Initiate Rule Making for the Adoption of Feed-in-Tariff”. The Petition proposed a specific *FIT* rate for each emerging renewable resource. After undergoing several public consultations and public hearings, on July 27, 2012, the *ERC* approved the *FIT* rates, which were to be applied. Such rates were lower than the rates applied by the *NREB*. The *ERC* also decided to defer approving a *FIT* rate for ocean-sourced energy to allow further study and more extensive data gathering.

To fund the *FIT* payments to eligible *RE* developers, a *FIT* allowance charge shall be imposed on all end-users. The *FIT* allowance shall be established by the *ERC* upon petition by *TransCo*, which had been designated as the *FIT* Fund Administrator. Similar to *NREB*’s *FIT* Rate Petition, the *FIT* Allowance Petition shall go through public hearings and consultations.

To supplement the *FIT* Rules, the *ERC* is currently drafting the “*FIT* Allowance Payment and Collection Guidelines”. This set of guidelines will govern how the *FIT* Allowance shall be calculated using the formulae provided. It will also outline the process of billing and collecting the *FIT* Allowance from the electricity consumers, the remittance to a specified fund, the disbursement from the *FIT* Allowance Fund and the payment to eligible *RE* developers. The draft is currently undergoing public consultation.

Net Metering Program

The Renewable Energy or *RE Act* mandates the *DUs* to provide the mechanism for the “physical connection and commercial arrangements necessary to ensure the success of the *RE* programs”, specifically the Net Metering Program. The *RE Act* defines Net Metering as “a system, appropriate for distributed generation, in which a distribution grid

user has a two-way connection to the grid and is only charged for his net electricity consumption and is credited for any overall contribution to the electricity grid". By their nature, net metering installations will be small (less than 100 kW) and will likely be adopted by the households and small business end-users of *DUs*.

On September 4, 2012, the *ERC* released the first draft of the Proposed Net Metering Rules. The proposed rules will govern the implementation of the Net Metering program for *RE* sources. It also seeks to establish the standards for interconnecting these *RE* sources to the *DUs*' systems. The pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. Meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. On September 21, 2012, the *ERC* conducted the first public consultation on the proposed rules.

After consultations with stakeholders, the *ERC* issued on July 3, 2013 its Resolution No. 09, Series of 2013, entitled, "A Resolution Adopting the Rules enabling the Net Metering Program for Renewable Energy". The rules will govern the *DUs*' implementation of the Net Metering program. Included in Rules are the Interconnection Standards that shall provide technical guidance to address engineering, electric system reliability, and safety concerns for net metering interconnections. The final pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. In the meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. The rules took effect on July 24, 2013. *MERALCO* started accepting net metering applications on the same day. As at March 17, 2014, *MERALCO* has already energized five Net Metering customers, the country's first participants to the net metering program.

Costs and Effects of Compliance with Environmental Laws

Compliance with environmental laws is part of *MERALCO*'s good governance, which enhances its relationships with environmental groups. Specific programs such as solid waste management, water conservation, air pollution control, and wastewater management have been implemented by *MERALCO* to ensure compliance with environmental laws and preservation of the natural resources within its franchise area. *MERALCO* has incurred a total amount of ₱700,000 representing renewal and application of permits for new or expansion projects; ₱9.36 million for the maintenance of Sewage Treatment Plants or *STPs* and ₱300,000 for solid waste collection and disposal.

Government Approval and Regulation

MERALCO is subject to regulation by the *ERC* and recognizes the rate-making policies of the *ERC*.

HUMAN RESOURCES PROFILE

Number of Employees

As at December 31, 2013, *MERALCO* has a total of 5,898 regular employees representing a reduction of 62 or 1% from the 2012 count of 5,960. This reduction in employee count is attributed to *MERALCO*'s continuing efforts to optimize its workforce through organizational restructuring and optimization programs, thereby, enhancing synergies across operating units and strengthening workforce capabilities.

The table below presents the manpower complement of *MERALCO*:

BUSINESS GROUP	Regular Employee Count		% Increase (Decrease)
	2013	2012	
Networks	3,289	3,333	(1.3%)
Customer Retail Services	1,657	1,639	1.1%
Shared Services	952	988	(3.6%)
TOTAL	5,898	5,960	1.0%

Of the total employee population, 10% is in management positions while the remaining 90% perform various tasks in professional, technical, office operations, administrative and skilled trade roles. Following is the distribution per classification.

Employee and Labor Relations

MERALCO and the Meralco Employees and Workers Association or *MEWA*, the official Collective Bargaining Representative of the Rank and File Employees, concluded their collective bargaining negotiations, and signed the agreement on December 12, 2013.

On September 12, 2013, *MERALCO* won the Asian Human Capital Award (AHCA). Meralco was recognized for its impactful and innovative people practices demonstrated through highly engaged workforce, a customer-centric culture and a strong sense of innovation, empowerment and performance. The AHCA is a prestigious, international recognition conferred by the Singapore Ministry of Manpower, Human Capital Leadership Institute, INSEAD and CNBC Asia. Meralco bagged the 2013 AHCA vied for by 89 entries from 58 reputable organizations across 11 Asian Countries.

Meralco also won the 2013 Philippine Quill Company of the Year Award and received 16 Awards of Excellence and 19 Awards of Merit.

Item 2. Properties

MERALCO's assets include utility plant assets, which are part of the regulatory asset base or *RAB*. *RAB* consists of electric capital assets and non-electric capital assets. In addition, *MERALCO* also hold non-*RAB* consisting of assets held for future substation or branch sites or retired office or sector sites, which are recognized as "Investment Properties" in the statements of financial position.

MERALCO's facilities in Pasig City host the networks system, which is the heart of the electric distribution operations, the telecommunications and trunk radio system, logistics process, Customer Retail Services and other support services organizations.

As at December 31, 2013, in addition to the head office, *MERALCO* has 10 networks sector offices, 30 branches and 7 auxiliary offices, 14 extension offices, 3 payment offices and 1 customer assistance office. Its network facilities consist of 113 substations (total capacity of 16,213.59 MVA), 858 circuits (total of 17,207.61 circuit-kms.) and 162,031 distribution transformers in service,

Separately, *CEDC*'s facilities consist of subtransmission and distribution assets and buildings and improvements located in *CSEZ*. *CEDC*'s distribution facilities include three (3) substations with a total capacity of 131MVA and 1,370 distribution transformers.

Its distribution network consists of 130.75 circuit-km linear length of primary lines and 56.17 km of secondary lines.

MGen, through its subsidiaries, *CAPC* and *Atimonan*, own several parcels of land for the development of a peaking plant (in Calamba, Laguna) and a Liquefied Natural Gas or *LNG*, plant (in Atimonan, Quezon), respectively.

Radius, *MERALCO*'s telecommunications subsidiary owns 2,000 kilometers of fiber optic cables and telecommunications infrastructure.

CIS-Bayad Center has 123 leased branches for its bills payment, e-purse loading and remittance services.

For more information on these properties, see *Note 8 – Utility Plant and Others* to the accompanying audited consolidated financial statements in Item 7.

The properties of the *DUs* (*MERALCO* and *CEDC*) are located within the franchise area to efficiently serve the customers. In our opinion, these properties are in good condition, except for ordinary wear and tear, and are adequately insured.

The properties of *MERALCO* and its subsidiaries are free from any mortgage, charge, pledge, lien or encumbrance.

The *MERALCO* Group also has various lease contracts as lessee for periods ranging from one year to 30 years covering certain office spaces, payment offices and substation sites and towers.

Item 3. Legal Proceedings

In accordance with the Securities Regulation Code Implementing Rules and Regulations or *SRC-IRR*, the following are the material legal proceedings to which *MERALCO* or its subsidiaries is a party, or to which any of their property is a subject, including pending claims for damages against the registrant exceeding 10% of its current assets:

1. In the matter of the Joint Application for Approval of the Settlement Agreement between Manila Electric Company and National Power Corporation, with Prayer for Provisional Authority, National Power Corporation and Manila Electric Company, Applicants

ERC Case No. 2004-109

(Filed by NPC and *MERALCO* on April 15, 2004)

This is a joint application filed by *MERALCO* and *NPC* for the approval of their Settlement Agreement, which resolved their dispute concerning a ten (10) year Contract for Supply of Electricity or *CSE*.

Under the Settlement Agreement, *MERALCO* was compensated by *NPC* for the losses incurred by the former due to *NPC*'s act of serving directly connected customers, which is in violation of *MERALCO*'s franchise rights, and for transmission line delays affecting *MERALCO*'s Independent Power Producers or *IPPs*. On the other hand, *MERALCO* shall pay *NPC* the net settlement amount of ₱14,320 million, representing *NPC*'s minimum charges corresponding to the fixed costs it incurred for the period 2002-

2004. Variable costs, such as fuel and similar operating expenses that were not incurred by NPC, were not included in the minimum charge computation.

The proceedings in this case are currently suspended pursuant to the ERC Order dated September 14, 2009 upon motion of MERALCO in order to obtain ruling from a regular court on issues raised by the Office of the Solicitor General or OSG, which are outside the jurisdiction of the ERC.

MERALCO v. NPC, Power Sector Assets and Liabilities Management Corporation, and the Republic of the Philippines, represented by the Office of the Solicitor General.

S.C.A. Case No. 3392, RTC – Pasig City, Branch 71
(Filed on November 23, 2009)

In connection with the Settlement Agreement between MERALCO and NPC, MERALCO filed a petition seeking the declaration by the court that said Settlement Agreement, independent of the pass-through provision, which is reserved for approval by the ERC, is valid and binding.

The RTC – Pasig rendered a Decision dated May 29, 2012 declaring the Settlement Agreement, independent of the pass-through provision, which is reserved for ERC approval, valid and binding. The OSG filed a Notice of Appeal and, in an Order dated June 28, 2012, the RTC-Pasig forwarded the records to the CA for appeal proceedings.

MERALCO v. NPC, Power Sector Assets and Liabilities Management Corporation (PSALM), and the Republic of the Philippines, represented by the Office of the Solicitor General.

CA-GR CV No. 99110, Court of Appeals

This is an appeal filed by the OSG questioning the RTC – Pasig Decision dated May 29, 2012, which declared the Settlement Agreement valid and binding. In a Notice dated October 16, 2012, the CA required the OSG to file its appeal brief. Acting on a motion for extension filed by the OSG, the CA, in a Resolution dated December 20, 2012, granted the OSG the maximum extension of ninety (90) days, or until March 20, 2012 within which to file its appeal brief. . *Both parties have submitted their respective appeal briefs. The matter is now submitted for the resolution of the CA.*

Republic of the Philippines, represented by the Office of the Solicitor General v. Hon. Franco T. Falcon, in his capacity as the Presiding Judge of Branch 71 Regional Trial Court (RTC), National Capital Judicial Region, Pasig City, Manila Electric Company (MERALCO) and National Power Corporation (NPC).

CA-GR SP No. 116863, Court of Appeals

Republic of the Philippines v. Manila Electric Company (MERALCO) and National Power Corporation (NPC).

GR No. 201715, Supreme Court

This is a Petition for Certiorari, prohibition and mandamus with the CA filed by the OSG on November 22, 2010 due to the denial of its motions to dismiss or to stay the proceedings, and for deferral of the pre-trial conference and referral of the case to

arbitration or S.C.A. Case No. 3392.

In a Decision dated 14 October 2011, the CA denied the petition holding that the trial court did not err in finding the OSG in default due to its failure to participate in the proceedings. The appellate court ordered the trial court to proceed with dispatch in hearing the case *ex-parte*, as against the OSG. The OSG filed a motion for reconsideration, which was denied by the CA in a Resolution dated April 25, 2012.

The OSG appealed the CA decision with the *Supreme Court*. *MERALCO* filed its Comment on October 29, 2012. *NPC* likewise filed its Comment to the Petition.

In a Decision dated December 11, 2013, the First Division of the *Supreme Court* denied the Petition for Review on Certiorari by the OSG and affirmed the decision promulgated by the CA on October 14, 2011 in C.A.-G.R. SP No. 116863.

2. In The Matter of the Application for the Approval of the Unbundled Rates Pursuant to the Provision of Republic Act No. 9136, Manila Electric Company, Applicant.
ERC Case No. 2001-900 RC
(Filed on October 30, 2001)

In connection with the decision of the *Supreme Court* in G.R. Nos. 166769 and 166818, where the *ERC* was directed to request the *COA* to undertake a complete audit of the books, records and accounts of *MERALCO*, the *COA* submitted its Report No. 2009-01 on the Rate Audit of the Unbundled Charges of *MERALCO* for Calendar Years 2004 to 2007 to the *ERC*.

In an Order dated June 21, 2011, the *ERC*, acting on the *COA* Audit, resolved to maintain and affirm its findings and conclusions in its Decision dated March 20, 2003 and Order dated May 20, 2003 in the original unbundling case.

National Association of Electricity Consumers for Reforms or *NASECORE*, filed its motion for reconsideration of the Order, which was opposed by *MERALCO*. In an Order dated February 4, 2013, the *ERC* denied *NASECORE*'s motion for reconsideration for lack of merit.

National Association of Electricity Consumers for Reforms, Inc. (NASECORE) v. Energy Regulatory Commission and Manila Electric Company
C.A.-G.R. SP No. 129052
(Petition dated April 2, 2013)

NASECORE filed a Petition for Review before the CA questioning the June 21, 2011 and February 4, 2013 Orders of the *ERC*. *MERALCO* is awaiting further action of the CA on this matter.

3. In the Matter of the Application for Refund of Overcharge (sic) Distribution Rates in the Residential Rates of ₱39 Billion in 2004-2007.

ERC Case No. 2008-092 CC
(Filed by the Applicant on July 15, 2008)

This application was filed against *MERALCO* by customer Genaro C. Lualhati, seeking the refund to residential consumers a total of P39 billion on the ground that *MERALCO* allegedly overcharged its distribution costs (distribution, metering, supply and systems loss charges) for the period of 2004-2007. The parties filed their respective Memoranda on October 24, 2008. On August 23, 2010, the *ERC* has issued a Decision dismissing the case. Mr. Lualhati filed a motion for reconsideration which is pending resolution.

4. Leonard S. De Vera (Equal Justice For All Movement), et al., vs. MERALCO, NPC and ERC.

Civil Case No. 08-484, RTC Makati, Branch 134
(Filed by the plaintiffs on June 25, 2008)

C.A. GR CV No. 95198, Court of Appeals (CA)

This is a class suit filed with the RTC by a group of *MERALCO* customers for accounting and refund of all *SL* charges, meter deposits, income taxes and other charges and assessments allegedly illegally collected and passed-on to customers.

The case was dismissed by the *RTC* in an Order dated May 14, 2009. A motion for reconsideration was filed by the plaintiffs but the same was denied in an Order dated April 16, 2012. Plaintiffs appealed the case to the *CA* and in a Decision dated November 15, 2012, the *CA* denied the appeal, and affirmed the *RTC* Orders. Plaintiffs have filed a motion for reconsideration of the *CA* Decision. *MERALCO* and *NPC* have filed their respective comments to the motion for reconsideration. In a Resolution dated April 8, 2013, the *CA* denied the motion for reconsideration.

5. In the matter of the Application to Implement MERALCO's PBR rates for Regulatory Years 2008 and 2009, under the ERC's Performance Based Regulation.

ERC Case Nos. 2008-004-RC and 2008-018-RC
(Filed on January 11 and April 1, 2008)

NASECORE, FOVA and FOLVA v. ERC and MERALCO.

C.A. GR SP No. 108663, Court of Appeals
(Filed by petitioners on May 28, 2009)

NASECORE, FOVA and FOLVA v. ERC and MERALCO.

G.R. No. 191150, Supreme Court
(Filed by petitioners on March 26, 2010)

On January 11 and April 1, 2008, *MERALCO* filed separate applications for the approval of its proposed translation of the Maximum Average Price or *MAP* for *RYs* 2008 and 2009, respectively, into different rate schedules for *MERALCO's* various customer segments. On October 17, 2008, the *ERC* released its consolidated Decision on the applications. To avoid price shocks and mitigate the rate impact on end-users, the *ERC*

subjected the proposed rate to side constraints and approved a *MAP* for the regulatory year 2009 of only ₱1.2280 per kWh. The *ERC*'s Decision also directed *MERALCO* to implement its approved distribution, supply and metering charges starting July 1, 2008.

The CA, in a Decision dated January 29, 2010, upheld the *ERC* decision. However, *NASECORE* and the other consumer groups elevated the case to the *Supreme Court*. *MERALCO* filed its comment on the petition and the case is awaiting the decision of the SC.

6. In the Matter of the Application for Approval of: a) *MAP* for RY 2012; and b) Translation of the *MAP* for RY 2012 into a Distribution Rate Structure for *MERALCO*'s Various Customer Classes, with Prayer for the Issuance of a Provisional Authority, Manila Electric Company (*MERALCO*), Applicant.

ERC Case No. 2011-088 RC
(Filed on June 21, 2011)

This is *MERALCO*'s application for the verification of its *MAP* for RY 2012 and its translation into tariffs by customer category. In an Order dated 3 October 2011, the *ERC* provisionally granted *MERALCO*'s proposed *MAP* of ₱1.6012 and rate structure. *MERALCO* started implementing the provisionally approved *MAP* 2012 in the October 2011 billing month. *MERALCO* has completed the presentation of its evidence and the parties have submitted their respective memoranda.

7. In the Matter of the Application for Approval of: a) *MAP* for RY 2013; and b) Translation of the *MAP* for RY 2013 into a Distribution Rate Structure for *MERALCO*'s Various Customer Classes, with Prayer for the Issuance of a Provisional Authority, Manila Electric Company (*MERALCO*), Applicant.

ERC Case No. 2012 - 054 RC
(Filed on March 29, 2012)

This is *MERALCO*'s application for the verification of its *MAP* for RY 2013 and its translation into tariffs by customer category.

On March 29, 2012, *MERALCO* filed an application for the verification of its *MAP* for RY2013 of ₱1.6333 per kWh and its translation into tariffs by customer category. The public hearings started on May 24, 2012. On June 11, 2012, the *ERC* released an Order provisionally approving a *MAP* for RY 2013 of ₱1.6303 per kWh which was reflected starting with the July 2012 customer bills. Hearings on this case have been completed and *MERALCO* is awaiting the final decision of the *ERC*.

8. In the Matter of the Application for Approval of the Annual Revenue Requirement and Performance Incentive Scheme for the Third Regulatory Period (2011 to 2015) in Accordance with the Provisions of the Rules for Setting Distribution Wheeling Rates (RDWR) as amended, Manila Electric Company (*MERALCO*), Applicant.

ERC Case No. 2010-069 RC
(Filed on June 18, 2010)

On June 18, 2010, *MERALCO* filed an application for the approval of its proposed *ARR* and *PIS* for the Third *RP* (July 1, 2011- June 15, 2015). On June 6, 2011, the *ERC* rendered its Final Determination on *MERALCO*'s application approving the *MAP* of ₱1.5828 per kWh, ₱1.5824 per kWh, ₱1.5821 per kWh, and ₱1.5817 per kWh for the *RYs* 2012, 2013, 2014 and 2015, respectively.

Several intervenors filed motions for reconsideration, which were denied by the *ERC* in an Order dated October 3, 2011. The said Order has since become final and executory. Only one of the intervenors, Uriel G. Borja, filed a petition with the *CA* claiming that grave abuse of discretion attended the issuance of the Final Determination. In a Resolution dated 03 February 2012 the appellate court dismissed the petition on the ground that Mr. Borja availed of the wrong remedy and the petition was filed out of time. Mr. Borja filed a motion for reconsideration which was similarly denied by the *CA* in a Resolution dated June 28, 2012.

Mr. Borja appealed the *CA* Resolutions to the *Supreme Court* but the same was denied in a Resolution dated August 29, 2012, for failure to show any reversible error. The judgment of the *Supreme Court* is now final and executory and an entry of judgment has been made.

9. In the Matter of the Resolution Issued by the Board of Directors of the Philippine Electricity Market Corporation (PEMC) Directing the Adjustment of Settlement Prices in the Wholesale Electricity Spot Market, PSALM v. PEMC and MERALCO

G.R. No. 190119

Supreme Court

(Petition dated November 25, 2009; Received by the Company on December 4, 2009)

This is a petition filed by *PSALM* with the *Supreme Court* appealing the Decision dated August 28, 2009 of the *CA* in C.A. G.R. SP No. 106322, which affirmed the Decision dated January 30, 2008 of the *ERC* setting the *WESM* settlement prices for the third and fourth billing periods at the *ERC*-approved *NPC-TOU* rates. With filing of *MERALCO*'s comment, the petition is now ripe for decision by the *Supreme Court*.

It may be recalled that in a Decision dated August 14, 2007, the *ERC* confirmed its December 13, 2006 Order and declared as invalid the action of the Board of *PEMC* in adjusting the *WESM* settlement prices for having been carried out beyond the scope of its authority and in violation of the *EPIRA* and the *WESM* Rules. The *ERC* further directed the implementation and adjustment of the *WESM* settlement prices for the 3rd and 4th billing periods and allowed *PEMC* to institute adjustments in its billing and settlement process to mitigate the impact of said Decision upon the *WESM* members. *MERALCO*, however, moved for a reconsideration of the Decision due to its impact on customers. It argued that the use of *WESM* settlement prices would result in additional imposition of P6.00 per kWh and translate to an increase in the generation charge by about P0.90 and P2.05 per kWh, for the supply months of September 2006 and October 2006, respectively. On January 30, 2008, the *ERC* rendered its Decision granting *MERALCO*'s motion and set the *WESM* settlement prices for the subject billing periods at the *ERC*-approved *NPC-TOU* rates.

ERC's decision directing the *WESM* settlement price for the 3rd and 4th billing months to be *NPC-TOU* rates prompted *PSALM* to file a Petition with the *CA*, which was denied on November 6, 2009. In December 2009, *PSALM* filed a Petition for Review on Certiorari with the *Supreme Court* where the petition is pending resolution.

10. In Re Petition for Dispute Resolution. Manila Electric Company v. Philippine Electricity Market Corporation, National Transmission Corporation, National Power Corporation and Power Sector Assets and Liabilities Management

ERC Case No. 2008-083 MC

(Filed on September 9, 2008)

This is a petition filed by *MERALCO* for dispute resolution against *PEMC*, *TransCo*, *NPC* and *PSALM* as a result of the congestion in the transmission system of *TransCo* arising from the outage of the San Jose-Tayabas 500kV Line 2 on June 22, 2008, followed by the outage of the 500kV 600 MVA Transformer Bank #2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The petition seeks, among others, to direct *NPC* and *PSALM* to refund the transmission line loss components of the line rentals associated with *NPC/PSALM* bilateral transactions from the start of *WESM* operation on June 26, 2006.

In a Decision dated March 10, 2010, the *ERC* granted *MERALCO*'s petition and ruled that there is double charging of the Transmission Line Cost on *MERALCO* by *NPC* for the *TSC* quantities to the extent of 2.98% loss factor, since the start of the *TSC* in November 2006. Thus, *NPC* was directed to refund/collect line rental adjustment to/from *MERALCO*. In the meantime, the *ERC* issued an Order on May 4, 2011 directing *PEMC* to submit an alternative methodology for the segregation of line rental into congestion cost and line losses from the start of the *WESM*, which *PEMC* has complied with.

On November 11, 2011, *MERALCO* filed its motion to implement the Decision dated 10 March 2010, to which *PEMC* and *PSALM* have filed their comments. *MERALCO* is awaiting the *ERC*'s resolution of this matter.

In an Order of the *ERC* dated June 21, 2012, *MERALCO* was directed to submit its computation of the amount of the double charging of line loss on a per month basis from June 26, 2006 up to the present. On July 4, 2012, *MERALCO* filed its Compliance to the said Order. Thereafter, the *ERC* issued an Order directing the parties to comment on *MERALCO*'s submissions.

In an Order dated March 4, 2013, the *ERC* approved the methodology proposed by *MERALCO* and *PEMC* in computing the double charged amount on line losses by deducting 2.98% from the *NPC-TOU* amount. Accordingly, the *ERC* determined that the computed double charge amount to be collected from *NPC* is ₱5.2 billion, covering the period November 2006 to August 2012 until actual cessation of the collection of the 2.98% line loss charge in the *NPC-TOU* rates imposed on *MERALCO*, while the amount to be collected from the Successor Generating Companies or *SGCs* is ₱4.7 billion. Additionally, *MERALCO* was directed to file a petition against the following *SGCs*: *MPPCL APRI*, *TLI*, *SMEC* and *Sem-Calaca*, within thirty (30) days from receipt thereof, to recover the line loss collected by them. *MERALCO* filed a motion for clarification with the *ERC* regarding the directives contained in the March 4, 2013 Order. On April 30, 2013 and May 8, 2013, *PSALM* and *NPC*, respectively, filed motions seeking reconsideration of the March 4, 2013 Order.

In an Order dated July 1, 2013, the *ERC* issued the following clarifications/resolutions: 1) *SPPC* should be included as one of the *SGCs* against whom a petition for dispute resolution should be filed by *MERALCO*; 2) Amount to be refunded by *NPC* is not only ₱5.2 billion but also the subsequent payments it received from *MERALCO*

beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates and Petition to be filed by *MERALCO* against the *SGCs* should not only be for the recovery of the amount of ₱4.7 billion but also the subsequent payments beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates; 3) "SCPC Ilijan" pertains to *SPPC* instead. Thus, the refundable amount of ₱706 million pertaining to "SCPC Ilijan" should be added to *SPPC*'s refundable amount of ₱1.1 billion; 4) Grant the "Motion for Extension" filed by *MERALCO* and was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC*, *Sem-Calaca* and *SPPC*, otherwise, it shall be the one liable to refund the subject amount to its customers; and 5) deny the respective "Motions for Reconsideration" filed by *NPC* and *PSALM*.

On September 12, 2013, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking approval of its proposal to offset the amount of ₱74 million against some of its monthly remittances to *PSALM*. *PSALM* and *NPC* filed their comment *ad cautelam* on *MERALCO*'s Manifestation and Motion. On November 4, 2013, *MERALCO* filed its Reply. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion.

PSALM vs. ERC, MERALCO and PEMC

CA GR. SP. No. 132446

On October 24, 2013, *MERALCO* received *PSALM*'s Petition for Certiorari with the Court of Appeals (With Urgent Temporary Restraining Order and/or Writ of Preliminary Mandatory Injunction Applications) to question the March 4, 2013 and July 1, 2013 Orders of the *ERC*. In a Resolution dated December 29, 2013, the CA gave *MERALCO* until December 26, 2013, within which to submit its *Comment* on the *Petition for Certiorari* and to show cause why the prayer for the Application for Temporary Restraining Order and/or Preliminary Injunction should not be granted ("Comment and Opposition"). On December 23, 2013, January 5, 2014 and January 15, 2014, *MERALCO* requested for an additional period of ten (10) days each, within which to submit its *Comment and Opposition*.

On February 2, 2014, *MERALCO* filed its Comment to said Petition. The CA has yet to rule on the Petition.

Petition for Dispute Resolution against SPPC, MPPCL, APRI, TLI, SMEC and Sem-Calaca

ERC Case No. 2013-077RC

On August 29, 2013, *MERALCO* filed a Petition for Dispute Resolution against *SPPC*, *MPPCL*, *APRI*, *TLI*, *SMEC* and *Sem-Calaca*. Said Petition seeks the following: 1) Refund of the 2.98% transmission line losses in the amount of ₱5.4 from said *SGCs*; and 2) approval of *MERALCO*'s proposal to correspondingly refund to its customers the aforementioned line loss amounts, as and when the same are received from the *SGCs*, until such time that the said over-recoveries are fully refunded, by way of automatic deduction of the amount of refund to the computed monthly generation rate. On September 20, 2013, *MERALCO* received the *SGCs*' Joint Motion to Dismiss. On October 7, 2013, *MERALCO* filed its Comment on the said Joint Motion. On October 8, 2013, *MERALCO* received the *SGCs* Manifestation and Motion. On October 14, 2013, *MERALCO* filed its *Opposition* thereto. On 24 October 2013, *MERALCO* received the *SGC*'s Reply to its Comment. On October 29, 2013, *MERALCO* filed its Rejoinder.

MERALCO is awaiting the *ERC*'s resolution of the *SGCs*' Joint Motion.

**11. Bayan Muna Representatives Neri Javier Colmenares and Carlos Isagani v. ERC
NASECORE, et. al. v. MERALCO and ERC
SC G.R. Nos. 210245 and 210255
Filed: December 19, 2013**

On December 19, 2013, several party-list representatives in Congress filed a Petition docketed as G.R. 210245 before the SC questioning the *ERC*'s approval of *MERALCO*'s proposed staggered recovery of the increase in generation charge for the November 2013 supply month, allegedly for lack of due process. The increase in the generation charge was from ₱5.6673/kWh in the November 2013 billing to ₱9.1070/kWh for the December 2013 billing which *MERALCO* proposed to recover in 3 tranches. A similar Petition was filed on December 20, 2013 challenging *MERALCO*'s automatic rate adjustments and increases, also allegedly for lack of due process. This Petition was docketed as G.R. 210255. Both Petitions prayed for the issuance of Temporary Restraining Order or *TRO* and Writ of Preliminary Injunction pending resolution of the case.

In December 23, 2013, the *Supreme Court* issued an Order consolidating the two Petitions and granting the application for *TRO* effective immediately and, for a period of sixty (60) days, enjoining (1) *ERC*, its agents, representatives, or persons acting in its place and stead, from implementing its December 9, 2013 Order and acting further on the letter – request of *MERALCO* dated December 5, 2013; and (2) *MERALCO*, its agents, representatives, or persons acting in its place and stead, from increasing the rates it charges to its consumers based on the matters it raised in its 5 December 2013 letter. Said Order likewise set the cases for oral arguments on January 21, 2014 and required respondents *ERC* and *MERALCO* to file their respective Comments on the cases. On January 8, 2014, *MERALCO* filed its Consolidated Comment/Opposition with Counter-Petition.

On January 2, 2014, the Office of the Solicitor General or OSG, filed a Manifestation with Motion praying that it be excused from filing a comment on behalf of *ERC* and *DOE*. In keeping with the spirit and intent of the SC, *MERALCO* maintained the pass-through charges at the November 2013 billing level for its January 2014 billing to customers.

On January 9, 2014, *MERALCO* received copies of the *ERC*'s Comment and the *PEPOA* Comment-in-Intervention. On even date, *MERALCO* received an Order from the SC which directed the Petitioners in said case to implead the Philippine Electricity Market Corporation or *PEMC*, and [some] Suppliers with whom *MERALCO* has existing Power Supply Agreements or *PSAs*, namely, *SEM-Calaca*, *Masinloc Power Partners Co. Ltd.*, *Therma Luzon Inc.*, *San Miguel Energy Corp.*, *South Premiere Power Corporation*, and *Therma Mobile, Inc.*, as necessary parties to the case. Consequently, these additional respondents were required (i) to file their respective Comments on the Petitions no later than January 20, 2014 and (ii) to attend the preliminary conference set on January 13, 2014, or to file, on or before 10 January 2014, the necessary manifestation should they desire to waive their right to participate in the scheduled oral arguments on January 21, 2014. Incidentally, the *Supreme Court* also denied in said Order the OSG's motion to be excused from filing Comment/s in behalf of the *ERC* and *DOE*. Accordingly, it was directed to file the necessary Comment/s and attend the preliminary conference.

On January 10, 2014, *MERALCO* received a related Petition for Certiorari, Prohibition and Mandamus filed before the SC by Rep. Hicap (Anak Pawis), et. al., docketed

as G.R. No. 210334.

On January 15, 2014, the *Supreme Court* issued an Advisory, which identified the issues, and outlined the procedure, for the oral arguments in G.R. Nos. 201245 & 210255 on January 21, 2014. The *Supreme Court* likewise acknowledged therein that the issues may involve technical matters, thus, it directed the *DOE* Secretary, the Chairman of *ERC* and the President of *PEMC* to serve as resource persons for technical questions.

On January 20, 2014, *MERALCO* received GN Power Mariveles Coal Plant Ltd. Co.'s or *GMCP*, National Grid Corporation of the Philippines' or *NGCP*, and *PEMC*'s Comments in the *Supreme Court* cases.

On January 21, 2014, *MERALCO* received Manifestations and Urgent Motions from Anak Pawis, et. al. On even date, *MERALCO* received another related Petition, dated January 16, 2014, which was filed before the SC by Mr. Augusto L. Syjoco, Jr. in his capacity as taxpayer and *MERALCO* customer. During the January 21, 2014 hearing, the SC, among other things, set the cases for additional hearings on February 4 and 11, 2014.

On January 24, 2014, a copy of Therma Mobile, Inc. or *TMO* and Therma Luzon, Inc.'s or *TLI* Consolidated Comment has been posted on the *Supreme Court*'s website. On January 29, 2014, *MERALCO* received a copy of the Power Sector Assets and Liabilities Corporation's or *PSALM*, Consolidated Comment on the Petitions (docketed as G.R. Nos. 210245 and 210255) and *MERALCO*'s Counter-Petition. Thereafter, or on January 30, 2014, *MERALCO* received Panasia Energy, Inc.'s Comment that prays for the dismissal of the Petitions and Counter-Petition in the *Supreme Court* cases.

Oral arguments on the cases were continued on February 4 and 11, 2014. *MERALCO* presented its position and was interpellated thereon by the SC. Therein, the *Supreme Court* clarified that the *TRO* only covered the December 2013 billing of *MERALCO*. During the February 11, 2014 hearing, the other respondents, including *DOE*, *ERC*, *PEMC*, *TMO*, *NGCP*, and *PSALM*, presented their respective positions before the *Supreme Court*. Thereafter, the *Supreme Court* gave the parties until February 26, 2014 to file their respective memoranda.

In the meantime, on January 30, 2014, *MERALCO* filed an Urgent Motion with Manifestation with the *ERC*. *MERALCO* manifested that certain statements were made that there have been gross violations of *WESM* rules and regulations as well as protocols on generation offers and plant dispatch by certain *WESM* participants which affected the market clearing prices. *MERALCO* prayed for the for the issuance of an Order: (a) directing *PEMC* to conduct market re-runs or re-calculations of *WESM* transactions and dispatches, or determine substituted prices or undertake any other appropriate measures to determine and recalculate the true cost of electricity in the *WESM*, during the November to December 2013 supply months (*MERALCO*'s December 2013 to January 2014 billing months) under such rules or guidelines as the *ERC* may deem appropriate and (b) directing *MERALCO* to subsequently recalculate its pass-through generation charges for the November to December 2013 supply months (*MERALCO*'s December 2013 to January 2014 billing months) based on the proper applicable prices for transactions in the *WESM* during the aforementioned months as so determined by the Honorable Commission based on the results of the market re-runs and/or re-calculations. This re-run is without prejudice to such action or decision the *ERC* may take following compliance of its investigation on whether or not there were acts committed by electric industry participants during the subject period which constitute anti-competitive practices, market power abuse, violation of any law or rules and regulations, or any failure of market competition. *MERALCO* then filed an Urgent Ex-Parte Motion (to Set for Hearing and/or Resolve the Omnibus Motion) on February 5, 2014 praying that its Urgent Motion with Manifestation be immediately set for hearing and

resolved. Both pleadings were noted by the *ERC* in its Order dated February 12, 2014.

On January 29, 2014, *MERALCO* also appeared before the Investigation Unit of the *ERC*. The Investigation Unit was created to determine if there has been anti-competitive behavior and/or abuse of market power by the *WESM* participants during the period affected by the Malampaya shutdown.

On February 18, 2014, the *Supreme Court* extended the *TRO* for another 60 days, or until April 22, 2014, and expanded the coverage to include the generation companies, *PEMC* and *NGCP* to enjoin them from collecting from *MERALCO*.

12. Recovery of the Differential Generation Charge for the December 2013 supply month

ERC Case No. 2014-013

Filed: February 17, 2014

In the light of the clarification of the *Supreme Court* that the *TRO* in G.R. Nos. 210245 and 210255 only covered the December 2013 billing, *MERALCO* filed an Application, with a prayer for provisional authority, on February 17, 2014 with the *ERC* to recover the incremental generation charge for the December 2013 supply month (January 2014 billing), docketed as *ERC* Case No. 2014-013RC. This represented the difference between the actual and billed generation charge for the January 2014 billing. The Application prayed that *MERALCO* be allowed: (a) to impose an incremental generation charge of ₱0.8440/kWh on its customers in their March 2014 billing, until the total incremental fuel costs amounting to Two Billion Forty-Nine Million Five Hundred Twenty-Nine Thousand Three Hundred Forty-Eight Pesos and Fifty-Nine Centavos (₱2,049,529,348.59) is fully recovered, and (b) to recover the remaining balance of the deferred generation costs equivalent to ₱0.7433/kWh every month, for an additional period of five (5) months starting April 2014 billing, until the balance of Nine Billion Twenty-Five Million Nine Hundred Twenty-One Thousand Two Hundred Eighty-Two Pesos and Six Centavos (₱9,025,921,282.06) is fully recovered, without prejudice to the resolution of G.R. Nos. 210245 and 210255 by the *Supreme Court* or *MERALCO*'s pending Omnibus Motion with Manifestation in *ERC* Case No. 2013-092 MC, or the findings of the *ERC*'s Investigation Unit in *ERC* Case No. 2014-001 MC.

Subsequently, on March 11, 2014, *MERALCO* received the *ERC*'s Order dated March 3, 2014 in *ERC* Case No. 2014-021 MC, declaring as void the Luzon *WESM* prices during the November and December 2013 supply months and imposing regulated prices in lieu thereof.

The regulated prices shall be calculated based on the load weighted average of the ex-post nodal energy prices and meter quantity of the same day same trading interval that have not been administered covering the period December 26, 2012 to September 25, 2013, subject to the payment to the oil-based plants of additional compensation to cover their full Fuel and Variable Operations and Maintenance Costs, if warranted, following the manner and procedure for computing additional compensation under the Administered Price Determination Methodology.

PEMC was directed to calculate these regulated prices and implement the same in the revised *WESM* bills of the concerned distribution utilities in Luzon for the November and December 2013 supply months for their immediate settlement, except for *MERALCO* whose November 2013 *WESM* bill shall be maintained, unless otherwise ordered by the *ERC*, in compliance to the Temporary Restraining Order issued by the *Supreme Court* in G.R. No. 21024 and G.R. No. 210255.

PEMC made recalculations based on the afore-quoted Order and on 18 March 2014, *MERALCO* received a copy of *PEMC*'s *WESM* billing adjustments to adjust the *WESM* bill for the regulated prices for the December 2013 supply month.

On March 25, 2014, *MERALCO* filed an Amended Application pursuant to the ERC Order and the recalculation made by *PEMC* of the December 2013 supply month bills.

Item 4. Submission of Matters to a Vote of Security Holders

No matter was submitted during the fourth quarter of the fiscal year covered by this report to a vote of security holders.

PART II – OPERATIONAL AND FINANCIAL INFORMATION

Item 5. Market for Issuer's Common Equity and Related Stockholders Matters

(1) Market Information

The principal market where *MERALCO*'s common equity is traded is the Philippine Stock Exchange or *PSE*. The quarterly high and low sales prices for the fiscal years 2013 and 2012 follow:

MER			
FROM	TO	HIGH	LOW
01/01/12	03/31/12	₱279.80	₱252.00
04/01/12	06/30/12	275.00	218.82
07/01/12	09/30/12	276.00	240.00
10/01/12	12/31/12	291.20	248.00
01/01/13	03/31/13	330.00	260.60
04/01/13	06/30/13	395.00	307.00
07/01/13	09/30/13	330.80	260.00
10/01/13	12/31/13	313.90	250.60
01/01/14	03/31/14	290.00	250.20

As at December 27, 2013 (the last trading day in 2013), the price for *MERALCO* Stocks is ₱251.00.

(2) Holders

The total number of stockholders as of December 31, 2013 is 46,409.

Top 20 Stockholders as of December 31, 2013

Rank	Stockholder Name	Number of Shares	Percent
1	Beacon Electric Asset Holdings, Inc.	564,124,042	49.96%
2	PCD Nominee Corporation (Filipino)	261,860,906	23.23%
3	JG Summit Holdings, Inc.	153,191,489	13.59%
4	PCD Nominee Corporation (Foreign)	54,054,613	4.80%
5	First Philippine Holdings Corporation	44,382,436	3.94%
6	Board of Administrators - ESOP	7,775,135	0.51%
7	Manuel M. Lopez and/or Ma. Teresa L. Lopez	1,449,293	0.13%
8	Manuel M. Lopez	795,957	0.07%
9	Concepcion and/or Araneta	774,257	0.07%
10	Lucio W. Yan	403,208	0.04%
11	Charlotte Cua Cheng	314,534	0.03%
12	Avesco Marketing Corporation	284,427	0.03%
13	B.P. Insurance Agency, Inc.	281,079	0.02%
14	Regina Capital Development Corporation	270,000	0.02%
15	Jesus P. Francisco	257,480	0.02%
16	Makati Supermarket Corporation	240,308	0.02%
17	Simeon Y. Tan	162,800	0.01%
18	Jose Ignacio A. Carlos	161,687	0.01%
19	Virgilio C. Flordeliza	136,649	0.01%
20	Antonino T. Antonio and/or Evelina S. Aquino	133,855	0.01%

(3) Dividends

Following are the cash dividends declared by *MERALCO*'s board of directors in favor of *MERALCO* common shares for the two (2) most recent years ended December 31, 2013 and 2012:

Year	Dividend Per Share	Declaration Date	Record Date	Payment Date
2012	P4.10	February 27, 2012	March 23, 2012	April 23, 2012
	P4.00	July 30, 2012	August 29, 2012	September 24, 2012
2013	P6.10	February 25, 2013	March 26, 2013	April 24, 2013
	P4.10	July 29, 2013	August 27, 2013	September 20, 2013

MERALCO's loan agreements contain restrictions on payments of cash dividends to common stockholders subject to meeting certain financial measures, which *MERALCO* complied with.

MERALCO strictly implements its dividend policy, approved by the Board of Directors or *BOD*, in 2010, which prescribes the regular payment of dividends equivalent to fifty percent (50%) of consolidated core net income. In 2013, *MERALCO* paid cash dividend of ₱10.20 per share to all its shareholders.

(4) Recent Issuance of Securities Constituting an Exempt Transaction

None.

Item 6. Management's Discussion and Analysis or Plan of Operation

The following discussion and analysis of financial position and results of operations of Manila Electric Company or *MERALCO*, and its subsidiaries, collectively referred to as the "*MERALCO Group*" should be read in conjunction with the consolidated financial statements as at December 31, 2013 and 2012 and January 1, 2012 and for each of the three years in the period ended December 31, 2013. The consolidated financial statements have been prepared in compliance with the Philippine Financial Reporting Standards or *PFRS*. *PFRS* includes statements named *PFRS* and Philippine Accounting Standards or *PAS*, including Interpretations issued by the Philippine Financial Reporting Standards Council or Philippine *FRSC*.

The financial information appearing in this report and in the accompanying consolidated financial statements is presented in Philippine peso, *MERALCO Group's* functional and presentation currency, as defined under *PFRS*. All values are rounded to the nearest million pesos, except when otherwise indicated. The exchange rate used to translate U.S. dollars to Philippine peso in this report and in the accompanying consolidated financial statements is ₱44.395 to US\$1.00, the closing rate as at December 27, 2013 (the last trading day in 2013) quoted through the Philippine Dealing System.

Financial Highlights and Key Performance Indicators

As at December 31				% Change	
	2013	2012 (As restated)	2011 (As restated)	2013 vs. 2012	2012 vs. 2011
(Amounts in millions, except financial ratios, earnings per share, and operational data)					
Condensed Statements of Financial Position					
Total assets	₱264,004	₱216,891	₱211,088	22	3
Current assets					
Continuing operations	107,486	92,243	77,424	17	19
Discontinued operations	—	—	18,349	—	(100)
Cash and cash equivalents	59,851	60,500	44,141	(1)	37
Equity attributable to equity holders of the parent	75,162	67,902	62,156	11	9
Total debt	33,591	24,613	24,443	36	1
Current liabilities					
Continuing operations	94,626	59,518	53,042	59	12
Discontinued operations	—	—	9,113	—	(100)
Financial Ratios					
Debt to equity	0.45	0.36	0.39		
Current ratio – continuing operations	1.14	1.55	1.46		
Operational Data					
Number of customers (in thousands):					
Residential	4,901	4,735	4,580	4	3
Commercial	453	440	433	3	2
Industrial	10	10	10	—	—
Streetlights	4	4	4	—	—
Years ended December 31					
	2013	2012 (As restated)	2011 (As restated)	2013 vs. 2012	2012 vs. 2011
Condensed Statements of Income					
Revenues	₱298,636	₱285,270	₱256,808	5	11
Costs and expenses	274,486	266,162	238,969	3	11
Other income, net of expenses	(177)	(2,914)	(907)	(94)	221
Income before income tax from continuing operations	24,327	22,022	18,746	10	17
Income from discontinued operations, net of income tax	—	978	966	(100)	1
Net income	17,273	17,259	13,759	—	25
Net income attributable to equity holders of the parent	17,211	17,117	13,260	1	29
Earnings per share					
Basic and diluted - attributable to equity holders of the parent	15.27	15.19	11.76	1	29
Basic and diluted - attributable to equity holders of the parent of continuing operations	15.27	14.40	11.31	6	27

	Years ended December 31			% Change	
				2013	2012
	2013	2012 (As restated)	2011 (As restated)	vs. 2012	vs. 2011
Condensed Statements of Cash Flows					
Net cash flows from operating activities	37,144	36,244	31,934	2	13
Net cash used in investing activities	(30,392)	(9,549)	(6,816)	218	40
Net cash used in financing activities	(7,401)	(10,336)	(4,578)	(28)	126
Financial Ratios					
Profit margin	5.8%	6.0%	5.2%	(3)	15
Return on equity	22.9%	25.2%	21.3%	(9)	18
Asset turnover	1.13	1.32	1.22	(14)	8
Operational Data					
Electricity sales volume (in GWh)	34,084	32,771	30,592	4	7
System loss (in percentage) ¹ :					
MERALCO	6.92%	7.04%	7.35%	(2)	(4)
CEDC	4.33%	3.75%	3.96%	15	(5)

¹ Based on 12-month moving average

OVERVIEW

MERALCO is the Philippines' largest electric power distribution company with franchise service area covering 9,337 square kilometers (km²). It provides power to 5.4 million customers in 34 cities and 77 municipalities, which include Metro Manila, the provinces of Rizal, Cavite and Bulacan, and parts of the provinces of Pampanga, Batangas, Laguna and Quezon. Turnover of business establishments in the franchise area accounts for almost 50% of the country's Gross Domestic Product or *GDP*.

Through Clark Electric Distribution Corporation or *CEDC*, a 65%-owned subsidiary, it holds the power distribution franchise for the Clark Special Economic Zone or *CSEZ*, in Clark, Pampanga. *CEDC*'s franchise area covers 320 km² and services 1,819 customers. *CEDC* is registered with Clark Development Corporation or *CDC*, under Republic Act or *RA No. 9400, Bases Conversion Development Act of 1992*, as a *CSEZ*-enterprise primarily engaged in owning, operating, and maintaining a power distribution system within the zone.

MERALCO Group's business is divided into two segments, namely, power and other services. The power segment consists primarily of the power distribution operations of *MERALCO* and its subsidiary, *CEDC*.

- Power

The Power segment consists of (a) electricity distribution, (b) power generation and (c) Retail Electricity Supply or *RES*.

Electricity distribution – This is principally electricity distribution and supply of power on a pass-through basis covering all the captive customers in the *MERALCO* franchise area and the *CEDC* franchise area in the Luzon Grid. Electricity distribution within the *MERALCO* franchise area accounts for approximately 55% of the power requirements of the country. *CEDC*'s service area covers the *CSEZ*.

Power generation – The *MERALCO Group*'s re-entry into the power generation business is through investments in operating companies or participation in the development of new or expansion power generation projects.

In October 2013, MERALCO PowerGen Corporation or *MGen*, the power generation arm of the *MERALCO Group* acquired a 20%-equity interest in Global Business Power Corporation or *GBPC*. *GBPC* has a total of 627 MegaWatt or *MW* gross capacity in operations and 232 *MW* gross capacity coal-fired power plants under construction in the Visayas.

In March 2013, *MGen* acquired an effective 28% equity in PacificLight Power Pte Ltd. or *PacificLight Power*, a 2x400 *MW* liquefied natural gas or *LNG*, plant in Jurong Island, Singapore.

MGen is currently developing a 500 *MW* gross (460 *MW* net) capacity of supercritical coal-fired power plant in Mauban, Quezon. On the other hand, land development for its 2 x 300 *MW* Circulating Fluidized Bed or *CFB*, coal-fired power generation plant in the Subic Freeport Zone by Redondo Peninsula Energy, Inc. or *RP Energy* is continuing, pending the decision of the Supreme Court of the Philippines or *Supreme Court*, on a Motion for Reconsideration or *MR*, filed. See related discussions under **OTHER QUANTITATIVE AND QUALITATIVE DISCLOSURES**.

Further, *MGen* is in various stages of pre-development of other power generation projects in Luzon.

Retail Electricity Supplier or *RES* – The *MERALCO* local *RES* sources and supplies electricity to its qualified contestable customers within the *MERALCO* franchise area under the brand *MPower* starting June 26, 2013.

- Other Services

“Other services” segment consists principally of electro-mechanical engineering, construction, consulting and related manpower as well as light rail-related maintenance services, e-transaction and bills collection, insurance and e-business development and energy systems management. These services are provided by Meralco Industrial and Engineering Services Corporation or *MIESCOR*, Miescor Builders, Inc. or *MBI*, and Miescor Logistics, Inc. or *MLI* (collectively known as “*MIESCOR Group*”), Corporate Information Solutions, Inc. or *CIS*, CIS Bayad Center, Inc. or *Bayad Center* and Customer Frontline Solutions, Inc. or *CFSI* (collectively referred to as “*CIS Group*”), Miescorrail, Inc. or *Miescorrail*, Republic Surety and Insurance Corporation or *RSIC*, Lighthouse Overseas Insurance Limited or *LOIL*, Meralco Financial Services, Inc. or *Finserve*, e-Meralco Ventures, Inc. or *e-MVI*, Paragon Vertical Corporation and Radius Telecomms, Inc. (collectively referred to as *e-MVI*) and Meralco Energy, Inc. or *MEI*.

MERALCO's Real Estate segment, which was provided by Rockwell Land Corporation or *Rockwell Land*, is involved in luxury residential and commercial real estate development and leasing. In 2012, the accounts of *Rockwell Land* were deconsolidated from those of *MERALCO* when *MERALCO*'s investment in common equity shares in *Rockwell Land* was declared as property dividends to stockholders of record as at March 23, 2012, except for foreign common shareholders who were paid the cash equivalent of the property dividends on May 14, 2012. The Securities and Exchange Commission or *SEC* approved the declaration of *Rockwell Land* as property dividends on April 25, 2012. This resulted in the presentation of the financial information of *Rockwell Land* as discontinued operations. Consequently, *MERALCO* reclassified the related assets, liabilities and accumulated other comprehensive income

of *Rockwell Land* as “Assets of discontinued operations”, “Liabilities of discontinued operations” and “Unrealized fair value gains on AFS investments of discontinued operations”, respectively, in the consolidated statement of financial position as at January 1, 2012. In 2011, the accounts of *Rockwell Land* were included in the other services segment.

Below is the summary of *MERALCO Group's* business segments:

BUSINESS SEGMENTS	
Power	Other Services
Electricity distribution <ul style="list-style-type: none"> • <i>MERALCO</i> • <i>CEDC</i> Power generation <ul style="list-style-type: none"> • <i>MGen</i> and subsidiaries Retail electricity supply <ul style="list-style-type: none"> • <i>MERALCO</i> through <i>MPower</i> business unit 	<ul style="list-style-type: none"> • <i>MIESCOR Group</i> • <i>Finserve</i> • <i>LOIL</i> • <i>RSIC</i> • <i>CIS Group</i> • <i>e-MVI Group</i> • <i>MEI</i> • <i>Miescorrail</i>

RESULTS OF OPERATIONS

The table below summarizes the consolidated results of operations and the contribution of each business segment of *MERALCO Group's* revenues, costs and expenses, and net income for the years ended December 31, 2013, 2012 and 2011.

For the year ended December 31, 2013				
	Power²	Other Services	Inter-segment Transactions	Consolidated
	<i>(Amounts in millions)</i>			
Revenues	₱294,849	₱5,258	(₱1,471)	₱298,636
Costs and expenses	271,798	4,159	(1,471)	274,486
Other expenses (income)	(262)	(6)	91	(177)
Net income attributable to equity holders of the parent	16,603	761	(153)	17,211

For the year ended December 31, 2012 (As restated)				
	Power³	Other Services	Inter-segment Transactions	Consolidated
	<i>(Amounts in millions)</i>			
Revenues	₱282,991	₱3,829	(₱1,550)	₱285,270
Costs and expenses	264,837	2,875	(1,550)	266,162
Other expenses (income)	(3,138)	(38)	262	(2,914)
Net income attributable to equity holders of the parent	15,839	1,682	(404)	17,117

²Principally electricity distribution

³Ibid

For the year ended December 31, 2011 (As restated)				
	Power ⁴	Other Services	Inter-segment Transactions	Consolidated
	<i>(Amounts in millions)</i>			
Revenues	₱253,989	₱3,923	(₱1,104)	₱256,808
Costs and expenses	237,304	2,769	(1,104)	238,969
Other expenses (income)	(1,689)	(100)	882	(907)
Net income attributable to equity holders of the parent	12,785	1,906	(1,431)	13,260

2013 versus 2012

REVENUES

The following table shows the composition of *MERALCO Group's* consolidated revenues for the years ended December 31, 2013 and 2012 by business segment:

	2013	%	2012	%	Increase/(Decrease)	
					Amount	%
	<i>(Amounts in millions)</i>					
Power ⁵	₱294,849	99	₱282,991	99	₱11,858	4
Other services	5,258	1	3,829	1	1,429	37
Inter-segment transactions	(1,471)	—	(1,550)	—	79	5
Total	₱298,636	100	₱285,270	100	₱13,366	5

Total revenues for the year ended December 31, 2013 amounted to ₱298,636, 5% higher compared with last year's ₱285,270. Revenues from power segment remained at 99% of the total revenues both in 2013 and 2012. The higher revenues are largely attributable to the 4% increase in volume and a higher share of residential and commercial customers in the overall sales mix. Average distribution charge was at ₱1.65 per *kWh* in 2013.

Power

Revenues from the power segment consist of generation, transmission, distribution charges and subsidies.

The composition of revenues of the power segment for the year ended December 31, 2013 and 2012 is summarized as follows:

	2013	%	2012	%	Increase/(Decrease)	
					Amount	%
	<i>(Amounts in millions)</i>					
Generation charge	₱192,558	65	₱183,708	65	₱8,850	5
Transmission charge	29,191	10	31,971	11	(2,780)	(9)
Distribution service charges	56,105	19	50,892	18	5,213	10
System loss charge	17,138	6	16,411	6	727	4
Subsidies and other charges	(134)	—	34	—	(168)	(494)
Power Act Reduction adjustment	(9)	—	(25)	—	16	64
Total	₱294,849	100	₱282,991	100	₱11,858	4

⁴Ibid

⁵Ibid.

Electricity Revenues

Generation charge represents the single largest component of electricity revenues, which is at 65% in 2013. Average generation charge to captive customers was at ₱5.39 per *kWh* in 2013 versus ₱5.61 per *kWh* in 2012. Transmission charge on the other hand, represents 10% of total power revenues or an equivalent ₱0.86 per *kWh* in 2013 compared with ₱0.98 per *kWh* in 2012. Overall, average transmission charge was lower by 9%. Average system loss charge in 2013 was at ₱0.46 per *kWh*, ₱0.52 per *kWh* lower than 2012 mainly due to the continuous improvement in system loss management. MERALCO's 12-month moving average system loss rate as at December 31, 2013 was at 6.92%, 0.12 percentage point lower compared with the 7.04% system loss rate as at December 31, 2012, and outperforming the ERC-imposed 8.50% cap by 1.58 percentage points as a result of its institutionalized system loss management programs. CEDC's 12-month moving average system loss rate as at December 31, 2013 was at 4.33%. Subsidies and other charges include interclass and lifeline subsidies and universal charges.

In December 2013, total revenues include ₱8,963 million or an equivalent ₱3.44 per *kWh* representing the amount subject of a Temporary Restraining Order or *TRO*, issued by the *Supreme Court* in respect of the implementation of the generation charge increase for the November 2013 supply month. The increase in generation charge was the result of (i) use of more expensive liquid condensate by the Sta. Rita and San Lorenzo gas-fired plants and bio-diesel by the Ilijan gas plant with the 30-day maintenance shutdown of the Malampaya natural gas production facility; (ii) scheduled and extended outages of several baseload plants; and (iii) unscheduled, forced and overlapping outages of several power plants. The ultimately recovery of the generation and related charges is pending the decision of the *Supreme Court*.

Distribution revenues comprise 19% of the total revenues of the power segment. Total distribution service charges for the year ended December 31, 2013 amounted to ₱56,105 million, reflecting a 10% increase compared with the same period in 2012. The higher distribution revenue is due to the 4% increase in sales volume and slightly higher average distribution rate in 2013. Total volume in 2013 was at 34,084 *GWh* compared with 32,771 *GWh* in 2012. Increase in sales volume is driven by the 3% growth in customer count and higher electricity consumption across all existing customers. The growth in the industrial sector was driven by higher demand of food and beverage, rubber and plastics as well as semiconductor industries. Commercial volume is driven by real estate and retail trade fuelled by the Business Process Outsourcing or *BPO*, industry expansion and higher consumer spending in entertainment, malls, hotels, and restaurants. Residential volume is driven by slightly warmer weather and continuous inflow of OFW remittances. Average distribution rate was at ₱1.65 per *kWh* in 2013. In July 2013, MERALCO implemented the Maximum Average Price or *MAP*, for Regulatory Year or *RY* 2014 at ₱1.6474 per *kWh*, which was provisionally approved by the Energy Regulatory Commission or *ERC* in June 2013.

The following table summarizes the customer count as at December 31, 2013 and 2012 and the corresponding electric consumption per customer class for the year ended December 31, 2013 and 2012:

Customer Class	No. of Customers (in thousands)		Electricity Sales (in GWh)		% Change	
	2013	2012	2013	2012	No. of Customers	Electricity Sales
Residential	4,901	4,735	10,235	9,779	4	5
Commercial	453	440	13,302	12,749	3	4
Industrial	10	10	10,417	10,111	—	3
Streetlights	4	4	130	132	—	(2)
Total	5,368	5,189	34,084	32,771	3	4

The first phase of Retail Competition and Open Access or *RCOA*, started commercial implementation on June 26, 2013. Contestable customers in the Luzon and Visayas grids whose connected load is at least one (1) *MW* over the past 12 months, commenced to source their power supply from various *ERC*-registered *RESS*s. Out of 782 qualified contestable customers in the *MERALCO* franchise area, 287 customers have opted for contestability and switched their supply to eight (8) *RESS*s, including *MERALCO*'s local *RES*, *MPower*. Total energy sourced from *RESS*s was 2,711 *GWh* for the period June 26 to December 31, 2013. *MPower* accounted for 167 of the 287 customers.

Other Services

Revenues from other services pertain to non-electric revenues of *MERALCO* and subsidiaries. Revenues generated from other services increased to ₱5,258 million in 2013 from ₱3,829 million in 2012. The 37% increase in revenues from other services is mainly attributable to the increase in third party payment service volume, business expansion of outsourced services of *Bayad Center* and increase in franchising fees of *Bayad Center*. *MIESCOR*'s contract revenues also increased in 2013, which include projects regarding rehabilitation of electrical and installation of fire alarm, and maintenance, janitorial and renovation activities. The *e-MVI Group* obtained additional requirements from international carriers, retail and distribution industry, and banks.

COSTS AND EXPENSES

Consolidated costs and expenses for the year ended December 31, 2013 amounted to ₱274,486 million, 3% higher compared with ₱266,162 million for the same period in 2012. The following table shows the details by business segment:

	2013	%	2012 (As restated)	%	Increase/(Decrease) Amount	
						%
			(Amounts in millions)			
Power ⁶	₱271,798	99	₱264,837	100	₱6,961	3
Other services	4,159	2	2,875	1	1,284	45
Inter-segment transactions	(1,471)	(1)	(1,550)	(1)	79	5
Total	₱274,486	100	₱266,162	100	₱8,324	3

⁶*Ibid.*

Power

The details of costs and expenses are summarized in the following table:

	2013	%	2012 (As restated)	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Purchased power	₱238,198	88	₱232,068	88	₱6,130	3
Salaries, wages and employee benefits	9,450	3	10,385	4	(935)	(9)
Depreciation and amortization	5,911	2	5,400	2	511	9
Contracted services	4,146	2	3,594	1	552	15
Others	14,093	5	13,390	5	703	5
Total	₱271,798	100	₱264,837	100	₱6,961	3

Costs and expenses of the power segment amounted to ₱271,798 million in 2013, 3% higher than the ₱264,837 million in 2012.

Purchased power accounted for 88% of the total costs and expenses. In 2013, *MERALCO's* power segment purchases all of the electricity distributed from (i) contracted capacities under the Power Supply Agreements or *PSAs*, with Successor Generating Companies or *SGCs* (up to December 25, 2012), National Power Corporation or *NPC* (up to June 25, 2013), (ii) long-term Power Purchase Agreements or *PPAs*, contracted with Independent Power Producers or *IPPs* and (iii) the Wholesale Electricity Spot Market or *WESM*. Higher purchased power costs was attributable to the 30-day shutdown of the Malampaya natural gas production facility, scheduled and extended as well as unscheduled or forced-outages of major baseload gas-fired and coal-fired power plants, which resulted in a higher average purchased power cost at ₱6.71 per *kWh* in 2013 compared with ₱6.60 per *kWh* in 2012. Total purchased power volume increased from 35,176 *GWh* in 2012 to 35,503 *GWh* in 2013, while the average cost of power purchased from *WESM* was higher at ₱19.93 per *kWh* in 2013 compared with ₱12.58 per *kWh* in 2012.

The volume of energy purchased under long-term *PPAs* with *IPPs*, First Gas Corporation or the *Sta. Rita Power Plant*, *FGP Corp.* or the *San Lorenzo Power Plant* and Quezon Power (Philippines) Limited Co. or *QPPL*, represents 36% of *MERALCO's* Net Systems Input. Purchases from *SGCs* and *NPC* and other special programs account for 59%, while the balance of 5% was sourced from the *WESM*. Electricity distributed by *CEDC* is sourced solely from the Sual Coal-fired Plant of San Miguel Energy Corporation.

Salaries, wages and employee benefits decreased by 9% from ₱10,385 million for the year ended December 31, 2012 to ₱9,450 million for the same period in 2013. This is mainly due to the fringe benefit tax expense paid in 2012 related to the issued Employee Share Purchase Plan or *ESPP*, shares. The decrease was partially offset by the annual increase in salaries of employees.

Contracted services increased by 15% from ₱3,594 million in 2012 to ₱4,146 million in 2013. Customer-related services such as meter reading, electric bill/disconnection notice delivery increased with higher customer count, and meter and service reconnection/disconnection increased due to intensified delinquency management programs. Contracted services also increased for network maintenance services, legal fees and consultants' fees related to *MERALCO's* implementation of an enterprise resource planning software.

Depreciation and amortization increased by 9% to ₱5,911 million in 2013 from ₱5,400 million in 2012. This is mainly due to additional depreciation from completed construction projects and newly installed capital assets and amortization of software application related to MERALCO's software upgrade.

Other expenses consist of business taxes and permits, provision for probable charges and expenses from claims, provisions for doubtful accounts, costs of materials, transportation, and other corporate expenses.

Other Services

The cost and expenses of other services business segment in 2013 amounted to ₱4,159 million, 45% higher compared with ₱2,875 million in 2012.

	2013	%	2012 (As restated)	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Salaries, wages and employee benefits	₱1,808	43	₱1,241	43	₱567	46
Contracted services	955	23	627	22	328	52
Depreciation and amortization	206	5	176	6	30	17
Others	1,190	29	831	29	359	43
Total	₱4,159	100	₱2,875	100	₱1,284	45

Salaries, wages and other employee benefits increased by 46% from ₱1,241 million in 2012 to ₱1,808 million in 2013. The increase is mainly due to the increase in the number of employees in most subsidiaries and annual salary increase of employees.

Contracted services increased by 52% from ₱627 million in 2012 to ₱955 million in 2013. This is mainly due to the implementation of the government-mandated wage adjustments at the start of 2013.

Depreciation and amortization in 2013 amounted to ₱206 million, 17% higher compared with the same period in 2012 as a result of capital expenditures of the subsidiaries.

Other expenses increased by 43% from ₱831 million in 2012 to ₱1,190 million in 2013. This is mainly due to business expansion activities, additional rent and utilities, and higher developmental costs of subsidiaries.

OTHER EXPENSES (INCOME)

The following table shows the breakdown of MERALCO Group's consolidated other income, net of expenses, for the years ended December 31, 2013 and 2012 by business segment:

	2013	%	2012	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Power ⁷	(₱262)	148	(₱3,138)	108	(₱2,876)	(92)
Other services	(6)	3	(38)	1	(32)	(84)
Inter-segment transactions	91	(51)	262	(9)	(171)	(65)
Total	(₱177)	100	(₱2,914)	100	(₱2,737)	(94)

⁷Ibid.

Consolidated other income, net of expenses, for the year ended December 31, 2013 decreased to ₱177 million, 94% lower compared with ₱2,914 million in 2012.

Power

Breakdown of other expenses (income) of power segment is summarized in the following table:

	2013	%	2012	%	Increase/(Decrease)	
					Amount	%
			(Amounts in millions)			
Interest and other financial charges	₱1,475	(563)	₱1,518	(48)	(₱43)	(3)
Interest and other financial income	(1,161)	443	(2,519)	80	(1,358)	(54)
Foreign exchange loss (gain)	(354)	135	2	–	356	17,800
Equity in net losses (earnings) of associates and joint ventures	168	(64)	(247)	8	(415)	(168)
Derivative mark-to-market loss (gain)	24	(9)	(40)	1	(64)	(160)
Others	(414)	158	(1,852)	59	(1,438)	(78)
Total	(₱262)	100	(₱3,138)	100	(₱2,876)	(92)

Other income, net of expenses, is lower by 92% from ₱3,138 million in 2012 to ₱262 million in 2013 due to decrease in interest and other financial income and other income as a result of lower interest rate. Also, in 2012, Interest and other financial income included the ₱730 million carrying charges related to the local franchise tax or *LFT*, recovery, and other income included the *LFT* recovery of ₱1,571 million approved in April 2012.

NET INCOME ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The following table shows the breakdown of *MERALCO*'s net income attributable to the equity holders of *MERALCO* for the years ended December 31, 2013 and 2012 by business segment:

	2013	%	2012 (As restated)	%	Increase/Decrease	
					Amount	%
	(Amounts in millions)					
Power ^a	₱16,603	97	₱15,839	92	₱764	5
Other services	761	4	1,682	10	(921)	(55)
Inter-segment transactions	(153)	(1)	(404)	(2)	(251)	(62)
Total	₱17,211	100	₱17,117	100	₱94	1

Power

Net income attributable to equity holders of the parent in 2013 is higher by 5% compared with 2012 mainly due to the increase in distribution revenue in 2013 driven by increased energy sales and slightly higher *RY2014 MAP* of ₱1.6474 per kWh.

Other Services

Net income from other services business segment attributable to the equity holders of the parent was 55% lower at ₱761 million in 2013 compared with ₱1,682 million in 2012, which included the gain on divestment from *Rockwell Land* amounting to ₱769 million. *MERALCO* divested its equity shares in *Rockwell Land* in May 2012.

⁸*Ibid.*

2012 versus 2011

REVENUES

The following table shows the composition of *MERALCO Group's* consolidated revenues for the years ended December 31, 2012 and 2011 by business segment:

	2012	%	2011	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Power ⁹	₱282,991	99	₱253,989	99	₱29,002	11
Other services	3,829	1	3,923	1	(94)	(2)
Inter-segment transactions	(1,550)	—	(1,104)	—	(446)	(40)
Total	₱285,270	100	₱256,808	100	₱28,462	11

Revenues from electricity sales amounted to ₱282,991 million, accounting for 99% of the total consolidated revenues, and 11% higher than the ₱253,989 million generated in 2011. The increase in revenues was attributable to the 7% growth in volume of energy sold, which reflected the broad-based growth of the economy, fuelled by the services, real estate and manufacturing sectors. This was further supported by the notable increase in remittances sent home by some 10 million overseas Filipino workers, which provided the impetus for increased domestic consumption and consequently, the growth in residential and commercial energy volume. In addition, the warmer temperature in 2012 resulted in higher energy sales, which offset the impact of six (6) weather disturbances within the franchise area during the year. The foregoing was complemented by earlier energization of new customers, shorter forced- and planned service interruption time and the recovery of self-generating and directly-connected customers, resulted in higher revenues.

Power

Revenues from electricity represent *MERALCO* and *CEDC's* sale of electricity, which include generation, transmission, distribution charges and subsidies. *MERALCO* and *CEDC* distribute electricity to industrial, commercial and residential customers.

The composition of revenues from electricity distribution for the year ended December 31, 2012 and 2011 is summarized as follows:

	2012	%	2011	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Electric revenues						
Generation charge	₱183,708	65	₱157,850	62	₱25,858	16
Distribution service charges	50,892	18	48,606	19	2,286	5
Transmission charge	31,971	11	32,340	13	(369)	(1)
System loss charge	16,411	6	15,500	6	911	6
Power act reduction	(25)	—	(106)	—	81	76
Inter-class, lifeline subsidies and others	34	—	(201)	—	235	117
Total	₱282,991	100	₱253,989	100	₱29,002	11

Generation, transmission, system loss, subsidies and other charges, which comprise pass-through charges represent 82% of the total electric revenue. Other bill components namely, value-added tax and *LFT* and universal charges are non-revenue items. Generation charges, transmission and system loss accounted for 65%, 11% and 6%, respectively of total electric revenues. Pass-through charges increased by 13% from

⁹*Ibid.*

₱205,383 million in 2011 to ₱232,099 million in 2012. *MERALCO* continues to reap the benefits of its institutionalized system loss management programs resulting in further improvements in performance. The 12-month moving average system loss rate in 2012 was 7.04%, surpassing the record rate of 7.35% in 2011. With the system loss rate below the regulatory cap of 8.50%, a total of ₱3.4 billion savings in 2012 or a cumulative ₱8.7 billion over the last 5 years, have been realized and passed on to the customers. *CEDC*'s system loss rate is at 3.75%.

Distribution revenues comprise 18% of the total electric revenues.

Total distribution service charges for the year ended December 31, 2012 amounted to ₱50,892 million, reflecting a 5% increase compared with the same period in 2011. Total energy sold for the year ended December 31, 2012 was 32,771 *GWh* or 7% higher than the 30,592 *GWh* in 2011. Sales across all customer classes reflected increases in 2012 compared with 2011. Sales to industrial customers increased by 11% to 10,111 *GWh*, which is largely attributable to the semiconductor, non-metallic and food and beverage manufacturers. Energy sold to commercial customers registered an increase of 6% to 12,749 *GWh* in 2012. Sales to residential customers increased by 5% to 9,779 *GWh* in 2012.

Billed customers steadily grew, with 162 thousand new customers representing an increase of 3% to almost 5.2 million as at December 31, 2012. Residential customers, while accounting for 30% of the total energy sold, represents 91% of the total 5.2 million customers. Commercial customers totaling 440 thousand, account for 39% of the total energy sold. Approximately, 10 thousand industrial customers account for 31% of total energy sold.

The following table summarizes the customer count as at December 31, 2012 and 2011 and the corresponding electric consumption per customer class for the years ended December 31, 2012 and 2011:

Customer Class	No. of Customers (in thousands)		Electricity Sales (in <i>GWh</i>)		% Change	
	2012	2011	2012	2011	No. of Customers	Electricity Sales
Residential	4,735	4,580	9,779	9,344	3	5
Commercial	440	433	12,749	12,027	2	6
Industrial	10	10	10,111	9,080	—	11
Streetlights	4	4	132	141	—	(6)
Total	5,189	5,027	32,771	30,592	3	7

Other Services

Revenues from sale of other services pertain mostly to the revenues generated by *MIESCOR*, a construction and electro-mechanical engineering company with expertise in the fields of power and industrial plants, transmission and distribution, waterworks and telecommunications. *MIESCOR* is a subsidiary of *MERALCO*.

COSTS AND EXPENSES

Consolidated costs and expenses for the year ended December 31, 2012 amounted to ₱266,162 million, 11% higher compared with ₱238,969 million for the same period in 2011. The following table shows the breakdown of *MERALCO Group*'s consolidated costs and expenses for the years ended December 31, 2012 and 2011 by business segment:

	2012 (As restated)	%	2011 (As restated)	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Power ¹⁰	₱264,837	99	₱237,304	99	₱27,533	12
Other services	2,875	1	2,769	1	106	4
Inter-segment transactions	(1,550)	–	(1,104)	–	(446)	40
Total	₱266,162	100	₱238,969	100	₱27,193	11

Power

The details of costs and expenses are summarized in the following table:

	2012 (As restated)	%	2011 (As restated)	%	Increase/(Decrease)	
					Amount	%
<i>(Amounts in millions)</i>						
Purchased power	₱232,068	88	₱205,674	87	₱26,394	13
Salaries, wages and employee benefits	10,385	4	9,789	4	596	6
Depreciation and amortization	5,401	2	5,360	2	41	1
Contracted services	3,594	1	3,835	2	(241)	(6)
Others	13,389	5	12,646	5	743	6
Total	₱264,837	100	₱237,304	100	₱27,533	12

Costs and expenses of the power segment for the year ended December 31, 2012 amounted to ₱264,837 million, 12% higher compared with the ₱237,304 million in 2011.

Purchased power accounted for 88% of the total costs and expenses. It is the biggest component of the costs and expenses of *MERALCO's* power segment. *MERALCO's* power segment does not operate its own generation capacity and purchases all of the electricity that it distributes from *NPC* and its *SGCs*, the *WESM* and *IPPs*. The increase in purchased power was mainly due to higher average purchased power cost which was at ₱6.60 per *kWh* in 2012 compared with ₱6.22 per *kWh* in 2011, higher volume of electricity purchased from 33,081 *GWh* in 2011 to 35,176 *GWh* in 2012 and higher average cost of power purchased from *WESM* at ₱12.58 per *kWh* in 2012 compared with ₱8.38 per *kWh* in 2011.

The volume of energy purchased under long-term power supply contracts with *IPPs*, the *Sta. Rita Power Plant*, the *San Lorenzo Power Plant* and *QPPL*, represent 45% of *MERALCO's* Net Systems Input. Purchases from *PSAs*, *NPC SGCs* and other special programs account for 48%, while the balance of 7% was sourced from the *WESM*.

Salaries, wages and employee benefits increased by 6% from ₱9,789 million for the year ended December 31, 2011 to ₱10,385 million for the same period in 2012. The increase is mainly attributed to the fringe benefit tax expense in 2012 for the issued *ESPP* shares and annual salary increase for employees.

Contracted services decreased by 6% from ₱3,835 million for the year ended December 31, 2011 to ₱3,594 million for the same period in 2012.

Depreciation and amortization increased by 1% to ₱5,401 million in 2012 from ₱5,360 million in 2011. This is mainly due to additional depreciation from completed construction projects and newly installed capital assets.

¹⁰*Ibid.*

Other expenses consist of business taxes and permits, provision for probable charges and expenses from claims, provisions for doubtful accounts, costs of materials, transportation, and other corporate expenses. The 6% increase in other expenses is mainly due to higher provision for probable charges and expenses from claims.

Other Services

The costs and expenses of other services business segment for the year ended December 31, 2012 amounted to ₱2,875 million, 4% higher compared with ₱2,769 million in 2011. The details are as follows:

	2012		2011		Increase/(Decrease)	
	(As restated)	%	(As restated)	%	Amount	%
<i>(Amounts in millions)</i>						
Salaries, wages and employee benefits	₱1,241	43	₱1,075	39	₱166	15
Contracted services	627	22	602	22	25	4
Depreciation and amortization	176	6	144	5	32	22
Others	831	29	948	34	(117)	(12)
Total	₱2,875	100	₱2,769	100	₱106	4

Salaries, wages and other employee benefits increased by 15% from ₱1,075 million in 2011 to ₱1,241 million in 2012. The increase is mainly due to the provisions of the Collective Bargaining Agreement or CBA, and increase in the number of employees in most subsidiaries.

Contracted services increased by 4% from ₱602 million for the year ended December 31, 2011 to ₱627 million for the same period in 2012. This is mainly due to the implementation of the government-mandated wage adjustments.

Depreciation and amortization for the year ended December 31, 2012 amounted to ₱176 million, 22% higher compared with the same period in 2011 as a result of asset acquisitions of the subsidiaries.

Other expenses decreased by 12% from ₱948 million in 2011 to ₱831 million in 2012. This is mainly due to lower corporate expenses (e.g., materials, transportation, utilities) which are slightly mitigated by higher provision for doubtful accounts and taxes and other permit fees.

OTHER EXPENSES (INCOME)

The following table shows the breakdown of *MERALCO Group's* consolidated other income, net of expenses, for the years ended December 31, 2012 and 2011 by business segment:

	2012		2011		Increase/(Decrease)	
		%		%	Amount	%
<i>(Amounts in millions)</i>						
Power ¹¹	(₱3,138)	108	(₱1,689)	186	₱1,449	86
Other services	(38)	1	(99)	11	(61)	(62)
Inter-segment transactions	262	(9)	881	(97)	(619)	(70)
Total	(₱2,914)	100	(₱907)	100	₱2,007	221

¹¹*Ibid.*

Consolidated other income, net of expenses, for the year ended December 31, 2012 increased to ₱2,914 million, 221% higher compared with ₱907 million in 2011.

Power

Breakdown of other expenses (income) of power segment is summarized in the following table:

	2012	%	2011	%	Increase/(Decrease)	
					Amount	%
			(Amounts in millions)			
Interest and other financial income	(₱2,519)	80	(₱2,186)	129	₱333	15
Interest and other financial charges	1,518	(48)	1,435	(85)	83	6
Equity in net earnings of associates and joint ventures	(247)	8	(914)	54	(667)	(73)
Derivative mark-to-market gain (loss)	(40)	1	16	(1)	(56)	(350)
Foreign exchange gain	2	—	9	(1)	(7)	(78)
Others	(1,852)	59	(49)	4	1,848	3,771
Total	(₱3,138)	100	(₱1,689)	100	₱1,449	86

Other income, net of expenses, is higher by 86% from ₱1,689 million in 2011 to ₱3,138 million in 2012 due to increase in interest and other financial income and other income. Interest and other financial income in 2012 included the ₱730 million carrying charges related to the *LFT* recovery. Other income in 2012 included the approved *LFT* recovery of ₱1,571 million in April 2012.

NET INCOME ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The following table shows the breakdown of *MERALCO*'s net income attributable to the equity holders of *MERALCO* for the years ended December 31, 2012 and 2011 by business segment:

	2012		2011		Increase/(Decrease)	
	(As restated)	%	(As restated)	%	Amount	%
<i>(Amounts in millions)</i>						
Power ¹²	₱15,839	92	₱12,785	96	₱3,054	24
Other services	1,682	10	1,906	14	(224)	(12)
Inter-segment transactions	(404)	(2)	(1,431)	(10)	(1,027)	(72)
Total	₱17,117	100	₱13,260	100	₱3,857	29

Power

Net income attributable to equity holders of the parent is higher by 24% for the year ended December 31, 2012 compared with 2011 mainly due to the (i) net increase in income from power distribution as a result of higher volume sold, net of lower average distribution rate; and (ii) recognition of the *ERC*-approved recovery of *LFT* amounting to ₱2,301 million, inclusive of carrying charge of ₱730 million.

¹²*Ibid.*

Other Services

Net income from other services business segment attributable to the equity holders of the parent was 12% lower at ₱1,682 million in 2012 compared with ₱1,906 million in 2011. The decrease is mainly attributed to the divestment of the *MERALCO* from *Rockwell Land* in May of 2012, deconsolidation effect of Rockwell Land, offset by the ₱780 million one-time gain and higher service income generated by *MIESCOR* in 2011 compared with 2012.

LIQUIDITY AND CAPITAL RESOURCES

The following table shows *MERALCO*'s consolidated cash flows for the year ended December 31, 2013 and 2012 as well as the consolidated capitalization and other selected consolidated financial data as at December 31, 2013:

	For the Years Ended December 31		
	2013	2012	2011
	<i>(Amounts in millions)</i>		
<u>Cash Flows</u>			
Net cash from operating activities	₱37,144	₱36,244	₱31,934
Net cash used in investing activities	(30,392)	(9,549)	(6,816)
Net cash used in financing activities	(7,401)	(10,336)	(4,578)
Net increase (decrease) in cash and cash equivalents	(649)	16,359	20,540
<u>Capital Expenditures</u>	10,187	10,321	8,997
	2013	2012	2011
	<i>(Amounts in millions)</i>		
<u>Capitalization</u>			
Interest-bearing long-term financial liabilities			
Current portion	₱11,021	₱2,360	₱4,560
Noncurrent portion	20,756	20,466	19,816
Notes payable	1,814	1,787	67
Equity attributable to equity holders of the parent	75,162	67,902	62,156
<u>Other Selected Financial Data</u>			
Total assets	264,004	216,891	211,088
Utility plant and others	112,586	109,312	105,510
Cash and cash equivalents	59,851	60,500	44,141

As at December 31, 2013, *MERALCO Group*'s consolidated cash and cash equivalents totalled ₱59,851 million, ₱649 million lower than the balance in 2012. Following are the significant sources and uses of consolidated cash and cash equivalents for the year 2013: a) cash flows from operating activities of ₱37,144 million; b) proceeds from the bonds issuance amounting to ₱18,314 million, net of debt issue cost); c) proceeds from subscription receivable of ₱142 million; d) settlement of debt principal and interest of ₱13,460 million; e) capital expenditures of ₱10,187 million; f) investment in associates and a joint venture of ₱16,383 million; g) placement of short-term investments of ₱4,841 million, and; h) dividends payment amounting to ₱12,553 million.

Operating Activities

Consolidated net cash provided by operating activities for the year ended December 31, 2013 of ₱37,144 million is 2.5% higher versus 2012 mainly due to higher operating revenues.

Investing Activities

Consolidated net cash flows used in investing activities in 2013 amounted to ₱30,392 million, ₱20,843 million higher compared with ₱9,549 million used in 2012. This is mainly due to the investment and advances to associates and a joint venture amounting to ₱16,383 million and placement of short-term investments of ₱4,841 million.

Financing Activities

Consolidated net cash used in financing activities amounted to ₱7,401 million for the year ended December 31, 2013, 28.4% lower compared with ₱10,336 million in 2012. In 2013, the cash flows from financing activities includes the proceeds from the issuance of bonds amounting to ₱18,314 million, net of debt issue cost. Portion of the proceeds was used to pre-terminate existing loans in 2013. In 2013, *MERALCO* paid cash dividends to its shareholders totalling ₱12,553 million.

Debt Financing

On September 23, 2013, the *BOD* of *MERALCO* authorized the offer, sale and issuance by way of public offering in the Philippines, a 7- and 12-year corporate bonds, putable in 5 and 10 years, respectively, with an aggregate principal amount of up to ₱15 billion with an over-allotment option of up to ₱5 billion. The 12-year corporate bonds also include a call option where *MERALCO* may redeem (in whole but not in part only) the outstanding 12-year corporate bonds on the 7th year from issue date at the early redemption price of 101.0%.

On December 12, 2013, the ₱11.5 Billion Fixed Rate Putable Bonds due in 2020 and ₱7.0 Billion Fixed Rate Putable and Callable Bonds due in 2025, were listed on the Philippine Dealing and Exchange Corporation.

MERALCO's loan agreements require compliance with debt service coverage of 1.2 times calculated at specific measurement dates. The agreements also contain restrictions with respect to the creation of liens or encumbrances on assets, issuance of guarantees, mergers or consolidations, disposition of a significant portion of its assets and related party transactions.

As at December 31, 2013, *MERALCO* is in compliance with all covenants of the loan agreements.

Equity Financing

Consistent with the provisions of *PAS 32*, "Financial Instruments: Disclosure and Presentation", *MERALCO*'s preferred shares are presented as debt while the dividends declared are recorded as interest expense. Accumulated and unpaid dividends were accrued and classified as accrued interest payable. Coupon rate on such preferred share is fixed at 10%. The preferred shares were issued to service applications, which would require extension or new distribution facilities beyond a specific distance. Beginning April

8, 2005, such requirement was discontinued. Instead, as provided in the “Implementing Guidelines of the Magna Carta for Residential Electricity Consumers”, customers were required to advance the costs of extension of lines and installation of additional facilities. All of the redeemable preferred shares have been called for redemption as at June 30, 2011, consistent with the terms of the Preferred Shares Subscription Agreement. The unpaid dividends amounted to ₱250 million and ₱256 million as at December 31, 2013 and 2012, respectively. Interest is no longer accrued on the preferred shares, which have been called for redemption.

As at December 31, 2013 and 2012, *MERALCO*'s capital stock consists of:

<i>(Amounts in millions, except par value and number of shares)</i>	2013	2012
Common stock - ₱10 par value		
Authorized - 1,250,000,000 shares	₱12,500	₱12,500
Issued - 1,127,271,117 shares	11,273	11,273
Treasury - 172,412 shares as at December 31, 2013 and 171,853 shares as at December 31, 2012	(11)	(11)

Treasury shares represent subscribed shares and the related rights of employees who have opted to withdraw from the *ESPP* in accordance with the provisions of the *ESPP* and which *MERALCO* purchased. For the years ended December 31, 2013 and 2012, a total of 559 shares and 25,830 shares, respectively, were acquired from employees who have opted to cancel their participation in the *ESPP*.

Cash dividends declared to shareholders for the years ended December 31, 2013 and 2012 amounted to ₱11,496 million and ₱9,129 million, respectively.

The table below summarizes the cash dividends declared in 2013 and 2012:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
				<i>(In millions)</i>
February 27, 2012	March 23, 2012	April 23, 2012	₱4.10	₱4,621
July 30, 2012	August 29, 2012	September 24, 2012	4.00	4,508
February 25, 2013	March 26, 2013	April 24, 2013	6.10	6,875
July 29, 2013	August 27, 2013	September 20, 2013	4.10	4,621

On February 27, 2012, the *BOD* of *MERALCO* approved the declaration of its investment in common shares of *Rockwell Land* as property dividends to all common stockholders as of March 23, 2012. Filipino common shareholders were distributed 2.82 shares for every *MERALCO* share held while the foreign common stockholders were paid the cash equivalent of the property dividends. Such property dividends were paid on May 14, 2012, within five (5) trading days after approval of the property dividends by the *SEC* and registration of the *Rockwell Land* shares under the Securities Regulation Code and the listing thereof with the *PSE* on May 11, 2012. On April 25, 2012, the *SEC* approved the property dividend declaration.

On March 17, 2014, the *BOD* approved cash dividend of ₱6.45 per share to all stockholders of record as at April 15, 2014, payable on May 8, 2014.

RISK FACTORS

The major factors affecting *MERALCO*'s financial position and results of operations are:

- Regulated rates and cost recoveries
- Sales volume and Philippine economic conditions
- Electricity supply
- Industry restructuring

Regulated Rates and Cost Recoveries

The most significant determinants of *MERALCO*'s and *CEDC*'s rate structure vis-à-vis operating results are “allowable returns” and “permitted cost recoveries”. Rates billed by *MERALCO* and *CEDC* are approved by the *ERC* and are set to allow a reasonable rate of return on investments. As distribution utilities serving captive customers, *MERALCO* and *CEDC* are allowed full pass-through of purchased power costs, system loss up to an annual cap enforced by the *ERC*, and taxes.

Performance-Based Regulation or PBR

MERALCO was among the Group A entrants to the *PBR*, together with two other private *DUs*.

Rate-setting under *PBR* is governed by the Rules on Distribution Wheeling Rates or *RDWR*. The *PBR* scheme sets tariffs based on the regulated asset base of the *DUs*, and the required operating and capital expenditures once every regulatory period or *RP*, to meet operational performance and service level requirements responsive to the needs for adequate, reliable and quality power, efficient service, and growth of all customer classes in the franchise area as approved by the *ERC*. The *PBR* also employs a mechanism that penalizes or rewards a *DU* depending on its network and service performance.

As part of the *PBR*, *MERALCO* implements payouts to customers for instances when its performance is beyond the guaranteed service levels or *GSL*.

Rate filings and settings are done on a *RP* basis. One (1) *RP* consists of four (4) Regulatory Years or *RYS*. An *RY* for *MERALCO* begins on July 1 and ends on June 30 of the following year. As at December 31, 2013, *MERALCO* is operating in the second half of the third *RY* of the third *RP*. The third *RP* is from July 1, 2011 to June 30, 2015.

Pass-through of Allowable Costs

The pass-through of allowable costs or costs that do not entail a revision of the rate base and/or rate of return of *MERALCO* is governed by various adjustment mechanisms promulgated by the *ERC*.

In approving *MERALCO*'s unbundled rate in May 2003, the *ERC* prescribed a generation charge that will be adjusted under the Generation Rate Adjustment Mechanism, or *GRAM*. This has since been superseded by the Guidelines for the Automatic Adjustment of Generation Rates and System Loss Rates by Distribution Utilities. The monthly automatic adjustment under the Automatic Generation Rate Adjustment or *AGRA*, mechanism provides timely price signals to consumers. While the *GRAM* only provided for changes in the generation charge, the new mechanism also allows the monthly adjustment

of the system loss charge. Implementation of the guidelines started with the November 2004 billing cycle.

The *ERC*'s approval of *MERALCO*'s second filing under *GRAM* was questioned before the *Supreme Court*, for failure by *MERALCO* and the *ERC* to comply with Section 4 (e) Rule 3 of *EPIRA*'s Implementing Rules and Regulations or *IRR*, which required publication, notice, and hearing of an application prior to issuance of an Order. On August 16, 2006, the SC ruled with finality that strict compliance with the requirements under the *IRR* of the *EPIRA* is jurisdictional and applies to any adjustment to the retail rate, including those for pass-through costs. The *AGRA* was then suspended beginning September 2006 and *MERALCO* could adjust generation and other pass-through charges only after the filing and approval by the *ERC* of an appropriate application.

On June 7, 2007, the Joint Congressional Power Commission approved amendments to Section 4 (e), Rule 3 of the *EPIRA*'s *IRR* that exempt the adjustments of pass-through electric rate components from the jurisdictional and hearing requirements of the *IRR*. The amendments were subsequently promulgated by the Department of Energy or *DOE*, on June 21, 2007. Thereafter, the *ERC* lifted the suspension of the *AGRA*, which allowed *MERALCO* to resume the monthly updating of generation and system loss charges beginning July 2007.

On August 12, 2009, the *ERC* issued its Resolution No. 16, Series of 2009, adopting the "Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities". These rules govern the recovery of pass-through costs, including over- or under-recoveries in the following bill components: Generation Charge, Transmission Charge, System Loss Charge, Lifeline rate subsidies, Local franchise and business taxes.

The rules will also synchronize the various confirmation processes for the foregoing charges, in which the *ERC* will verify whether the *DU* incurred over- or under-recoveries in the implementation of the said charges. Luzon *DUs*, such as *MERALCO*, were required to file not later than October 30, 2009 their consolidated applications to resolve over- or under-recoveries accumulated from the start of their rate unbundling until December 2008. Subsequent filings will be every three (3) years thereafter.

On October 8, 2009, *MERALCO* filed a petition at the *ERC* seeking an amendment to the *ERC*'s Resolution No. 16, Series of 2009. In particular, *MERALCO* proposed a modification to the formula used in confirming the system loss charges of *DUs*, shifting the reckoning of the system loss cap from a monthly to an annual reckoning to more fairly reflect the actual system loss performance of *DUs*.

On October 18, 2010, the *ERC* ruled on *MERALCO*'s Petition and agreed that there is a need to address the mismatch between the billing periods of the *DUs* and of their suppliers in the confirmation of the system loss. However, the *ERC* did not adopt *MERALCO*'s proposed modification to the formula and instead prescribed a new formula. Resolution No. 21, Series of 2010 adopted the new formula and correspondingly amended the one prescribed in Resolution No. 16, Series of 2009. The Resolution also prescribed the period of filing for the *DUs*' consolidated applications, which for Luzon *DUs* was by March 31, 2011 and setting March 31, 2011 (covering adjustments implemented from the rate unbundling until the billing month of December 2010) and March 31, 2014 (covering adjustments from January 2011 to December 2013) as the new deadlines for *DUs* in Luzon to file their respective applications. Subsequent filings shall likewise be every three (3) years thereafter.

Applications for the Recovery of Generation Costs and SL Charges

MERALCO filed separate applications for the full recovery of generation costs, including value-added tax or VAT, incurred for the supply months of August 2006 to May 2007 or total under-recoveries of ₱12,679 million for generation charges and ₱1,295 million for SL charges.

The separate applications for the full recovery of generation charges have been approved by the *ERC* in its decisions released on January 18, 2008, September 3, 2008 and August 16, 2010.

As at December 31, 2013, the remaining balance of ₱137 million of such unrecovered generation costs will be billed subsequent to December 2013 at the rate of ₱0.0314 per *kWh* until fully recovered. The amount is recoverable within 12 months and is included in the "Trade and other receivables" account.

With respect to the ₱1,295 million SL charge under-recoveries, the *ERC* ordered *MERALCO* to file a separate application for the recovery of SL adjustments after the *ERC* confirms the transmission rate to be used in the calculation of the SL rate in accordance with the SL rate formula of the Automatic Generation Rate Adjustments Guidelines. *MERALCO* has filed the application for recovery of the ₱1,295 million SL charge under-recoveries with the *ERC*. This was included in the Consolidated Application of over- or under-recoveries in generation, transmission, SL and lifeline subsidy charges filed on March 31, 2011 with the *ERC*. Hearings were completed on October 25, 2011. On December 12, 2011, *MERALCO* filed for the admission of its Supplemental Application. An expository hearing was conducted on February 1, 2012. As at March 17, 2014, *MERALCO* has already filed its Formal Offer of Evidence or *FOE*, and is awaiting the final resolution by the *ERC*.

System Loss

On December 8, 2008, the *ERC* promulgated a resolution providing for a lower maximum rate of SL (technical and non-technical) that a utility can pass on to its customers. The revised SL cap is 8.5% for private utilities, effective January 2010 billing. This is one percentage point lower than the SL cap of 9.5% provided under *RA No. 7832*. The actual volume of electricity used by *MERALCO* (administrative loss) is treated as part of the operation and maintenance expense beginning July 2011. The manner by which the utility is rewarded for its efforts in SL reduction is addressed by the *ERC* in the *PIS* under *PBR*.

On December 8, 2009, *MERALCO* filed a Petition to amend the said Resolution with an urgent prayer for the immediate suspension of the implementation of the new SL cap of 8.5% starting January 2010. The proposed amendment is aimed at making the Resolution consistent with the provisions of *RA No. 9136* and *RA No. 7832*, by increasing the SL cap to not less than 9%. The hearing on the Petition was conducted on November 18, 2010. Thereafter, *MERALCO* was directed to submit its *FOE*.

MERALCO's 12 month average system loss of 6.92% as at December 31, 2013 improved by 12 basis points from the 7.04% registered in 2012. *CEDC*'s system loss of 4.33% in 2013 was well within the 8.5% cap set by the *ERC* for the private *DUs*.

Sales Volume and Philippine Economic Conditions

The sale of electric energy is driven mainly by prevailing economic conditions and the number of customers being served by *MERALCO*. *MERALCO*'s franchise area accounts for an estimated 50% of the Philippines' Gross Domestic Product or *GDP*, with 37% from Metro Manila.

The favourable economic environment, supported by robust overseas Filipino workers, business process outsourcing and capital inflows, low interest rate and inflation rates, 'wealth creation' associated with significantly higher equity and property prices, and sustained confidence in the National Government, boosted strong domestic consumption and local and foreign investments. These affected per capital electricity consumption.

In 2013, *MERALCO Group's* energy sales volume was 34,084 *GWh*, 4% higher compared than 2012. The growth in sales volume in 2013 was mainly due to the following factors: increased use of cooling load due to warmer temperature in the first half of 2013, higher consumption of residential customers due to benign inflation, and increased demand of industrial and commercial sectors particularly from food and beverages, rubber and plastics, semiconductor, real estate, *BPO* industry, and entertainment, malls, hotels, and restaurants. *MERALCO* still managed to grow customers by 3% largely from the commercial and residential sectors. *MERALCO* has 5,368 thousand customers as at December 31, 2013.

Average temperature in 2013 was 28.2°C or about 0.3°C warmer throughout. *MERALCO* peak demand was at 5,928 *MW*, which occurred on May 8, 2013, 5.2% higher compared with the peak demand on May 10, 2012 of 5,633 *MW*.

Electricity Supply

MERALCO purchases all of the power it distributes from the privatized plants of the *NPC-SGCs*, *IPPs* and *WESM*. *WESM* is a venue where suppliers and buyers trade electricity as a commodity. For the year ended December 31, 2013, *MERALCO* purchased 36% of its requirements from *IPPs*, 59% from the privatized plants of *NPC* and other renewable power plants, and 5% from the *WESM*.

MERALCO and *NPC* had a *TSC*, effective the earlier of five (5) years from November 16, 2006 up to December 25, 2011 or one year after the introduction of Open Access, should *RCOA* be in place within the five-year contract period. Two addenda for additional contracted volumes were signed, the last being in 2010. The adjusted contracted volume was for a total of more than 40,000 *GWh* up to 2011.

On December 26, 2011, the *TSC* with *NPC* was extended until December 25, 2012 or three months after the implementation of the *RCOA*, whichever comes first.

As a result of the extension of the *TSC*, the Customer Choice Program or *CCP*, which is a joint program of *NPC* and *MERALCO* aimed at providing *NPC* time-of-use or *TOU*, benefits to qualified customers, has also been extended to be co-terminus with the *TSC*. The *CCP* program expired on December 25, 2012.

With respect to the *TSC*, *MERALCO*, *NPC* and *PSALM* then executed a Memorandum of Agreement which further extended the *TSC* until June 25, 2013.

Following are the *PSAs* entered into by *MERALCO*:

Date	Power Supplier	Plant/contracted capacity	Terms of <i>PSA</i>
December 12, 2011	South Premiere Power Corporation or <i>SPPC</i>	Ilijan Power Plant in Batangas, for the full 1,180 <i>MW</i> net capacities	Under the <i>PSA</i> , <i>MERALCO</i> will procure power from <i>SPPC</i> until December 25, 2019, with an option to extend the term for another three years.
December 21, 2011	Masinloc Power Partners Co., Ltd. or <i>MPPCL</i>	The initial contracted capacity is 330 <i>MW</i> , to increase to 430 <i>MW</i> by December 26, 2015	The <i>PSA</i> has a term of seven years and can be extended by the parties for another three years.
December 26, 2011	SEM-Calaca Power Corporation, or <i>Sem-Calaca</i>	The initial contracted capacity is 210 <i>MW</i> and will be increased to 420 <i>MW</i> upon the commercial operation of the plant's Unit 1.	Term of seven years, which may be extended by the parties for another three years.
February 29, 2012	Therma Luzon, Inc., or <i>TLI</i>	Pagbilao coal-fired power plant with contracted capacity of 350 <i>MW</i> located in Quezon Province	Term of seven years, which may be extended for three years upon agreement of parties
June 25, 2012	San Miguel Energy Corporation, or <i>SMEC</i>	Sual coal-fired power plant with initial contracted capacity of 200 <i>MW</i> to increase to 500 <i>MW</i> by December 26, 2012	Term of seven years, which may be extended up to five years upon agreement of parties
April 26, 2012	Pangea Green Energy Philippines, Inc., or <i>PGEP</i>	Biogas power plant methane gas with a total nominal generating capacity of 1 <i>MW</i> .	Term of two years from the delivery period commencement date, unless amended by the parties.

On January 30, 2012, the *ERC* indefinitely extended the provisional authority to the Contract of Supply of Electricity with Bacavalley Energy Inc., the owner/operator of a 4 *MW* landfill gas-to-power plant.

In March 2012, the application for approval of the *PSAs* was filed with the *ERC*. In separate Decisions dated December 17, 2012, the *ERC* approved with modifications the *PSAs* of *MERALCO* with *MPPCL*, *SPPC*, *Sem-Calaca*, *TLI* and *SMEC*.

Motions for Reconsideration were filed regarding the *ERC* decisions on the *PSAs* with *SPPC*, *Sem-Calaca* and *SMEC*. *MERALCO* is awaiting the decisions of the *ERC*.

With respect to the motion for reconsideration of the Decision on the *PSA* of *Sem-Calaca*, hearings have been scheduled.

On March 16, 2012, *MPower* signed a new *PSA* with *MPPCL* for 30 *MW* of contracted capacity from the Masinloc coal-fired power plant in Zambales for seven (7) years, extendable for three (3) years upon agreement of the parties.

On December 27, 2012, *MERALCO* executed the *PSAs* with *TLI* and *Aboitiz Power* to cover the volume needed by *MERALCO* during the six-month transition period before the start of the commercial operations of *RCOA*. Under the *PSAs* with *TLI* and *Aboitiz Power*, *MERALCO* will procure power from *TLI* and *Aboitiz Power* from the expiration of the Transition Supply Contract or *TSC* until June 25, 2013 conditioned upon *ERC* approval. The said *PSAs* had been submitted to the *ERC* for approval on January 2, 2013. The hearings on both *PSAs* have already been terminated and are already submitted for decision.

Under the *PSAs*, fixed capacity fees and fixed operating maintenance fees are recognized monthly based on their contracted capacities. The annual projection of these payments is shown in the table below:

Year	Contracted Capacity	Fixed Payment Amount
	<i>(In MW)</i>	<i>(In Millions)</i>
2014	3,000	₱35,419
2015	3,084	37,775
2016	3,114	39,865
2017	3,114	39,574
2018	2,880	39,198
2019	2,460	33,864

Industry Restructuring

Under the *EPIRA*, the Philippine power industry continues to undergo fundamental restructuring.

These restructuring measures include:

- The deregulation of, and introduction of competition in, power generation and supply activities and pricing;
- The privatization of the *NPC*'s power generating assets and *IPP* contracts;
- The unbundling of the relative costs of the various segments of the power supply chain and reflecting these in the bills to customers;
- Freedom of consumers to choose electricity suppliers;
- Open and non-discriminatory access in the networks of *DUs*, subject to the fulfillment of certain conditions precedent;
- The implementation of the *WESM*; and
- Removal of inter-grid, intra-grid, and inter-class cross-subsidies.

ELECTRIC POWER INDUSTRY DEVELOPMENTS AND UPDATES

1. Implementation of Performance-Based Regulation or *PBR*

As *DUs*, *MERALCO* and *CEDC* are subject to the rate-making regulations and regulatory policies of the *ERC*. Billings to customers are itemized or “unbundled” into a number of bill components that reflect the various units incurred in providing electric service. The adjustment to each bill component is governed by mechanisms promulgated and enforced by the *ERC*, mainly: [i] the “Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities,” which govern the recovery of pass-through costs, including over- or under-recoveries of the bill components, namely, (a) generation charge, (b) transmission charge, (c) system loss charge, (d) lifeline rate subsidies, (e) *LFT* and (f) business taxes; and [ii] the modified “Rules for the Setting of Distribution Wheeling Rates for Privately Owned Electricity

Distribution Utilities Operating under Performance Based Regulation (First Entry Group: Third Regulatory Period) or *RDWR*”, which govern the determination of the *MERALCO*’s distribution, supply, and metering charges.

The rate-setting mechanism of *CEDC* is likewise in accordance with *ERC* regulations. The following is a discussion of matters related to rate-setting of *MERALCO* and *CEDC*:

Rate Applications

CEDC Rate Unbundling

On August 19, 2011, *CEDC* received an *ERC* Order to implement certain revisions of its schedule of rates effective on its August 2010 billing cycle, after the *ERC* approved *CEDC*’s unbundling application pursuant to Section 36 of *RA* No. 9136, *EPIRA*.

Thereafter, on June 21, 2012, *CEDC* received an Order from the *ERC* (docketed on May 28, 2012) directing *CEDC* to refund to its customers the amount of ₱0.8 million (the difference between its then existing rates and the rates approved by the *ERC*) at a rate equivalent to ₱0.0067 per *kWh* for a period of five (5) months or until the said amount shall have been fully refunded. The refund process was completed by *CEDC* in October 2012.

PBR

a. MERALCO

Maximum Average Price or MAP for RY 2008 and RY 2009

On January 11 and April 1, 2008, *MERALCO* filed separate applications for the approval of its proposed translation of the *MAP* for *RY* 2008 and *RY* 2009, respectively, into different rate schedules for its various customer segments. A portion of the distribution charge under-recoveries as a result of the delay in the implementation of *PBR* was incorporated in the proposed *MAP* for *RY* 2009.

In April 2009, the *ERC* approved the implementation of *MERALCO*’s average distribution rate of ₱1.2227 per *kWh* effective billing period of May 2009. This rate is inclusive of the under-recoveries for calendar year 2007 of ₱0.1285 per *kWh*.

On May 28, 2009, certain electricity consumer groups filed a Petition with the Court of Appeals, or *CA*, questioning the decision and Order of the *ERC* on *MERALCO*’s rate translation application for *RY* 2008 and *RY* 2009. In a decision dated January 27, 2010, the *CA* denied the Petition. Consequently, the consumer groups brought the case to the *Supreme Court*. Comments and responses were filed by both parties with a Manifestation filed by *MERALCO* on January 26, 2011. As at March 17, 2014, the *Supreme Court* has yet to render its decision on this case.

MAP for RY 2012

On June 21, 2011, *MERALCO* filed its application for the approval of its *MAP* for *RY* 2012 and its translation into rate tariffs by customer category. On October 6, 2011, the *ERC* provisionally approved the *MAP* for *RY* 2012 of ₱1.6012 per *kWh* and the rate translation per customer class was reflected commencing with the October 2011 customer bills. Hearings for the final approval of the application have been completed and all parties have submitted their respective memoranda. As at March 17, 2014, the application is pending final approval by the *ERC*.

MAP for RY 2013

On June 11, 2012, the *ERC* provisionally approved the *MAP* for *RY* 2013 of ₱1.6303 per *kWh* which was reflected starting with the July 2012 customer bills. Hearings on this case have been completed and *MERALCO* is awaiting the final decision of the *ERC*.

MAP for RY 2014

On April 1, 2013, *MERALCO* filed its application for the approval of its *MAP* for *RY* 2014 of ₱1.6510 per *kWh* and the translation thereof into rate tariffs by customer category. Hearing was completed on May 9, 2013. *MERALCO* filed its *FOE* on May 10, 2013 and the case pending decision of the *ERC*. On June 10, 2013, the *ERC* provisionally approved the *MAP* for *RY* 2014 of ₱1.6474 per *kWh* and the rate translation per customer class. As at March 17, 2014, the application is pending final approval by the *ERC*.

b. CEDC

CEDC was among the four (4) Group D entrants to the *PBR*. Similar to *MERALCO*, it is subject to operational performance and service level requirements approved by the *ERC*. The second *RP* of *CEDC* began on October 1, 2011 and ends on September 30, 2015.

Reset Application and MAP for RY 2012

In compliance with the *ERC*'s *PBR* rate setting mechanism, on September 24, 2010, *CEDC* filed a reset application for the approval of its Annual Revenue Requirement or *ARR* and Performance Incentive Scheme or *PIS* with the *ERC*. *CEDC* filed its revised application on November 3, 2010, which underwent a series of hearings and public consultations in 2011. The *ERC* issued *CEDC*'s Final Determination on August 5, 2011. Subsequently, *CEDC* filed with the *ERC* its application for *RY* 2012 Rate Translation into the different customer classes.

On April 10, 2012, the *ERC* approved with modification, *CEDC*'s application for the approval of the translation into distribution rates of different customer classes for the first *RY* of the approved *ARR* under the *PBR* for the *RP* October 1, 2011 to September 30, 2015. *CEDC* implemented the approved distribution, supply and metering charges of ₱0.8527 per *kWh* and the new customer segments in its June 2012 billing.

MAP for RY 2013

On August 30, 2012, *CEDC* filed its application for the approval of its *MAP* for *RY* 2013. The *ERC*, on December 17, 2012, approved a *MAP* of ₱0.8953 per *kWh*. The revised rates based on the approved *MAP* 2013 were implemented by *CEDC* starting January 2013.

2. Application for Recoveries

Applications for the Recovery of Generation Costs and System Loss Charges

MERALCO filed separate applications for the full recovery of generation costs, including value-added tax or *VAT*, incurred for the supply months of August 2006 to May 2007 or total under-recoveries of ₱12,679 million for generation charges and ₱1,295 million for *SL* charges.

The separate applications for the full recovery of generation charges have been approved by the *ERC* in its decisions released on January 18, 2008, September 3, 2008 and August 16, 2010.

As at December 31, 2013, the remaining balance of ₱137 million of such unrecovered generation costs will be billed subsequent to December 2013 at the rate of ₱0.0314 per *kWh* until fully recovered.

With respect to the ₱1,295 million *SL* charge under-recoveries, the *ERC* ordered *MERALCO* to file a separate application for the recovery of *SL* adjustments after the *ERC* confirms the transmission rate to be used in the calculation of the *SL* rate in accordance with the *SL* rate formula of the Automatic Generation Rate Adjustments Guidelines. *MERALCO* has filed the application for recovery of the ₱1,295 million *SL* charge under-recoveries with the *ERC*. This was included in the Consolidated Application of under/over recoveries in generation, transmission, *SL* and lifeline charges filed on March 31, 2011 with the *ERC*. Hearings were completed on October 25, 2011. On December 12, 2011, *MERALCO* filed for the admission of its Supplemental Application. An expository hearing was conducted on February 1, 2012. As at March 17, 2014, *MERALCO* has already filed its *FOE* and is awaiting the final resolution by the *ERC*.

Inter-Class Cross Subsidy and Lifeline Subsidy

MERALCO filed separate applications to recover inter-class cross subsidy (on November 14, 2007) and lifeline subsidy (on February 19, 2008).

In a decision dated November 16, 2009, the *ERC* authorized *MERALCO* to recover the interclass cross subsidy under-recoveries covering the period June 2003 to October 2006 amounting to ₱1,049 million and total lifeline subsidy under-recoveries covering the period June 2003 to December 2007 amounting to ₱856 million.

In December 2009, *MERALCO* implemented the decisions of the *ERC* on the interclass cross and lifeline subsidies. The balances of inter-class cross subsidies and lifeline subsidies were fully recovered in April 2013 and December 2013, respectively.

Consolidated Applications for the Confirmation of Over/Under-recoveries of Pass-through Charges

On August 12, 2009, the *ERC* issued Resolution No. 16, Series of 2009, adopting the "Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities." These rules govern the recovery of pass-through costs, including over- or under-recoveries with respect to the following bill components: generation charge, transmission charge, *SL* charge, lifeline and interclass rate subsidies, *LFT* and business tax. On October 18, 2010, the *ERC* promulgated *ERC* Resolution No. 21, Series of 2010, amending certain formula contained in *ERC* Resolution No. 16, Series of 2009, and setting March 31, 2011 (covering adjustments implemented until the billing month of December 2010) and March 31, 2014

(covering adjustments from January 2011 to December 2013) as the new deadlines for *DUs* in Luzon to file their respective applications. Subsequent filings shall be made every three years thereafter.

On March 31, 2011, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries accumulated from June 2003 to December 2010 in compliance with Resolution No. 16, Series of 2009, as subsequently amended by Resolution No. 21, Series of 2010. Hearings were completed on October 25, 2011. On December 8, 2011, *MERALCO* filed an Omnibus Motion praying, among other things, for the admission of the Supplemental Application. In an Order dated December 12, 2011, the *ERC* granted *MERALCO*'s Omnibus Motion and admitted its Supplemental Application. Accordingly, hearings on the Supplemental Application were conducted where *MERALCO* presented additional evidence. *MERALCO* filed its Formal Offer of Evidence or *FOE*, on September 13, 2012. The consolidated filing includes net generation charge under-recoveries of ₱1,000 million, net transmission charge over-recoveries of ₱111 million, net lifeline subsidy under-recoveries of ₱9 million and net *SL* over-recoveries of ₱425 million, excluding any applicable carrying charges.

On July 6, 2012, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries for the calendar year 2011. The consolidated filing includes net generation charge under-recoveries of ₱1,826 million, transmission charge under-recoveries of ₱253 million, net lifeline subsidy under-recoveries of ₱39 million and *SL* over-recoveries of ₱445 million, excluding any applicable carrying charges. Hearings on the application have been terminated and *MERALCO* has submitted its *FOE* on January 25, 2013. As at March 17, 2014, the application is pending decision by the *ERC*.

Application for Recovery of LFT

On March 25, 2011, *MERALCO* filed with the *ERC* an Application for recovery of *LFT* paid but are not yet billed to customers for the period beginning first quarter of 1993 up to the second quarter of 2004 for five (5) provinces, namely: Bulacan, Batangas, Cavite, Laguna and Rizal; and 14 cities, namely: San Jose Del Monte, Batangas, San Pablo, Tagaytay, Lucena, Mandaluyong, Marikina, Quezon, Caloocan, Pasay, Las Piñas, Manila, Pasig and Calamba. The *LFT* is recognized as a legitimate and reasonable *DU* expense in the *ERC*'s unbundling decision.

In a Decision dated February 27, 2012, the *ERC* released its Order approving with modifications *MERALCO*'s application. The *ERC* approved recovery of *LFT* amounting to ₱1,571 million plus carrying charges of ₱730 million. As directed by the *ERC*, the recovery was reflected as a separate item in the *MERALCO* billing statement to its customers beginning April 2012. As at December 31, 2013, a total of ₱856 million *LFT* and carrying charges have been billed to affected customers.

3. Revised System Loss Caps

On December 8, 2008, the *ERC* promulgated a resolution providing for a lower maximum rate of *SL* (technical and non-technical) that a utility can pass on to its customers. The revised *SL* cap is 8.5% for private utilities, effective January 2010 billing. This is one percentage point lower than the *SL* cap of 9.5% provided under *RA* No. 7832. The actual volume of electricity used by *MERALCO* (administrative loss) is treated as part of the operation and maintenance expense beginning July 2011. The manner by which the utility is rewarded for their efforts in *SL* reduction is addressed by the *ERC* in the *PIS* under *PBR*.

On December 8, 2009, *MERALCO* filed a Petition to amend the said Resolution with an urgent prayer for the immediate suspension of the implementation of the new *SL* cap of 8.5% starting January 2010. The proposed amendment is aimed at making the Resolution consistent with the provisions of *RA No. 9136* and *RA No. 7832*, by increasing the *SL* cap to not less than 9%. The hearing on the Petition was conducted on November 18, 2010. Thereafter, *MERALCO* was directed to submit its *FOE*.

4. Benefit Sharing Scheme to Lower System Loss

On January 26, 2011, *MERALCO*, together with Private Electric Power Operators Association Inc. or *PEPOA* and Philippine Rural Electric Cooperative Association or *PHILRECA*, filed a joint petition to the *ERC* to initiate rule-making praying that a Resolution be issued adopting the *Proposed Guidelines for the Implementation of an Incentive Scheme to Lower the System Losses of Private Distribution Utilities and Electric Cooperatives to Level Below the System Loss Cap, for the Benefit of End-Users*. This was aimed to encourage the *DUs* to reduce system loss levels below the cap set by the *ERC* and benefit the end-users through lower system loss charge rates. Public hearings were conducted and completed on June 15, 2011.

On December 11, 2012, the *ERC* posted on its website the second draft of the *Rules to Govern the Implementation of a Benefit Sharing to Lower the System Losses of Electric Distribution Utilities*. The salient points of *ERC*'s draft rules includes calculation of System Loss Charge using the prevailing system loss cap or the lowest consecutive five year average system loss, whichever is lower, and an equitable sharing (50-50) of incentives between the customer and the *DU* on the savings which is the difference between the lower of this system loss level and the *DU*'s actual system loss. Any system loss reward from the Performance Incentive Scheme or *PIS* under the *RDWR* for private *DUs* or the *RSEC-WR* for *ECs*, shall be offset from the rewards the *DU* will receive from this Benefit-Sharing scheme, except when the net benefit from this scheme is less than the *PIS* rewards of the *DU*, in which case the *DU* will retain the rewards under the *PIS* and forego its share under this Benefit-Sharing Scheme. The foregone share of the *DU* shall be added to the End-user share correspondingly. The implementation of this scheme is dependent on the release of the final set of rules by the *ERC*.

5. Retail Competition

On February 24, 2012, the *DOE* issued a department circular designating the *PEMC* as the Central Registration Body or *CRB*, under the *RCOA*. The *CRB* is tasked to develop market infrastructure, systems and processes capable of supporting *RCOA* registration, customer switching and information exchange among industry participants.

On May 9, 2012, the *DOE* issued another department circular, prescribing the general policies for the implementation of *RCOA*. The circular provides the overall direction *DOE* intends to take in developing the policy framework for *RCOA* implementation.

On September 27, 2012, the *DOE* and the *ERC* issued a joint statement setting the initial *RCOA* implementation on December 26, 2012. The joint statement clarified that the *RCOA* commencement is on a phase-in and partial implementation of the program, with the first six (6) months of *RCOA* implementation (December 26, 2012 – June 25, 2013) allotted as the Transition Period to allow all concerned parties to undertake their respective preparations to operationalize the mechanism for *RCOA*. An initial *RCOA* Commercial Operation using an interim *IT* system started on June 26, 2013.

On December 17, 2012, the *ERC* issued Resolution No. 16 series of 2012 adopting the Transitory Rules for the implementation of *RCOA*. The resolution provides the detailed responsibilities of industry participants during the *RCOA* transition period.

On March 22, 2013, the *ERC* released a resolution that directed all *DUs* and licensed *RES* in Luzon and Visayas to disclose to the *ERC* their capacity and energy allocations for the customers they intend to serve. *MERALCO* complied with the directive.

On March 26, 2013, the *PEMC* began the *RCOA* Trial Operations Program, a nine-week test period participated in by the various entities and service providers of *RCOA*.

On June 19, 2013, the *ERC* issued a resolution adopting the Supplemental Rules to the Transitory Rules for the implementation of *RCOA*. The resolution seeks to prevent contestable customers who have yet to execute a Retail Supply Contract or *RSC*, with a *RES* from being disconnected or transferred to Supplier of Last Resort or *SoLR*, service upon the commencement of initial commercial operations of *RCOA*. Qualified contestable customers who fail to enter into a *RSC* with a *RES* shall be deemed to stay with their current *DU* until December 26, 2013 or until such time that it is able to find a *RES* provided that they inform the *DU*.

In accordance with the *ERC*'s "Transitory Rules for the Initial Implementation of Open Access and Retail Competition", commercial operations of *RCOA* began on June 26, 2013.

Nineteen *RESs* were licensed by the *ERC* to provide competitive retail supply service to eligible contestable customers.

On July 22, 2013, the *DOE* issued a circular promulgating the Retail Market Manuals for the following: Registration Criteria and Procedures, Market Transactions Procedures, Disclosure and Confidentiality of Contestable Customer Information, and Metering Standards and Procedures.

On September 4, 2013, the *ERC* conducted a public consultation on its proposed amendments to the *RES Licensing Rules*, for which *MERALCO* submitted comments and participated in the public consultation.

As at December 31, 2013, there are about 782 contestable customers in *MERALCO*'s franchise area. However, out of said number only 287 have already switched to their respective *RESs*. There are 167 contestable customers who have chosen *MPower* to become their *RES*. While other contestable customers obtained their supply from other *RESs*.

6. Philippine Economic Zone Authority or *PEZA*, Registration – *ERC* Jurisdiction

On September 13, 2007, *PEZA* issued "Guidelines in the Registration of Electric Power Generation Facilities/Utilities/Entities Operating Inside the Ecozones" and "Guidelines for the Supply of Electric Power in Ecozones." Under these Guidelines, *PEZA* effectively bestowed upon itself franchising and regulatory powers in Ecozones operating within the legislative franchise areas of *DUs* which are under the legislatively-authorized regulatory jurisdiction of the *ERC*. The Guidelines are the subject of an injunction case filed by the *DUs* at the Regional Trial Court-Pasig or *RTC*-Pasig.

In support of the government's objective of providing lower cost to Ecozone locators, *MERALCO* entered into a Memorandum of Agreement or *MOA*, with *NPC* on September

17, 2007 for the provision of special Ecozone rates to high load factor *PEZA*-accredited industries. The *ERC* authorized the immediate implementation of the Ecozone Rate Program or *ERP*. The program expired in December 2012.

The *ERP* was initially scheduled to expire by December 25, 2011 but has been extended twice and was terminated as at December 25, 2012.

In January 2013, *MERALCO* entered into a tripartite agreement with *PEZA* and Trans-Asia Oil and Energy Development Corporation for the sale of power to Cavite Special Economic Zone or *CSEZ*, and its locators beginning January 26, 2013.

7. Decision on the ₱0.167 per *kWh* Refund

Following the *Supreme Court's* final ruling that directed *MERALCO* to refund affected customers

₱0.167 per *kWh* for billings made from February 1994 to April 2003, the *ERC* approved the release of the refund in four (4) phases. The refund period, which has been extended to end in December 2015 is still ongoing.

8. Expanded Senior Citizens Act of 2010 or *ESCA*

RA No. 9994, otherwise known as the Expanded Senior Citizens Act of 2010 or *ESCA*, was signed into law last February 16, 2010 mandating the grant of benefits to senior citizens.

The *ESCA* grants senior citizens whose monthly consumption does not exceed 100 *kWh* a minimum five percent (5%) discount on the monthly electric bill, for services that are registered in their name. The law also gives a discount of at least 50% on the consumption of electricity by senior citizens centers and residential care/group homes.

On January 5, 2011, the *ERC* issued a Resolution, which took effect January 22, 2011 adopting the "Rules Implementing the Discounts to Qualified Senior Citizen End-Users and Subsidy from the Subsidizing End-Users on electricity Consumption under Sections 4 and 5 of *RA No. 9994*". *MERALCO* implemented the discount starting with its February 2011 billing.

9. *MERALCO's* Peak/Off-Peak or *POP* Program

On November 15, 2012, *MERALCO* filed an application with the *ERC* for the approval of its revised Time of Use or *TOU*, rates program, also known as the Peak Off-Peak or *POP*, Program. The *POP* is a rate program being offered by *MERALCO* to customers whose load characteristics can benefit from *TOU* rates as well as to those that can shift their loads from peak to off-peak hours. The proposed revised *POP* Rate aims to provide better savings to avalees by providing them with a *TOU* program that has a wider pricing difference between peak and off-peak rates.

In an Order dated December 17, 2012, the *ERC* provisionally approved the *POP* Program.

10. Purchase of Sub-transmission Assets or *STAs*

On November 25, 2009, *MERALCO* signed a Contract to Sell with the National Transmission Corporation or *TransCo* for the sale and purchase of certain sub transmission assets for ₱86 million. On February 25, 2010, the *ERC* provisionally

approved this Contract to Sell. On June 1, 2012, the *ERC* rendered a Decision dated March 6, 2012, approving the sale of the said *STAs* in favor of *MERALCO* for ₱85 million. On April 17, 2012, *MERALCO* and *TransCo* filed a joint application for the approval of the Batch 4 contract to sell with the *ERC*. On April 22, 2013, the *ERC* issued its Decision on *MERALCO*'s joint application for the acquisition of the Batch 4 contract to sell. *MERALCO* thereafter filed a motion for reconsideration regarding the exclusion of certain facilities for acquisition, which has yet to be resolved by the *ERC*.

On December 12, 2011, *MERALCO* signed various agreements for the acquisition of certain sub-transmission assets of *TransCo* within the *MERALCO* franchise area for its sole account, as well as with a consortium with Batangas II Electric Cooperative, Inc., or *BATELEC II* and First Bay Power Corporation or *FBPC*. On September 18, 2012, an amended consortium agreement was executed between *MERALCO* and *FBPC*. On October 17, 2012, *MERALCO* signed two separate amended consortium agreements with *BATELEC II*, and with *FBPC* and *BATELEC II*. These amended consortium agreements superseded the ones signed on December 12, 2011. On December 27 and 28, 2012, the Contract to Sell and Consortium Agreements, respectively, covering these sub-transmission assets were filed with the *ERC* for approval.

11. Feed-in-Tariff

Pursuant to Republic Act No. 9513, or the Renewable Energy Act of 2008 or *RE Act*, the *ERC* issued Resolution No. 16, Series of 2010, Adopting the Feed-in-Tariff or *FIT* Rules, on July 23, 2010. As defined under the *FIT* Rules, the *FIT* system is as a renewable energy policy that offers a guaranteed payment on a fixed rate per kilowatt-hour for electricity from wind, solar, ocean, hydropower and biomass energy sources.

On May 16, 2011, the National Renewable Energy Board or *NREB* filed its Petition to Initiate Rule Making for the Adoption of *FIT*. The Petition proposed a specific *FIT* Rate for each emerging renewable resource. On July 27, 2012, after undergoing several public consultations and public hearings, the *ERC* approved *FIT* Rates that are significantly lower than the rates applied by the *NREB*.

To fund the *FIT* payments to eligible *RE* developers, a *FIT*-Allowance charge will be imposed on all end-users. The *FIT*-Allowance will be established by the *ERC* upon petition by the *TransCo*, which had been designated as the *FIT* Fund Administrator. Similar to the *NREB*'s *FIT* Rate Petition, the *FIT*-Allowance Petition will go through the process of public hearings and consultations.

To supplement the *FIT* Rules, the *ERC* is currently drafting *FIT*-Allowance Payment and Collection Guidelines. This set of guidelines will govern how the *FIT*-Allowance will be calculated using the formulae provided. It will also outline the process of billing and collecting the *FIT*-Allowance from the electricity consumers, the remittance to a specified fund, the disbursement from the *FIT*-Allowance fund and the payment to eligible *RE* developers. The draft is currently undergoing public consultations.

12. Lifeline Subsidy

On June 21, 2011, *Republic Act No. 10150*, "An Act Extending the Implementation of the Lifeline Rate, Amending for the Purpose Section 73 of the Republic Act 9136, otherwise known as the *EPIRA* of 2001," was promulgated. The Act extended the implementation of the lifeline rate for another 10 years.

13. Net Metering Program

The Renewable Energy or *RE* Act mandates the *DUs* to provide the mechanism for the “physical connection and commercial arrangements necessary to ensure the success of the *RE* programs”, specifically the Net Metering Program. The *RE* Act defines Net Metering as “a system, appropriate for distributed generation, in which a distribution grid user has a two-way connection to the grid and is only charged for his net electricity consumption and is credited for any overall contribution to the electricity grid”. By their nature, net metering installations will be small (less than 100 kW) and will likely be adopted by the households and small business end-users of *DUs*.

On September 4, 2012, the *ERC* released the first draft of the Proposed Net Metering Rules. The proposed rules will govern the implementation of the Net Metering program for *RE* sources. It also seeks to establish the standards for interconnecting these *RE* sources to the *DUs*’ systems. The pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. Meantime, the distribution utilities’ blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. On September 21, 2012, the *ERC* conducted the first public consultation on the proposed rules.

After consultations with stakeholders, the *ERC* issued on July 3, 2013 its Resolution No. 09, Series of 2013, entitled, “A Resolution Adopting the Rules enabling the Net Metering Program for Renewable Energy”. The rules will govern the *DUs*’ implementation of the Net Metering program. Included in Rules are the Interconnection Standards that shall provide technical guidance to address engineering, electric system reliability, and safety concerns for net metering interconnections. The final pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. Meantime, the distribution utilities’ blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. The rules took effect on July 24, 2013. *MERALCO* started accepting net metering applications on the same day.

OTHER QUANTITATIVE AND QUALITATIVE DISCLOSURES

Any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in *MERALCO*’s liquidity increasing or decreasing in any material way.

Not applicable

Any events that will trigger direct or indirect contingent financial obligation that is material to *MERALCO*, including any default or acceleration of an obligation.

Mediation with NPC

The *NPC* embarked on a Power Development Program or *PDP*, which consisted of contracting generating capacities and the construction of its own, as well as private sector, generating plants, following a crippling power supply crisis. To address the concerns of the creditors of *NPC*, namely, Asian Development Bank and the World Bank, the *DOE* required that *MERALCO* enter into a long-term supply contract with *NPC*.

Accordingly, on November 21, 1994, *MERALCO* entered into a 10-year Contract for Sale of Electricity or *CSE*, with *NPC* to commence on January 1, 1995. The *CSE* and the rates and amounts charged to *MERALCO* therein were approved by the *BOD* of *NPC* and the then Energy Regulatory Board, respectively.

Separately, the *DOE* further asked *MERALCO* to provide a market for half of the output of the Camago-Malampaya gas field to enable its development and production of natural gas, which was to generate significant revenues for the Philippine Government and equally significant foreign exchange savings for the country to the extent of the fuel imports which the domestic volume of natural gas will displace.

MERALCO's actual purchases from *NPC* exceeded the contract level in the first seven (7) years of the *CSE*. However, the 1997 Asian crisis resulted in a significant curtailment of energy demand.

While the events were beyond the control of *MERALCO*, *NPC* did not honor *MERALCO*'s good faith notification of its offtake volumes. A dispute ensued and both parties agreed to enter into mediation.

The mediation resulted in the signing of a Settlement Agreement or *SA* between the parties on July 15, 2003. The *SA* was approved by the respective *BODs* of *NPC* and *MERALCO*. The net settlement amount of ₱14,320 million was agreed upon by *NPC* and *MERALCO* and manifested before the *ERC* through a Joint Compliance dated January 19, 2006. The implementation of the *SA* is subject to the approval of *ERC*.

Subsequently, the Office of the Solicitor General or *OSG* filed a "Motion for Leave to Intervene with Motion to Admit Attached Opposition to the Joint Application and Settlement Agreement between *NPC* and *MERALCO*." As a result, *MERALCO* sought judicial clarification with the *RTC-Pasig*. Pre-trials were set which *MERALCO* complied with and attended. However, the *OSG* refused to participate in the pre-trial and opted to seek a Temporary Restraining Order or *TRO* from the *CA*.

In a Resolution dated December 1, 2010, the *CA* issued a *TRO* against *RTC-Pasig*, *MERALCO* and *NPC* restraining the respondents from further proceeding with the case. Subsequently, in a Resolution dated February 3, 2011, the *CA* issued a writ of preliminary injunction enjoining the *RTC-Pasig* from conducting further proceedings pending resolution of the Petition. In a Decision dated October 14, 2011, the *CA* resolved to deny the Petition filed by the *OSG* and lifted the injunction previously issued. The said Decision likewise held that the *RTC-Pasig* committed no error in finding the *OSG* in default due to its failure to participate in the proceedings. The *RTC-Pasig* was thus ordered to proceed to hear the case *ex-parte*, as against the *OSG*, and with dispatch. The *OSG* has filed an *MR*, which was denied by the *CA* in its Resolution dated April 25, 2012. The *OSG* filed a Petition for Review of the Certiorari with the *Supreme Court*. In a Resolution dated July 25, 2012, the *Supreme Court* required *MERALCO* to file a Comment. *MERALCO*'s Comment was filed on October 29, 2012. The *SC* then issued a Resolution dated November 26, 2012 requiring the *OSG* to file a Reply. On February 19, 2013, the *OSG* filed a motion for extension to file a Consolidated Reply. *MERALCO* has yet to receive the *OSG*'s Consolidated Reply.

With the dismissal of the petition filed by the *OSG* with the *CA*, *MERALCO* filed a motion for the reception of its evidence *ex-parte* with the *RTC-Pasig* pursuant to the ruling of the *CA*. In a Decision dated May 29, 2012, the *RTC-Pasig* declared the *SA*, independent of the pass-through for the settlement amount, which is reserved for the *ERC*, valid and binding. The *OSG* has filed a Notice of Appeal with the *RTC-Pasig* on June 19, 2012.

Both parties have filed their respective appeal briefs. The case is deemed submitted for resolution by the CA.

On January 22, 2014, *MERALCO* received a Notice of Judgment from the *Supreme Court* in stating that a Decision dated December 11, 2013 was rendered by the First Division of the *Supreme Court* denying the Petition for Review on Certiorari by the OSG and affirming the decision promulgated by the CA on October 14, 2011.

Sucat-Araneta-Balintawak Transmission Line

The Sucat-Araneta-Balintawak transmission line is a two-part transmission line, which completed the 230kV-line loop within Metro Manila. The two main parts are the Araneta to Balintawak leg and, the Sucat to Araneta leg, which cuts through Dasmariñas Village, Makati City.

On March 10, 2000, certain residents along Tamarind Road, Dasmariñas Village, Makati City or plaintiffs, filed a case with the Regional Trial Court – Makati Branch or *RTC-Makati* against *NPC*, enjoining *NPC* from further preparing and installing high voltage cables to the steel pylons erected near the plaintiffs' homes and from energizing and transmitting high voltage electric current through said cables because of the alleged health risks and danger posed by the same. Following its initial status quo Order issued on March 13, 2000, *RTC-Makati* granted on April 3, 2000 the preliminary injunction sought for by the plaintiffs. The decision was affirmed by the *Supreme Court* on March 23, 2006, which effectively reversing a decision of the CA to the contrary. The *RTC-Makati* subsequently issued a writ of execution based on the order of the *Supreme Court*. *MERALCO*, in its capacity as an intervenor, was constrained to file an Omnibus Motion to maintain status quo because of the significant effect of a de-energization of the Sucat-Araneta line to the public and economy. Shutdown of the 230-kV line will result in widespread and rotating brownouts within *MERALCO*'s franchise area with certain power plants unable to run at their full capacities.

On September 8, 2009, the *RTC-Makati* granted the motions for intervention filed by intervenors *MERALCO* and *NGCP* and dissolved the Writ of Preliminary Injunction issued, upon the posting of the respective counter bonds by defendant *NPC*, intervenors *MERALCO* and *NGCP*, subject to the condition that *NPC* and intervenors pay all damages, which the plaintiffs may incur as a result of the Writ of Preliminary Injunction.

Thereafter, the plaintiffs questioned the *RTC-Makati* order before the CA. As at March 17, 2014, this case remains pending for resolution in the CA.

Moreover, in its Order dated February 5, 2013, the *RTC-Makati* granted plaintiffs' motion and directed the re-raffle of the case to another court after the judicial dispute resolution failed.

Real Property Tax Assessment

Several Local Government Units or *LGUs*, assessed *MERALCO* for deficiency *RPTs* on certain assets of *MERALCO*. The assets include electric poles, wires, insulators, and transformers, collectively referred to as *TWIP*. Of these *LGUs*, one has secured a favorable decision from the CA. Such decision was appealed by *MERALCO* to the *Supreme Court* for the benefit of *MERALCO* customers, where it is now submitted for resolution. The cases of the other *LGUs* are pending with their respective administrative bodies or government offices.

MERALCO also filed a case against the City of Manila before *RTC–Pasig* to enjoin the collection of real property taxes on the company's transformers and poles and nullify the *RPT* assessments made thereon based on the argument that these are not within the ambit of the definition of real property under the *LGC*. The case is set for mediation after the City of Manila filed its comment on *MERALCO*'s petition.

In the event that the assessments are sustained by the *SC* and payment is warranted or appropriate, *MERALCO* will file for the recovery of any resulting real estate tax payments from customers in the relevant *LGU* through separate application with the *ERC*.

Local Franchise Tax

Certain municipalities have served assessment notices on *MERALCO* for local franchise taxes. As provided in the *LGC*, only cities and provincial governments may impose taxes on establishments doing business in their localities. On the basis of the foregoing, *MERALCO* and its legal counsel believe that *MERALCO* is not subject or liable for such assessments.

Deferred Purchased Power Adjustment or PPA

On October 14, 2009, the *ERC* released its findings on *MERALCO*'s implementation of the collection of the approved pass-through cost under-recoveries in 2004. *ERC* directed *MERALCO* to refund ₱268 million of deferred *PPA* transmission line costs related to *QPPL* and deferred accounting adjustments or *DAA* incurred to customers, along with ₱184 million in carrying charges, or an equivalent of ₱0.0169 per *kWh*. *MERALCO* implemented the refund beginning November 2009 until September 2010. However, the *ERC* has yet to rule on *MERALCO*'s deferred *PPA* under-recoveries of ₱106 million, which does not represent the transmission line fee. As at March 17, 2014, *MERALCO* has filed a Motion for Reconsideration, which is pending decision by the *ERC*.

SC Decision on Unbundling Rate Case

On May 30, 2003, the *ERC* issued an Order approving *MERALCO*'s unbundled tariffs that resulted in a total increase of ₱0.17 per *kWh* over the May 2003 tariff levels. However, on August 4, 2003, certain consumer and civil society groups filed a Petition for Review with the *CA* on the *ERC*'s ruling. On July 22, 2004, the *CA* set aside the *ERC*'s ruling on *MERALCO* rate unbundling and remanded the case to the *ERC*. Further, the *CA* opined that the *ERC* should have asked the Commission on Audit or *COA*, to audit the books of *MERALCO*. The *ERC* and *MERALCO* subsequently filed separate motions asking the *CA* to reconsider its decision. On January 24, 2005, as a result of the denial by the *CA* of the motions, the *ERC* and *MERALCO* elevated the case to the *SC*.

In an En Banc decision promulgated on December 6, 2006, the *SC* set aside and reversed the *CA* ruling saying that a *COA* audit was not a prerequisite in the determination of a utility's rates. However, while the *SC* affirmed *ERC*'s authority in rate-fixing, the *SC* directed the *ERC* to request *COA* to undertake a complete audit of the books, records and accounts of *MERALCO*. On January 15, 2007, in compliance with the directive of the *SC*, *ERC* requested *COA* to conduct an audit of the books, records and accounts of *MERALCO* using calendar year 2004 and 2007 as test years.

The *COA* audit, which began in September 2008, was completed in August 2009.

On February 17, 2010, the *ERC* issued its Order directing *MERALCO* and all intervenors in the case to submit within 15 days from receipt their respective comments on the COA's "Report No. 2009-01 Rate Audit Unbundled Charges."

On July 1, 2011, the *ERC* maintained and affirmed its findings and conclusions in its Order dated March 20, 2003. The *ERC* stated that the COA recommendation to apply disallowances under *PBR* to rate unbundling violates the principle against retroactive rate-making. An intervenor group filed a motion for reconsideration of the said Order. On September 5, 2011, *MERALCO* filed its comment to the intervenor's motion for reconsideration. On February 4, 2013, the *ERC* denied the intervenor's motion for reconsideration. The intervenor filed a petition for review before the CA. *MERALCO* is awaiting further action of the CA on this matter.

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

Not Applicable.

Any material commitments for capital expenditures, the general purpose of such commitments, and the expected sources of funds for such expenditures should be described.

2014 Capital Expenditure Requirements (In millions)

Electric capital projects	₱9,778
Non-electric projects and other capitalized items	2,366
Total capital expenditures	₱12,144

As at December 31, 2013, *MERALCO* has met, and expects that it will continue to meet its capital expenditure requirements primarily from cash flow from operations.

MERALCO is required by the *ERC* to take necessary steps, including making necessary capital expenditures, to build and maintain its network so as to meet minimum performance and service requirements and in any event to make capital expenditures in each quarter at least equal to the amount of depreciation taken in the prior years. Most expenditure on transmission and substation projects, supervisory control and distribution automation, and distribution line projects are non-discretionary. The remaining capital expenditure is discretionary, which encompasses allocation projects, telecommunications projects and other non-electrical capital expenditure. If the actual peak demand is lower than the forecasted demand, a portion of the non-discretionary capital expenditure may become discretionary.

MERALCO has an approved capital expenditure budget of ₱12,144 million for the year ended December 31, 2014, of which about 80% represents planned expenditures for the electric projects of the power distribution business. It has to prioritize its projects to only those deemed urgent in the 2013 project line up. Funding of capital expenditures will be sourced substantially from internally generated cash flow and borrowings from local and foreign financial institutions.

The ₱12,144 million approved capital expenditure budget is geared to support projects on areas with large concentration of core customers, give priority to correction of normal

deficiencies in the system, stretch loading limits of *MERALCO* facilities and initiate practical and cost-effective projects to correct system deficiencies.

Any known trends, events or uncertainties that have had or that are reasonably expected to have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations should be described.

Retail Competition

See related preceding discussions under **ELECTRIC POWER INDUSTRY DEVELOPMENTS AND UPDATES.**

Petition for Dispute Resolution

On September 9, 2008, *MERALCO* filed a Petition for Dispute Resolution with the *ERC*, against the Philippine Electricity Market Corporation or *PEMC*, *TransCo*, *NPC* and Power Sector Assets and Liabilities Management Corporation or *PSALM*, as a result of the congestion in the transmission system of *TransCo* arising from the outages of the San Jose-Tayabas 500kV Line 2 on June 22, 2008, and the 500kV 600 MVA Transformer Bank No. 2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The Petition seeks to, among others, direct *PEMC* to adopt the *NPC-TOU* rate or the new price determined through the price substitution methodology of *PEMC* as approved by the *ERC*, as basis for its billing during the period of the congestion and direct *NPC* and *PSALM* to refund the transmission line loss components of the line rentals associated with *NPC/PSALM* bilateral transactions from the start of *WESM* operation on June 26, 2006.

In a Decision dated March 10, 2010, the *ERC* granted *MERALCO*'s petition and ruled that there is double charging of the Transmission Line Cost on *MERALCO* by *NPC* for the *TSC* quantities to the extent of 2.98% loss factor, since the start of the *TSC* in November 2006. Thus, *NPC* was directed to refund/collect line rental adjustment to/from *MERALCO*. In the meantime, the *ERC* issued an Order on May 4, 2011 directing *PEMC* to submit an alternative methodology for the segregation of line rental into congestion cost and line losses from the start of the *WESM*. *PEMC* has filed its compliance submitting its alternative methodology.

On September 8, 2011, *MERALCO* received a copy of *PEMC*'s compliance to *ERC*'s directive and on November 11, 2011, *MERALCO* filed a counter-proposal which effectively simplifies *PEMC*'s proposal.

On November 11, 2011, *MERALCO* filed its Motion to Implement the Decision Dated March 10, 2010 By Immediately Effecting the Refund/(Collection) of Line Rental Adjustments to Consumers. On December 21, 2011, *PSALM* filed its Comment on *MERALCO*'s said Motion. Then, in an Order of the *ERC* dated January 24, 2012, it directed *PEMC*, *TransCo* and *NPC* to submit their respective comments on *MERALCO*'s motion within five days from receipt.

In an Order of the *ERC* dated June 21, 2012, *MERALCO* was directed to submit its computation of the amount of the double charging of line loss on a per month basis from June 26, 2006 up to the present. On July 4, 2012, *MERALCO* filed its Compliance to the said Order. Thereafter, the *ERC* issued an Order directing the parties to comment on *MERALCO*'s submissions.

In an Order dated March 4, 2013, the *ERC* approved the methodology proposed by *MERALCO* and *PEMC* in computing the double charged amount on line losses by deducting 2.98% from the *NPC-TOU* amount. Accordingly, the *ERC* determined that the computed double charge amount to be collected from *NPC* is ₱5.2 billion, covering the period November 2006 to August 2012 until actual cessation of the collection of the 2.98% line loss charge in the *NPC-TOU* rates imposed on *MERALCO*, while the amount to be collected from the *SGCs* is ₱4.7 billion. Additionally, *MERALCO* was directed to file a petition against the following *SGCs*: *MPPCL*, Aboitiz Power Renewables, Inc. or *APRI*, *TLI*, *SMEC* and *Sem-Calaca*, within thirty (30) days from receipt thereof, to recover the line loss collected by them. *MERALCO* filed a motion for clarification with the *ERC* regarding the directives contained in the March 4, 2013 Order.

In an order dated July 1, 2013, the *ERC* issued the following clarifications/resolutions: (1) *SPPC* should be included as one of the *SGCs* against whom a petition for dispute resolution should be filed by *MERALCO*; (2) amount to be refunded by *NPC* is not only ₱5.2 billion but also the subsequent payments it received from *MERALCO* beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates; and Petition to be filed by *MERALCO* against the *SGCs* should not only be for the recovery of the amount of ₱4.7 billion but also the subsequent payments beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates; (3) “*SCPC Ilijan*” pertains to *SPPC* instead. Thus, the refundable amount of ₱706 million pertaining to “*SCPC Ilijan*” should be added to *SPPC*’s refundable amount of ₱1.1 billion; (4) Grant the “Motion for Extension” filed by *MERALCO* and was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC*, *SCPC* and *SPPC*, otherwise, it shall be the one liable to refund the subject amount to its customers; and (5) deny the respective “Motions for Reconsideration filed by *NPC* and *PSALM*.”

On September 12, 2013, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking approval of its proposal to offset the amount of ₱74 million against some of its monthly remittances to *PSALM*. *PSALM* and *NPC* filed their comments *ad cautelam* on *MERALCO*’s Manifestation and Motion. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion. On November 4, 2013, *MERALCO* filed its Reply. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion.

On October 24, 2013, *MERALCO* received *PSALM*’s Petition for Certiorari with the *CA* (With Urgent *TRO* and/or Writ of Preliminary Mandatory Injunction Applications) to question the March 4, 2013 and July 1, 2013 Orders of the *ERC*. In a Resolution dated December 29, 2013, the *CA* gave *MERALCO* until December 26, 2013, within which to submit its Comment on the Petition for Certiorari and to show cause why the prayer for the Application for *TRO* and/or Preliminary Injunction should not be granted (“*Comment and Opposition*”). On December 23, 2013, January 5, 2014 and January 15, 2014, *MERALCO* requested for an additional period of ten (10) days each, within which to submit its *Comment and Opposition*.

On February 2, 2014, *MERALCO* filed its Comment to said Petition. The *CA* has yet to rule on the Petition.

PSALM versus *PEMC* and *MERALCO*

Due to the unusually large increases in *WESM* prices during the 3rd and 4th months of the *WESM* operations, *MERALCO* raised concerns with the *PEMC* to investigate whether *WESM* rules were breached or if anti-competitive behavior had occurred.

While resolutions were initially issued by the *PEMC* directing adjustments of *WESM* settlement amounts, a series of exchanges and appeals with the *ERC* ensued. *ERC*'s decision directing the *WESM* settlement price for the 3rd and 4th billing months to be *NPC-TOU* rates, prompted *PSALM* to file a Motion for Reconsideration with the *CA*, which was denied on November 6, 2009. In December 2009, *PSALM* filed a Petition for Review on Certiorari with the *Supreme Court*.

As at March 17, 2014, *PSALM*'s petition for review is pending resolution by the *Supreme Court*.

Petition for Dispute Resolution with NPC on Premium Charges

On June 2, 2009, *MERALCO* filed a Petition for Dispute Resolution against *NPC* and *PSALM* with respect to *NPC*'s imposition of premium charges for the alleged excess energy it supplied to *MERALCO* covering the billing periods May 2005 to June 2006. The premium charges amounted to ₱315 million during the May-June 2005 billing periods, which have been paid for by *MERALCO*, and ₱318 million during the November 2005, February 2006 and April-June 2006 billing periods, which is being disputed and withheld by *MERALCO*. *MERALCO* believes that there is no basis for the imposition of the premium charges. The hearings on this case have been completed and *MERALCO* is now awaiting the resolution of the *ERC* on the petition.

Recovery of Local Franchise Tax

On March 25, 2011, *MERALCO* filed with the *ERC* an Application for recovery of *LFT* paid but are not yet billed to customers for the period beginning first quarter of 1993 up to the second quarter of 2004 for five (5) provinces, namely: Bulacan, Batangas, Cavite, Laguna and Rizal; and 14 cities, namely: San Jose Del Monte, Batangas, San Pablo, Tagaytay, Lucena, Mandaluyong, Marikina, Quezon, Caloocan, Pasay, Las Piñas, Manila, Pasig and Calamba. The *LFT* is recognized as a valid and reasonable *DU* expense in the *ERC*'s unbundling decision.

In a Decision dated February 27, 2012, the *ERC* released its Order approving with modifications *MERALCO*'s application. The *ERC* approved recovery of *LFT* amounting to ₱1,571 million plus carrying charges of ₱730 million. As directed by the *ERC*, the recovery was reflected as a separate item in the *MERALCO* billing statement to its customers beginning April 2012. As at December 31, 2013, a total of ₱856 million *LFT* and carrying charges have been billed to affected customers.

Supreme Court Temporary Restraining Order on MERALCO's December 2013 Billing Rate Increase

On December 9, 2013, the *ERC* gave clearance to the request of *MERALCO* to implement a staggered collection over three (3) months covering the December 2013 billing month for the increase in generation charge and other bill components such as *VAT*, *LFT*, transmission charge, and *SL* charge, which reflected a total increase of ₱4.15 per *kWh* for a 200-*kWh* residential consumer. The generation costs for the November 2013 supply month increased significantly because of the use of the more expensive liquid fuel by the natural gas-fired power plants that were affected by the Malampaya Gas Field or *Malampaya*, shutdown from November 11 to December 10, 2013. This was compounded by the aberrant spike in the *WESM*, charges on account of the scheduled and extended shutdowns, and the forced outages of several base load power plants, as

well as the non-compliance with *WESM* Rules by certain plants resulting in significant power generation capacities not being offered and dispatched.

The Department of Justice commenced an investigation while the House of Representatives and the Senate conducted separate hearings to determine the underlying reasons for the price increase, including any possible collusion among the power firms. In the meantime, *MERALCO* proceeded with billing its captive customers with the *ERC* approval.

On December 19, 2013, several interest groups filed a Petition against *MERALCO*, *ERC* and the *DOE* before the *Supreme Court*, questioning the *ERC* clearance granted to *MERALCO* to charge the ₱4.15 per *kWh* price increase, alleging the lack of hearing and due process. It also sought for the declaration of the unconstitutionality of the *EPIRA*, which essentially declared the generation and supply sectors competitive and open, and not considered public utilities. A similar petition was filed by a consumer group and several private homeowners associations challenging also the legality of the *AGRA* that the *ERC* had promulgated. Both petitions prayed for the issuance of a *TRO* and a Writ of Preliminary Injunction.

On December 23, 2013, the *Supreme Court* consolidated the two (2) Petitions and granted the application for *TRO* effective immediately and for a period of sixty (60) days, which effectively enjoined the *ERC* and *MERALCO* from implementing the ₱4.15 per *kWh* price increase. The *Supreme Court* also ordered *MERALCO*, *ERC* and *DOE* to file their respective comments to the Petitions and set the hearing for Oral Arguments on January 21, 2014. The *Supreme Court* further set two more Oral Arguments on February 4, 2014 and February 11, 2014. After the conclusion of the Oral Arguments, the *Supreme Court* gave all the Parties to the consolidated Petitions to file their respective Memorandum on or before February 26, 2014 after which the Petitions will be deemed submitted for resolution of the *Supreme Court*. *MERALCO* complied with said directive and filed its Memorandum on said date.

On February 18, 2014, acting on the motion filed by the Petitioners, the *Supreme Court* extended for another period of 60 days or until April 22, 2014, the *TRO* that it originally issued against *MERALCO* and *ERC* last December 23, 2013. The *TRO* was also similarly applied to the generating companies, specifically Masinloc Power Partners Co. Ltd or *MPPCL*, San Miguel Energy Corporation or *SMEC*, South Premier Power Corporation or *SPPC*, First Gas Power Corporation or *FGPC*, and the National Grid Corporation of the Philippines or *NGCP*, and the Philippine Electricity Market Corporation or *PEMC* (the administrator of *WESM* and market operator) who were all enjoined from collecting from *MERALCO* the deferred amounts representing the ₱4.15 per *kWh* price increase for the November 2013 supply month.

In the meantime, on January 30, 2014, *MERALCO* filed an Omnibus Motion with Manifestation with the *ERC* for the latter to direct *PEMC* to conduct a re-run or recalculation of the *WESM* prices for the supply months of November to December 2013. Subsequently, on February 17, 2014, *MERALCO* filed with the *ERC* an Application for the recovery of deferred generation costs for the December 2013 supply month praying that it be allowed to recover the same over a six (6)-month period.

On March 3, 2014, the *ERC* issued an Order voiding the Luzon *WESM* prices given that the prices in *WESM* during the November and December 2013 supply months could not qualify as reasonable, rational and competitive. *PEMC* was given seven days upon receipt of the Order to calculate these regulated prices and implement the same in the revised *WESM* bills of the concerned

As at March 17, 2014, *MERALCO* is still awaiting decisions of the *Supreme Court* on the *TRO*.

- **Any significant elements of income or loss that did not arise from the registrant's continuing operations.**

None

Any seasonal aspects that had a material effect on the financial condition or results of operations.

Seasonality of Operations and Growth Drivers

Approximately 99% of *MERALCO Group's* operating revenues pertain to sale of electricity distributed by *MERALCO* and *CEDC*.

The electricity sales of *MERALCO* and *CEDC* exhibit a degree of quarterly seasonality. The *kWh* sales in the first quarter is lower than the average of the year as this period is characterized by cooler temperature and softer consumer demand following heightened consumer spending in the last quarter of the year. The second quarter is marked by higher than average *kWh* sales. This is due to a number of factors, including: increased consumption of households and commercial establishments due the summer season; increased production of industries to replenish stocks and in preparation for the opening of classes; and, heightened construction activity to take advantage of the sunny weather. Manufacturing industries that cater to the export market have their peak production schedule at this time as they rush to meet shipping deadlines to foreign markets. Industries catering to the domestic market are also now starting production in preparation for the Christmas season. Lastly, the fourth quarter performance is about the average of the year. Industrial production winds down while households and commercial establishments also cut down on their cooling loads. Given this perspective on the seasonality of *kWh* sales, a higher proportion of the *MERALCO's* and *CEDC's* revenues are earned on the second half of the year.

Aside from the quarterly seasonal pattern, *kWh* sales on a year-on-year basis adjust as a result of a number of factors. Sales of electricity normally increase in periods of economic growth, low inflation and electricity rates, and in periods of high temperatures over extended period of time, e.g. the El Niño episodes.

The following table sets forth *MERALCO Group's* quarterly sales in *GWh*.

Period	2013	2012
First Quarter	7,777	7,687
Second Quarter	9,086	8,528
Third Quarter	8,753	8,233
Fourth Quarter	8,468	8,323
Total	34,084	32,771

The businesses of all other subsidiaries are not highly seasonal.

Any known trends, demands, commitments, events or uncertainties that will have a material impact of the issuer's liquidity.

The Management is not aware of any known trends, demands, commitments, events or uncertainties that may potentially have a material impact on *MERALCO* Group's liquidity as at December 31, 2013.

Discussion of *MERALCO*'s and its majority-owned subsidiaries top five (5) key performance indicators. It shall include a discussion of the manner by which *MERALCO* calculates or identifies the indicators presented on a comparable basis.

Listed in the succeeding page are *MERALCO*'s five (5) major subsidiaries namely *CEDC*, *MIESCOR*, *e-MVI*, *RSIC* and *CIS*. The following table summarizes their key financial performance and indicators as at December 31, 2013 and 2012 and for the years then ended.

**Financial Highlights and Ratios¹² of Top 5 Subsidiaries
As at and for the years ended December 31, 2013 and 2012**

	CEDC			MIESCOR			e-MVI			RSIC			CIS		
	December 31			December 31			December 31			December 31			December 31		
	2013	2012	% Change	2013	2012	% Change	2013	2012	% Change	2013	2012	% Change	2013	2012	% Change
<i>(Amounts in million pesos, except for financial ratios)</i>	65%	65%		99%	99%		100%	100%		100%	100%		100%	100%	
Percentage of ownership															
Condensed Statements															
Financial Position															
Total assets	1,414	1,106	28	2,259	1,728	31	993	897	11	1,281	1,180	9	1,274	912	40
Current assets	876	594	47	1,886	1,465	29	362	328	10	877	816	7	1,202	851	41
Cash and cash equivalents	594	376	58	338	357	(5)	131	204	(36)	208	248	(16)	544	476	14
Equity	469	644	(27)	914	896	2	820	793	3	316	315	-	443	270	64
Total debt ¹³	-	-	-	114	87	31	-	-	-	-	-	-	-	-	-
Current liabilities	666	287	132	1,305	774	69	156	92	70	283	290	(2)	825	636	30
Financial Ratios															
Debt-to-equity ratio	-	-	-	0.12	0.10	20	-	-	-	-	-	-	-	-	-
Current ratio	1.32	2.07	36	1.45	1.89	(23)	2.32	3.57	(35)	3.10	2.81	10	1.46	1.34	9
	Year Ended	December 31	% Change	Year Ended	December 31	% Change	Year Ended	December 31	% Change	Year Ended	December 31	% Change	Year Ended	December 31	% Change
	2013	2012		2013	2012		2013	2012		2013	2012		2013	2012	
Condensed Statements of Income															
Revenues	2,598	2,014	29	2,863	1,915	50	450	400	13	161	185	(13)	883	674	31
Costs and expenses	2,420	1,894	28	2,825	1,908	48	270	237	14	170	150	13	647	497	30
Net income	177	130	36	14	20	(30)	127	109	17	2	34	(94)	173	133	30
Financial Ratios															
Profit margin	6.8%	6.5%	5	0.5%	1.0%	(50)	28.2%	27.3%	3	1.2%	18.4%	(93)	19.6%	19.7%	(1)
Return on equity	37.7%	20.2%	87	1.5%	2.2%	(31)	15.5%	13.7%	13	0.6%	10.8%	(94)	39.1%	49.3%	(21)
Asset turnover	1.84	1.82	1	1.27	1.11	14	0.45	0.45	-	0.13	0.16	19	0.69	0.74	(7)

¹¹ The manner of computing the financial ratios for subsidiaries is the same with computing for the financial ratios of MERALCO as presented in *Financial Highlights and Key Performance Indicators*.

¹³ Total Debt is composed of notes payable and interest-bearing long-term financial liabilities, current and non-current portions.

Aging of Trade and Other Receivables

As at December 31, 2013

(Amounts in millions)

	<u>T o t a l</u>	<u>1 - 30 days</u>	<u>31 - 60 days</u>	<u>61 - 90 days</u>	<u>Over 90 days</u>
Trade receivables – electricity					
A) Billed trade receivables					
Residential	₱9,446	₱6,251	₱875	₱205	₱2,115
Commercial	12,179	8,489	993	231	2,466
Industrial	5,128	3,943	122	38	1,025
Flat Streetlights	528	12	78	30	408
Total billed trade receivables	27,281	18,695	2,068	504	6,014
B) Unbilled trade receivables	4,175	4,175	–	–	–
Total trade receivables- electricity	31,456	22,870	2,068	504	6,014
Other trade receivables	2,398	2,398	–	–	–
Gross trade receivables	33,854	25,268	2,068	504	6,014
Non-trade receivables	2,016	2,016	–	–	–
Total receivables	35,870	27,284	2,068	504	6,014
Allowance for doubtful accounts	(3,152)	–	–	–	(3,152)
Net receivables	₱32,718	₱27,284	₱2,068	₱504	₱2,862

Item 7. Financial Statements

Refer to Index to Financial Statements

Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

There are no changes in and disagreements with accountants on accounting and financial disclosure.

The auditing firm, SyCip Gorres Velayo & Co. or *SGV*, is *MERALCO*'s independent auditors since 1986. The signing partner of the consolidated financial statements of *MERALCO* beginning calendar year 2013 is Mr. Martin C. Guantes. Mr. Guantes issued a statement confirming the independence of *SGV* with respect to *MERALCO and Subsidiaries* in accordance with the Code of Ethics for Professional Accountants in the Philippines adopted by the Philippine Board of Accountancy.

The terms of engagement, scope of services and fees of the external auditor were reviewed and approved by the Audit and Risk Management Committee. The Audit and Risk Management Committee is composed of six (6) members and chaired by independent director, retired Chief Justice Artemio V. Panganiban. The other members of the committee are Pedro E. Roxas (independent director), directors Jose Ma. K. Lim, Eric O. Recto and Vicente L. Panlilio and non-director, Anabelle L. Chua. Directors Eric O. Recto and Vicente L. Panlilio tendered their resignation as directors and members of the Audit and Risk Management Committee effective December 16, 2013. Mr. James L. Go and Mr. Lance Y. Gokongwei were nominated to the Board and appointed as members of Audit and Risk Management Committee effective December 16, 2013.

The representatives of *SGV* will be present during the annual meeting and will be given an opportunity to make a statement, if they desire to do so. They are also expected to respond to questions, if needed.

PART III – CONTROL AND COMPENSATION INFORMATION

Item 9. Directors and Executive Officers

As of March 14, 2014, the names of the incumbent Directors and Executive Officers of *MERALCO* and their respective ages, citizenship, current positions, periods of service and business experiences during the past five years are as follows:

MANUEL V. PANGILINAN, 66, Filipino
Director (since May 26, 2009)
President and CEO (July 1, 2010 to May 29, 2012)
Chairman (since May 29, 2012)

Mr. Pangilinan is the Chairman of Philippine Long Distance Telephone Company, Smart Communications, Inc., PLDT Communications and Energy Ventures (formerly Piltel), Beacon Electric Asset Holdings, Inc., Metro Pacific Investments Corporation*, Landco Pacific Corporation, Medical Doctors, Inc., Colinas Verdes Corporation (operating the Makati Medical Center and Cardinal Santos Medical Center),

Davao Doctors, Inc., Riverside Medical Center, Inc. in Bacolod City, Our Lady of Lourdes Hospital, Asian Hospital, Inc. Maynilad Water Services Corporation, Mediaquest, Inc., Associated Broadcasting Corporation (TV5), Philex Mining Corporation* and Manila North Tollways Corporation. He is the Chief Executive Officer and Managing Director of First Pacific Company Limited, a publicly-listed company in Hong Kong and Co-Chairman of the newly-organized US-Philippines Business Society. Mr. Pangilinan was a member of the Board of Overseers of The Wharton School, University of Pennsylvania. He is the Chairman of the Board of Trustees of San Beda College, Hong Kong Bayanihan Trust and was Chairman of the Board of Trustees of the Ateneo de Manila University. Mr. Pangilinan holds a Bachelor of Arts degree, *cum laude*, in Economics from the Ateneo de Manila University and a Masters in Business Administration from Wharton School of Finance and Commerce, University of Pennsylvania, where he was a Procter & Gamble Fellow.

RAMON S. ANG, 59, Filipino
Director and Vice Chairman (since February 1, 2009)

Mr. Ang is the Vice Chairman, President and Chief Operating Officer of San Miguel Corporation. He is the Chairman and Chief Executive Officer of Petron Corporation, Petron Marketing Corporation and SMC Global Power Holdings Corporation. Mr. Ang also holds the following positions: President and Chief Operating Officer of PAL Holdings, Inc. and Philippine Airlines, Inc.; Vice Chairman of Ginebra San Miguel, Inc., San Miguel Pure Foods Company, Inc. and San Miguel Yamamura Haiphong Glass Co. Limited (Vietnam); Director of Air Philippines Corporation; Chairman of San Miguel Brewery Inc., San Miguel Foods, Inc., The Purefoods-Hormel Company, Inc., San Miguel Yamamura Packaging Corporation, South Luzon Tollway Corporation, Eastern Telecommunications Philippines, Inc., Liberty Telecoms Holdings, Inc., Sea Refinery Corporation and Philippine Diamond Hotel and Resort Inc.; Chairman and President of San Miguel Properties, Inc., San Miguel Consolidated Power Corporation, San Miguel Electric Corporation, San Miguel Energy Corporation, SMC Consolidated Power Corporation, SMC Power Generation Corporation and SMC PowerGen, Inc. Mr. Ang is a Director of other subsidiaries and affiliates of the San Miguel Group of Companies in the Philippines and Southeast Asia. He holds a Bachelor of Science degree in Mechanical Engineering from Far Eastern University.

OSCAR S. REYES, 66, Filipino
Director (since July 26, 2010)
Chief Operating Officer (July 26, 2010 to May 29, 2012)
President and CEO (since May 29, 2012)

Mr. Reyes is a member of the Advisory Board of Philippine Long Distance Telephone Company and of the Board of Directors of the Bank of the Philippine Islands, Manila Water Company, Inc., Ayala Land, Inc., PLDT Communications and Energy Ventures, Inc., Pepsi Cola Products Philippines, Inc., Sun Life Financial Phils., Inc. and Basic Energy Corporation, Cosco Capital, Inc., among other firms. He is also President of MERALCO PowerGen Corporation and Chairman of Meralco Industrial Engineering Services Corporation (MIESCOR), CIS Bayad Center, Inc., Meralco Energy, Inc., Redondo Peninsula Energy, Inc. and PacificLight Pte. Ltd. He served as Country Chairman of the Shell Companies in the Philippines and concurrently President of Pilipinas Shell Petroleum Corporation and Managing Director of Shell Philippines

Exploration B.V. He is a member of the Board of Trustees of One Meralco Foundation, Inc., Pilipinas Shell Foundation, Inc., SGV Foundation, Inc. and El Nido Foundation, Inc. He holds a Bachelor of Science degree, *cum laude*, in Economics from the Ateneo de Manila University and finished post-graduate studies at the Ateneo Graduate School of Business Administration, Waterloo Lutheran University and the Harvard Business School.

RAY C. ESPINOSA, 57, Filipino
Director (since May 26, 2009)

Atty. Espinosa is a Managing Director of First Pacific Company Limited, the Vice Chairman of the Board of PhilWeb Corporation. He is a Director of Philippine Long Distance Telephone Company, Metro Pacific Investments Corporation, Philstar Daily, Inc. and Wolfpac Mobile, Inc.; Independent Director of Lepanto Consolidated Mining Company; and the Associate Director of First Pacific Company Limited. He was the President and Chief Executive Officer of Mediaquest Holdings, Inc. and ePLDT, Inc. Atty. Espinosa holds a Bachelor of Laws degree, *salutatorian*, from the Ateneo de Manila University and a Master of Laws degree from the University of Michigan Law School as a Clyde Alton Dewitt Fellow. He placed first in the Philippine Bar examinations in 1982.

JAMES L. GO, 74, Filipino
Director (since December 16, 2013)

Mr. Go is the Chairman and Chief Executive Officer of JG Summit Holdings, Inc. and Oriental Petroleum and Minerals Corporation. He is also Chairman of Universal Robina Corporation, Robinsons Land Corporation, JG Summit Petrochemical Corporation and JG Summit Olefins Corporation. He also serves as Vice Chairman and Chief Executive Officer of Robinsons Retail Holdings, Inc.; and Director of Cebu Air, Inc., Singapore Land, Ltd., Marina Center Holdings, Inc., UIC, Hotel Marina City Private Limited and Philippine Long Distance Telephone Company. Mr. Go holds a Bachelor of Science degree and a Master of Science degree in Chemical Engineering from the Massachusetts Institute of Technology.

JOHN L. GOKONGWEI, JR.¹⁴, 87, Filipino
Director (since March 31, 2014)

Mr. Gokongwei is the Founder and Chairman Emeritus of JG Summit Holdings, Inc. He is the Chairman and Chief Executive Officer of Robinsons Retail Holdings, Inc.; Director and Chairman Emeritus of Universal Robina Corporation, Robinsons Land Corporation and JG Summit Petrochemical Corporation; and Chairman Emeritus of Robinsons Bank. He also serves as Deputy Chairman and Director of United Industrial Corporation Limited and Singapore Land Limited; and Director of Cebu Air, Inc., and A. Soriano Corporation. Mr. Gokongwei holds a Masters in Business Administration degree from the De La Salle University and attended the Advance Management Program, Harvard University, Massachusetts.

¹⁴ Elected as Director as of March 31, 2014

LANCE Y. GOKONGWEI, 47, Filipino
Director (since December 16, 2013)

Mr. Gokongwei is the President and Chief Operating Officer of JG Summit Holdings, Inc. He is also the President and Chief Executive Officer of Universal Robina Corporation, Cebu Air, Inc., JG Summit Petrochemical Corporation and JG Summit Olefins Corporation. Mr. Gokongwei also serves as the Vice Chairman and Chief Executive Officer of Robinsons Land Corporation; Chairman of Robinsons Bank; Vice Chairman of Robinsons Retails Holdings, Inc.; and Director of Oriental Petroleum and Minerals Corporation, United Industrial Corporation Limited and Singapore Land Limited. Mr. Gokongwei holds a Bachelor of Science degree in Finance and a Bachelor of Science degree in Applied Science from the University of Pennsylvania.

JOSE MA. K. LIM, 60, Filipino
Director (since May 29, 2012)

Mr. Lim is the President and Chief Executive Officer of Metro Pacific Investments Corporation. He is also a Director of Beacon Electric Asset Holdings, Inc., Metro Pacific Tollways Corporation, Manila North Tollways Corporation, Tollways Management Corporation, Maynilad Water Services, Inc., Indra Philippines, Inc., Medical Doctors, Inc., Cardinal Santos Medical Center and Our Lady of Lourdes Hospital. He serves as Chairman of Asian Hospital, Davao Doctors Hospital and Riverside Medical Center in Bacolod City. He is the President of Metro Strategic Infrastructure Holdings, Inc. which holds a minority ownership in Citra Metro Manila Tollways Corporation (Skyway) and a Founding Member and Treasurer of the Shareholders Association of the Philippines. Mr. Lim holds a Bachelor of Arts degree in Philosophy from the Ateneo de Manila University and a Masters in Business Administration from the Asian Institute of Management.

MANUEL M. LOPEZ, 70, Filipino
Director (since April 14, 1986)
Chairman and CEO (July 1, 2001 to June 30, 2010)
Chairman (July 1, 2010 to May 29, 2012)

Mr. Lopez is the Philippine Ambassador to Japan. He is the Chairman and Chief Executive Officer of Lopez Holdings Corporation and is the Chairman of Indra Philippines, Inc., Rockwell Land Corporation and Rockwell Leisure Club. He is the Vice Chairman of First Philippine Holdings Corporation and Lopez Inc. Mr. Lopez also serves as Director of ABS-CBN Corporation, ABS-CBN Holdings Corporation, Sky Cable Corporation and Lopez Group Foundation, Inc.; and, President of Eugenio Lopez Foundation, Inc. Mr. Lopez holds a Bachelor of Science degree in Business Administration and attended the Harvard Program for Management Development..

ESTELITO P. MENDOZA, 83, Filipino
Director (since February 1, 2009)

Atty. Mendoza heads the law firm Estelito P. Mendoza and Associates. He is a Director of San Miguel Corporation, Petron Corporation, Philippine National Bank and Philippine Airlines, Inc. A practicing lawyer for more than 60 years, he was consistently listed as a "Leading Individual in Dispute Resolution" among lawyers in the Philippines

in the following directories/journals: “The Asia Pacific Legal 500”, “Chambers of Asia” and “Which Lawyer?” yearbooks for several years . He has also been a Professorial Lecturer of law at the University of the Philippines and served as Solicitor General, Minister of Justice, Member of the National Assembly and Provincial Governor of Pampanga. He was also the Chairman of the Sixth (Legal) Committee, 31st Session of the UN General Assembly and the Special Committee on the Charter of the United Nations and the Strengthening of the Role of the Organization. He holds a Bachelor of Laws degree from the University of the Philippines and Master of Laws degree from Harvard Law School..

NAPOLEON L. NAZARENO¹⁵, 64, Filipino
Director (since March 31, 2014)

Mr. Nazareno is the President and Chief Executive Officer of Philippine Long Distance Telephone Company and Smart Communications, Inc. He also serves as Chairman of the Board of SMART e-Money, Inc., PLDT Communications and Energy Ventures, Smart Broadband, Inc., Wolfpac Mobile, Inc., i-Contacts Corporation, Airborne Access, Inc., Aces Philippines Cellular Satellite Corporation, Digital Telecommunications, Inc. (Digitel) and Digitel Mobile Phils., Inc. He is a Director of PLDT Global Corporation, ePLDT, Inc., GSM Association Worldwide and Wireless Applications Community. He is also the Chairman of the Board of Trustees and Governors of the Asian Institute of Management; Trustee of Ideaspace and Philippine Disaster Recovery Foundation, Inc. He holds a Bachelor of Science degree in Mechanical Engineering from the University of San Carlos in Cebu City and a Masters in Business Management degree from the Asian Institute of Management. He attended the INSEAD Executive Program at The European Institute of Business Administration in France.

ARTEMIO V. PANGANIBAN, 77, Filipino
Independent Director (since May 27, 2008)

Justice Panganiban was a former Chief Justice of the Supreme Court of the Philippines. He was also Chairperson of the Presidential Electoral Tribunal, Judicial and Bar Council and Philippine Judicial Academy. He serves as Independent Director of Petron Corporation, Bank of the Philippine Islands, First Philippine Holdings Corporation, Philippine Long Distance Telephone Company, Metro Pacific Investment Corporation, Robinsons Land Corporation, GMA Network, Inc., GMA Holdings, Metro Pacific Tollways Corporation, Tollways Management Corporation and Asian Terminals, Inc.; Non-Executive Director of Jollibee Foods Corporation; Senior Adviser of Metropolitan Bank and Trust Company; Chairman of the Board of Advisers of Metrobank Foundation; Chairman of Pan Philippine Resources Corporation and Peecee Realty, Inc.; Chairman of the Board of Trustees of Foundation for Liberty and Prosperity and Philippine Dispute Resolution Center, Inc.; and a columnist for the Philippine Daily Inquirer. He holds a Bachelor of Laws degree, *cum laude*, from the Far Eastern University and was awarded the degree of Doctor of Laws (*Honoris Causa*) by the University of Iloilo, Far Eastern University, University of Cebu, Angeles University and Bulacan State University. He placed sixth in the Philippine Bar Examinations in 1960.

¹⁵ Elected as Director as of March 31, 2014

PEDRO E. ROXAS, 57, Filipino
Independent Director (since May 25, 2010)

Mr. Roxas is the Executive Chairman, and President and Chief Executive Officer of Roxas and Company, Inc. He is also the Chairman of Roxas Holdings, Inc., Club Punta Fuego, Inc. and Philippine Sugar Millers Association. He is a member of the Board of Directors of Philippine Long Distance Telephone Company, BDO Private Bank and Brightnote Assets Corporation; Director and President of Fundacion Santiago; and Trustee of Philippine Business for Social Progress. Mr. Roxas holds a Bachelor of Science degree in Business Administration from the University of Notre Dame in Indiana, USA.

SIMEON KEN R. FERRER, 56, Filipino
Corporate Secretary (since May 26, 2009)

Atty. Ferrer is a Senior Partner at the SyCip Salazar Hernandez and Gatmaitan and is Chairman of the law firm's Hiring Committee. He is a Director and Corporate Secretary of Habibi Cove Realty Corporation, Marbelene Realty Corporation, Maxim Philippine Assembly Corporation, among others. Atty. Ferrer is a member of the Integrated Bar of the Philippines and the Philippine Bar Association and a Fellow of the Institute of Corporate Directors. He is also the International Alumni Contact for the Philippines of the University of Michigan Alumni Association. He holds a Bachelor of Science degree in Business Economics and Bachelor of Laws degree from the University of the Philippines and a Master of Laws degree from the University of Michigan as a DeWitt Fellow.

RICARDO V. BUENCAMINO, 69, Filipino
Senior Executive Vice President (since January 1, 2013) and Head, Networks

Mr. Buencamino is a Director of Clark Electric Distribution Corporation, Meralco Energy, Inc., Calamba Aero Power Corporation, Atimonan Land Ventures Development Corporation, Meralco Industrial Engineering Services Corporation and Asian Hospital, Inc. He is the Vice Chairman of General Electric Philippines Meter and Instrument Co. Inc. and was formerly a Director of First Private Power Corporation and Landbees Corporation.

ROBERTO R. ALMAZORA, 53, Filipino
Senior Vice President (since March 2009), Energy Market Advisor and Head, MPower

Mr. Almazora served as Director of Indra Philippines, Inc. He has been a Director of Meralco Energy, Inc., Meralco Industrial Engineering Services Corporation, General Electric Philippines Meter and Instrument Co., Inc., MIESCOR Builders, Inc., Landbees Corporation, Clark Electric Distribution Corporation and First Private Power Corporation.

ALFREDO S. PANLILIO, 51, Filipino
Senior Vice President (since September 2010) and Head, Customer Retail Services and Corporate Communication

Mr. Panlilio is a Director of CIS Bayad Center, Corporate Information Solutions, Inc., Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation), Meralco Energy, Inc., Miescorrail, Inc., Radius Telecoms, Inc., General Electric Philippines Meter and Instrument Co., Inc., Indra Philippines, Inc. and SEIPI. He also serves as Chairman and Director of Paragon Vertical Corporation; Chairman of e-Meralco Ventures, Inc. and Loyola Meralco Sparks FC; Trustee of One Meralco Foundation, Inc.; and President of MVP Sports Foundation, Inc. He was formerly a Director of PLDT Global Corporation and Vice Chairman and Trustee of MMLDC Foundation, Inc.

ANGELITO D. BERMUDO, 54, Filipino
Senior Vice President (since January 2013)

Mr. Bermudo is the President and Chief Executive Officer of Meralco Industrial Engineering Services Corporation and the MIESCOR Group, Miescor Builders, Inc., and Miescor Logistics, Inc. He was the former President and Chief Executive Officer of AG&P Company of Manila.

RAMON B. SEGISMUNDO, 56, Filipino
Senior Vice President (since February 2010) and Head, Human Resources and Corporate Services

Mr. Segismundo is the Chairman of Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation). He is also a Director of Meralco Industrial Engineering Services Corporation, CIS Bayad Center, Inc. and General Electric Philippines Meter and Instrument Co., Inc.; Trustee of One Meralco Foundation, Inc., Meralco Pension Fund, Loyola Meralco Sparks FC and Samahang Basketbol ng Pilipinas. He is also the President and Trustee of Meralco Power Academy; and the Chairman and Governor of the Philippine Basketball Association.

BETTY C. SIY-YAP, 52, Filipino
Senior Vice President and Chief Finance Officer (since July 2009)

Ms. Siy-Yap is a Director of Clark Electric Distribution Corporation, CIS Bayad Center, Inc., Meralco Industrial Engineering Services Corporation, General Electric Philippines Meter and Instrument Co., Inc., Radius Telecoms, Inc., Indra Philippines, Inc., Philippine Commercial Capital, Inc., Meralco PowerGen Corporation, Miescorrail, Inc., Meralco Financial Services Corporation, Calamba Aero Power Corporation and Redondo Peninsula Energy, Inc. She is the President of Lighthouse Overseas Insurance Limited. She is also a Member of the Auditing and Assurance Council of the Philippines; Trustee of Meralco Pension Fund, One Meralco Foundation, Inc., and the Loyola Agila Futbol Club, Inc.; Treasurer of First Pacific Leadership Academy, Inc. and MVP Sports Foundation, Inc. She serves as Alternate Governor of the Philippine Basketball Association for the Meralco Bolts. She was formerly a Director of Rockwell Land Corporation and was a Partner of SyCip Gorres Velayo and Co. from 1995 to 2009.

RAFAEL L. ANDRADA, 54, Filipino
First Vice President (since January 2005) and Group Treasurer, One Meralco (since January 2014)

Mr. Andrada is a Director of CIS Bayad Center, Inc., General Electric Philippines Meter and Instrument Co., Inc., Republic Surety and Insurance Co., Inc., Meralco Industrial Engineering Services Corporation and Lighthouse Overseas Insurance Company, Ltd. He is also the Director and Treasurer of Clark Electric Distribution Corporation; and Treasurer of Meralco PowerGen Corporation, Calamba Aero Power Corporation, Redondo Peninsula Energy, Inc. and Atimonan Land Ventures Development Corporation. He was formerly a Director of Rockwell Land Corporation and Rockwell Leisure Club, Inc.

RUBEN B. BENOSA, 57, Filipino
First Vice President (since January 2010) and Head, Corporate Logistics Office

Mr. Benosa is the Chairman of Meralco Financial Services Corporation. He serves as Director of Radius Telecoms, Inc., Meralco Energy, Inc. and Miescorrail, Inc. He has been the Chairman of Outsourced Telleserve Corporation; and was a Director of e-Meralco Ventures, Inc., MIESCOR Builders, Inc., Landbees Corporation and Bayan Trade.

HELEN T. DE GUZMAN, 56, Filipino
First Vice President (since January 2010) and Head, Internal Audit

Ms. De Guzman served as Director of Outsourced Telleserve Corporation now Customer Frontline Solutions, Inc. and MIESCOR Builders, Inc. She is a Member and Past Director and Chapter President of the Institute of Internal Auditors Philippines and the Philippine Institute of Certified Public Accountants. She was also the Honorary Treasurer and the Honorary Secretary of the Asian Confederation of Institutes of Internal Auditors in 2008 and 2012-2013, respectively.

IVANNA G. DELA PEÑA, 59, Filipino
First Vice President (since January 2010) and Head, Regulatory Management Office

Ms. Dela Peña is a Director of Radius Telecoms, Inc., Clark Electric Distribution Corporation, Share An Opportunity and Medical Ambassadors, Philippines.

WILLIAM S. PAMINTUAN, 52, Filipino
First Vice President (since January 2012), Deputy General Counsel, Assistant Corporate Secretary, Compliance Officer and Head, Legal and Corporate Governance Office

Atty. Pamintuan is the Corporate Secretary of Meralco PowerGen Corporation, Atimonan Land Ventures, Inc., Calamba Aero Power Corporation, Luzon Natural Gas Energy Corporation, Kalilayan Power, Inc., MPG Holdings Phils., Inc., MPG Mauban LP Corporation, Redondo Peninsula Energy, Inc., Miescorrail, Inc., Meralco Industrial Engineering Services Corporation and First Pacific Leadership Academy, Inc. He was a former Director of Miescorrail, Inc.; former Corporate Secretary and Senior Vice President of Digital Telecommunications Phils., Inc. and Digitel Mobile Phils., Inc.; and General Manager of Digitel Crossing, Inc. He is the incumbent Assistant Corporate Secretary of Cebu Pacific, Inc.

ANTONIO M. ABUEL, JR., 45, Filipino
Vice President (since January 2014) and Head, Sub-Transmission Services

Mr. Abuel is a Trustee of the Meralco Savings and Loan Association. He previously served as Chairman, President and Trustee of Meralco Employees Mutual Aid and Benefits Association, Inc.

IRENEO D. ACUNA, 48, Filipino
Vice President (since January 2013) and Head, Electric Distribution and Development Office

Mr. Acuna is a Director of MIESCOR Builders, Inc. He is also a Director and Treasurer of Meridian Atlantic Light Company, Limited (Nigeria). He was a former Director of Radius Telecoms, Inc., Landbees Corporation and e-Meralco Ventures, Inc.

RONNIE L. APEROCHO, 45, Filipino
Vice President (since January 2014) and Head, Networks - Designate

Mr. Aperocho is a Director of Meralco Employees Mutual Aid and Benefits Association, Inc.

ANGELITA S. ATANACIO, 55, Filipino
Vice President (since June 2008) and Head, Organization Transformation and Management Services

Ms. Atanacio is a Director of Meralco Financial Services Corporation. She previously served as Director of Miescorrail, Inc.

BENNETTE D. BACHOCO, 45, Filipino
Vice President (since September 2011) and Head, Financial Planning and Reporting

Ms. Bachoco is a Director of Meralco Financial Services Corporation, MIESCOR Builders, Inc., Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation) and Meralco Energy, Inc. She was Senior Vice President for Finance of Trans-Asia Oil and Energy Development Corporation.

EDGARDO V. CARASIG, 48, Filipino
Vice President (since January 2013) and Head, HR Operations

Mr. Carasig is a Director of MIESCOR Builders, Inc., Miescor Logistics and Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation).

MARTHYN S. CUAN, 34, Filipino
Vice President (since January 2011) and Chief Information Officer

Mr. Cuan is a Director of Radius Telecoms, Inc. and Indra Philippines, Inc. He is the Vice President and Co-Founder of Ideospace Foundation. He served as the Operations Head, Information Enterprise Services of Deutsche Bank Group-Manila Shared Service Center.

RUSTICO C. DE BORJA, JR. 59, Filipino
Vice President (since July 2007) and Head, Central Distribution Services

Mr. De Borja was a former Director of Meralco Industrial Engineering Services Corporation, MIESCOR Builders, Inc., and Meralco Employees Savings and Loan Association. He also served as Trustee of Meralco Management and Leadership Development Corporation.

GERARDO F. DELA PAZ, 55, Filipino
Vice President (since January 2010) and Deputy Head, Corporate Governance

Mr. Dela Paz is a Trustee of Good Governance Advocates and Practitioners of the Philippines. He previously served as a Trustee and Treasurer of Meralco Management and Leadership Development Corporation; and the Secretary and Treasurer of Harvest Time Philippines.

MANOLO C. FERNANDO, 58, Filipino
Vice President (since January 2010), Assistant Treasurer (since July 2001) and Head, Treasury Services

Mr. Fernando is a Director of Republic Surety and Insurance Co., Inc., Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation), Miescor Logistics, Inc. and ATRKE Philippine Balanced Fund, Inc. He is also the President and Director of Meralco Financial Services Corporation; Treasurer of Meralco Energy, Inc., Meralco Industrial Engineering Services Corporation, e-Meralco Ventures, Inc. and Radius Telecoms, Inc.

FERDINAND O. GELUZ, 49, Filipino
Vice President (since January 2013) and Head, HMB – Central Business Area

Mr. Geluz previously served as a Director of Meralco Energy, Inc.

VICTOR S. GENUINO, 42, Filipino
Vice President (since January 2011) and Head, Corporate Business Group

Mr. Genuino is a Director of Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation), Miescor Logistics, Inc., MIESCOR Builders, Inc. and Loyola Meralco Sparks FC. He was former District Head, Hong Kong and Singapore of PLDT (HK) Ltd.

NIXON G. HAO, 55, Filipino
Vice President (since June 2008) and Head, Network Asset Management

Mr. Hao is a Director of Clark Electric Distribution Corporation, Philippine Electricity Market Corporation and Society of Risk Management Professionals, Inc. He was a former Director of Meralco Employees Savings and Loan Association.

ERNIE G. IMPERIAL, 45, Filipino
Vice President (since January 2014) and Head, Business Transformation Office

Mr. Imperial served as the Senior Vice President and Hubs Central Team Head – Manila Hub of Australia and New Zealand Bank (ANZ); and Vice President of Deutsche Knowledge Services, Ltd.

DEXTER C. LEE, 40, Filipino
Vice President (since January 2014)

Mr. Lee is the President and Chief Executive Officer of Meralco Energy, Inc. (MServ). He is concurrently the Head of Strategy Development and Initiatives, Meralco and a member of the Board of Directors of MServ. He is presently a Trustee of the Wharton Penn Alumni Association, Inc.

FORTUNATO C. LEYNES, 56, Filipino
Vice President (since January 2006)

Mr. Leynes was appointed as Chief Executive Officer of Ibadan Electricity Distribution Company, privatized and acquired by the Nigerian investor, Integrated Energy Distribution and Marketing Limited. He was formerly a Director of Clark Electric Distribution Corporation and Meralco Financial Services Corporation; and was the Chairman of the Board of Electrical Engineering, Professional Regulation Commission.

REDENTOR L. MARQUEZ, 56, Filipino
Vice President (since January 2008) and Head, HMB – North Business Area

Mr. Marquez served as a Director of Meralco Savings and Loan Association, Meralco Energy, Inc. and Meralco Industrial Engineering Services Corporation.

RAYMOND B. RAVELO, 36, Filipino
Vice President (since May 2011) and Head, Corporate Business Strategy

Mr. Ravelo is the President and Chief Executive Officer and a member of the Board of Directors of Radius Telecoms, Inc. He was formerly a Trustee of Wharton Penn Alumni Association, Inc.

JOSE RAINIER A. REYES, 45, Filipino
Vice President (since January 2013) and Head, Small & Medium Enterprise Business Group

Mr. Reyes was formerly the Head of Sales of Globe Telecom.

NESTOR P. SARMIENTO, 55, Filipino
Vice President (since January 2012) and Head, Engineering Design

Mr. Sarmiento serves as a Director of Miescor Logistics, Inc., MIESCOR Builders, Inc. and Radius Telecoms, Inc. He is also a Director and the Corporate Secretary of Distribution Management Committee representing Luzon Private and Local Government Distributors.

LIZA ROSE G. SERRANO-DIANGSON, 54, Filipino
Vice President (since January 2010) and Head, Customer Process

Ms. Serrano-Diangson was a former Trustee of Meralco Millennium Foundation, Inc.; and was a Director of Customer Frontline Solutions, Inc. (formerly Outsourced Telleserve Corporation).

MANUEL LORENZO L. TUASON, 51, Filipino
Vice President (since January 2014)

Mr. Tuason is the President and Chief Executive Officer and a member of the Board of Directors of CIS Bayad Center, Inc. He is concurrently the President and Chief Executive Officer of Customer Frontline Solutions, Inc.; and President of Corporate Information Solutions, Inc.

JOSE ANTONIO T. VALDEZ, 49, Filipino
Vice President (since January 2011) and Head, Marketing, Customer and Product Development

Mr. Valdez served as the Head of Business Development and Marketing of PLDT Global Corporation and Vice President for Retail Marketing of PLDT. He is a Director of Bahay Maria, a shelter for street children in Makati.

Term of Office

The Directors are elected at the annual meeting of stockholders for a term of one year, until their successors are duly elected and qualified.

Nominees

The members of the Board of Directors of *MERALCO* are elected from a Final List of Candidates qualified by its Nomination and Governance Committee. The Final List of Candidates is determined after pre-screening and evaluation of qualifications of the nominees nominated by stockholders of record. The Nomination and Governance Committee is composed of Pedro E. Roxas, as Chairman, and Lance Y. Gokongwei, Napoleon L. Nazareno, Jose Ma. K. Lim and James L. Go as members. The candidates for directors for the ensuing calendar year are:

1. Ray C. Espinosa
2. James L. Go
3. John L. Gokongwei, Jr.
4. Lance Y. Gokongwei
5. Jose Ma. K. Lim
6. Manuel M. Lopez
7. Napoleon L. Nazareno
8. Artemio V. Panganiban
9. Manuel V. Pangilinan
10. Oscar S. Reyes
11. Pedro E. Roxas

Below is a summary of relevant information regarding the nominees for independent directors:

Name of Nominee	Nominated By	Relationship	Date of First Appointment
Artemio V. Panganiban	Mark Dennis Y.C. Joven	None	May 27, 2008
Pedro E. Roxas	Mark Dennis Y.C. Joven	None	May 25, 2010

MERALCO has adopted the provisions of Rule 38 of the SRC on nominations and election of independent directors. (Article II, Section 2 of the Amended By-Laws, as approved by the SEC on June 14, 2005)

Significant Employees

The employees are the most valued asset of *MERALCO* and contribute to the attainment of its goals.

Family Relationships

There are no family relationships up to the fourth civil degree, either by consanguinity or affinity, among directors, executive officers, or nominees.

Involvement in Certain Legal Proceedings

The registrant is not aware of any legal proceedings that occurred during the past five (5) years of the nature required to be disclosed under Part IV of Annex “C” of the SRC with respect to directors and executive officers.

Certain Relationships and Related Transactions

Except with respect to the Related Party Transactions as discussed in Note 24 to the consolidated financial statements as at December 31, 2013 and 2012 and January 1, 2012 and for each of the three years in the period ended December 31, 2013, there was no transaction during the last two (2) years involving *MERALCO* in which any of its directors or executive officers, any nominee for election as director, or security holder owning 10% or more of *MERALCO*’s total outstanding shares and members of their immediate family had a material interest.

Item 10. Executive Compensation

Compensation of Directors and Officers

The aggregate annual compensation for the last two fiscal years and projected compensation for the ensuing year of *MERALCO*’s Chief Executive Officer and four most highly compensated executive officers, as a group, and all other key officers, other officers and directors, as a group, are as follows:

NAME	YEAR	SALARIES ¹	BONUSES	OTHER COMPENSATION ²
		(in Millions of Pesos)		
Chief Executive Officer and four (4) most highly compensated executive officers	Projected 2014	117	18	49
	2013 ³	106	16	233
	2012	92	14	34
All other key officers, other officers and directors as a group (excluding the CEO and four most highly compensated executive officers)	Projected 2014	197	27	76
	2013	167	22	332
	2012	137	17	44

¹ Basic salary, allowances and government-mandated 13th month pay.

² Includes mid-year bonus and special Christmas bonus.

³ Includes variable pay and other payments. Variable pay is an annual incentive plan that is based on both Company and individual employee performance.

⁴ Comprised of the following: Oscar S. Reyes, President & Chief Executive Officer; Ricardo V. Buencamino, Senior Executive Vice President & Head of Networks; Alfredo S. Panlilio, Senior Vice President & Head of Customer Retail Services & Corporate Communication; Betty C. Siy-Yap, Senior Vice President & Chief Finance Officer and Ramon B. Segismundo, Senior Vice President & Head of Human Resources & Corporate Services.

As provided in *MERALCO's* Amended By-Laws, directors, as such, shall not receive any stated salary for their services, but by resolution of the stockholders, a fixed sum and expenses of attendance, if any, may be allowed for attendance at each regular or special meeting of the *BOD*; but nothing herein contained shall be construed to preclude any director from serving the Company in any other capacity and receiving compensation therefor.

MERALCO has no standard arrangement on the remuneration of its existing directors and officers aside from the compensation herein stated.

Pursuant to the terms of *MERALCO's ESPP*, as at March 14, 2014, the equity securities beneficially owned by executive officers covered by subscriptions to existing offerings of the ESPP, including stock dividends, are as follows:

Title of Class	Name of Executive Officer	Number of Shares	Citizenship	Percent of Class
Common	Ricardo V. Buencamino	42,278	Filipino	0.00%
Common	Roberto R. Almazora	36,408	Filipino	0.00%
Common	Ruben B. Benosa	22,261	Filipino	0.00%
Common	Helen T. De Guzman	25,513	Filipino	0.00%
Common	Antonio M. Abuel, Jr.	7,927	Filipino	0.00%
Common	Ireneo D. Acuna	18,355	Filipino	0.00%
Common	Rustico C. De Borja, Jr.	23,043	Filipino	0.00%
Common	Gerardo F. Dela Paz	21,000	Filipino	0.00%
Common	Manolo C. Fernando	21,274	Filipino	0.00%
Common	Ferdinand O. Geluz	12,877	Filipino	0.00%
Common	Redentor L. Marquez	22,116	Filipino	0.00%
Common	Liza Rose G. Serrano-Diangson	22,689	Filipino	0.00%

Subscriptions under the Plan are payable over a period of 5 years through payroll deduction.

Item 11. Security Ownership of Certain Beneficial Owners and Management

(1) Security Ownership of Certain Record and Beneficial Owners

Based on *MERALCO's* stock and transfer book, the security ownership as of March 15, 2013 of certain record and beneficial owners of more than 5% of any class of its voting securities is as follows:

Title of Class	Name, address of Record Owner and Relationship with Issuer	Name of Beneficial Owner and Relationship with Record Owner	Citizenship	No. of Shares Held	Percent
Common	Beacon Electric Asset Holdings, Inc. 10/F MGO Bldg., Legaspi corner Dela Rosa Streets, Legaspi Village, Makati City	Same as the record owner	Filipino	563,124,042	49.96%
Common	JG Summit Holdings, Inc. 42/F Robinsons Equitable Tower, ADB Avenue corner Poveda Road, Ortigas Center, Pasig City	Same as the record owner	Filipino	153,191,489 152,497,908 *	13.59% 13.53%
Common	PCD Nominee Corp. 37/F Tower One Enterprise Center, 6766 Ayala Avenue corner Paseo de Roxas, Makati City	PCD Participants	Filipino and Foreign	316,273,655	28.06%

**lodged & part of the 28.06% of PCD*

Beacon Electric Asset Holdings, Inc. or *Beacon Electric* is a special purpose company jointly owned by PLDT Communications and Energy Ventures, Inc. or *PCEV* formerly Pilipino Telephone Corporation and Metro Pacific Investments Corporation or *MPIC* whose sole purpose is to hold *PCEV*'s and *MPIC*'s shares in *MERALCO*. The Chairman, or in his absence, the President of *Beacon Electric*, or any other representative designated by the President of Beacon Electric, is duly authorized as proxy to vote its *MERALCO* shares as he may deem proper or beneficial to *Beacon Electric*.

JG Summit Holdings, Inc. or *JG Summit* was incorporated in November 1990 as the holding company for a group of companies with substantial business interests in branded consumer foods, agro-industrial and commodity food products, property development and hotel management, air transportation, petrochemicals, and international capital and financial services. In addition, *JG Summit* has business interests in other sectors, including power generation and insurance. The Company conducts its businesses throughout the Philippines, but primarily in and around Metro Manila and in the regions of Visayas and Mindanao. *JG Summit*, through its

subsidiaries, also has branded foods businesses in the People's Republic of China and the ASEAN region, including an interest in a property development company in Singapore. The Chairman, or in his absence, the President of *JG Summit*, or any other representative designated by the President of *JG Summit*, is duly authorized as proxy to vote its *MERALCO* shares as he may deem proper or beneficial to *JG Summit*.

PCD Nominee Corporation is a wholly-owned subsidiary of the Philippine Depository and Trust Corporation or *PDTC*. Originally, stock certificates were issued to investors every time they acquired shares of the Company. However, with the Philippine Central Depository's or *PCD* computerized Book Entry System that took effect in November 1997, investors of *MERALCO* shares now have an option whether they will be issued certificates or not. Their shares may be lodged at the *PCD* and further trading will be scripless (computerized with no certificates) until they request for the issuance of certificates. The *PCD* Nominee Corporation holds the shares as the registered owner thereof in *MERALCO*'s books on behalf of *PCD* Participants and their clients. The participants of *PCD* are the beneficial owners of such shares and may be nominated as proxy to vote the same. Stockholders with *PCD*-lodged shares have no record of their shareholdings with *MERALCO* or its transfer agent, Securities Transfer Services, Inc. or *STSI*. Only certificated shares are recorded in *MERALCO*'s books, which may be voted by the registered owners or their proxies.

(2) Security Ownership of Management

As of March 14, 2014, the securities fully paid and owned beneficially, directly or indirectly, by directors, nominees and executive officers of *MERALCO* are as follows:

Title of Class	Name of Beneficial Owner	Number of Shares and nature of Beneficial Ownership	Citizenship	Percent of Class
Common	Manuel V. Pangilinan	25,000 (Direct)	Filipino	0.00%
Common	Oscar S. Reyes	268 (Direct)	Filipino	0.00%
Common	Ray C. Espinosa	21,000 (Direct)	Filipino	0.00%
Common	James L. Go	10 (Direct)	Filipino	0.00%
Common	John L. Gokongwei, Jr.	10 (Direct)	Filipino	0.00%
Common	Lance Y. Gokongwei	10 (Direct)	Filipino	0.00%
Common	Jose Ma. K. Lim	10 (Direct)	Filipino	0.00%
Common	Manuel M. Lopez	2,245,918 (Direct)	Filipino	0.20%
Common	Napoleon L. Nazareno	1,000 (Direct)	Filipino	0.00%
Common	Artemio V. Panganiban	1 (Direct)	Filipino	0.00%
Common	Pedro E. Roxas	1,000 (Direct)	Filipino	0.00%
Common	Simeon Ken R. Ferrer	767 (Direct)	Filipino	0.00%
Common	Ricardo V. Buencamino	20,000 (Direct)	Filipino	0.00%
Common	Roberto R. Almazora	56,674 (Direct)	Filipino	0.01%
Common	Ramon B. Segismundo	6,500 (Direct)	Filipino	0.00%
Common	Rafael L. Andrada	20,000 (Direct)	Filipino	0.00%

Common	Ruben B. Benosa	11,731 (Direct)	Filipino	0.00%
Common	Helen T. De Guzman	2,591 (Direct)	Filipino	0.00%
Common	Ivanna G. Dela Peña	26,731 (Direct)	Filipino	0.00%
Common	Antonio M. Abuel, Jr.	2,500 (Direct)	Filipino	0.00%
Common	Ronnie L. Aperoch	14 (Direct)	Filipino	0.00%
Common	Angelita S. Atanacio	1,000 (Direct)	Filipino	0.00%
Common	Marthyn S. Cuan	2,150 (Direct)	Filipino	0.00%
Common	Rustico C. De Borja, Jr.	31,194 (Direct)	Filipino	0.00%
Common	Gerardo F. Dela Paz	9,074 (Direct)	Filipino	0.00%
Common	Manolo C. Fernando	14,456 (Direct)	Filipino	0.00%
Common	Ferdinand O. Geluz	1,000 (Direct)	Filipino	0.00%
Common	Nixon G. Hao	2,791 (Direct)	Filipino	0.00%
Common	Ernie G. Imperial	460 (Direct)	Filipino	0.00%
Common	Fortunato C. Leynes	6,000 (Direct)	Filipino	0.00%
Common	Nestor P. Sarmiento	18,976 (Direct)	Filipino	0.00%
Common	Manuel Lorenzo L. Tuason	22,180 (Direct)	Filipino	0.00%
Common	Liza Rose G. Serrano-Diangson	16,294 (Direct)	Filipino	0.00%

The aggregate number of shares owned on record by the Chief Executive Officer, Executive Officers, Directors and Nominees as of March 14, 2014 is 2,567,310 shares or 0.23% of *MERALCO*'s total outstanding shares.

(3) Voting Trust Holders

MERALCO is not aware of any person holding more than 5% of common shares under a voting trust or similar agreement.

(4) Changes in Control

Based on *MERALCO*'s stock and transfer book, there is no change in the control of *MERALCO* since the beginning of the last fiscal year.

Item 12. Certain Relationships and Related Transactions

Except with respect to the Related Party Transactions as discussed in Note 24 to the consolidated financial statements as at December 31, 2013 and 2012 and January 1, 2012 and for each of the three years in the period ended December 31, 2013, there was no transaction during the last two (2) years involving *MERALCO* in which any of its directors or executive officers, any nominee for election as director, or security holder owning 10% or more of *MERALCO*'s total outstanding shares and members of their immediate family had a material interest.

PART IV – CORPORATE GOVERNANCE

Item 13. Corporate Governance

In accordance with the SEC MEMORANDUM CIRCULAR NO. 5, Series of 2013, the Corporate Governance section in the Annual Report (SEC Form 17-A) has been deleted.

PART V- EXHIBITS AND SCHEDULES

Item 14. Exhibits and Reports

(a) Report on SEC Form 17-C and other Disclosure

	JANUARY 2013
JANUARY 3	<ul style="list-style-type: none"> SEC Form 17-C – Press Release: Meralco files application with the Energy Regulatory Commission for approval of Power Supply Agreements with Therma Luzon, Inc. and AP Renewables, Inc.
JANUARY 4	<ul style="list-style-type: none"> SEC Form 17-C – Certification of Attendance of Meralco directors in Board Meetings and Board Committee Meetings for the period January 2012 to December 2012.
JANUARY 7	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended December 31, 2012.
JANUARY 7	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended December 31, 2012.
JANUARY 8	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities of Beacon Electric Assets Holdings, Inc.
JANUARY 9	<ul style="list-style-type: none"> Clarification of News Article: “Meralco sets 2013 capex at P13B” published in the January 8, 2013 issue of the Business Mirror.
JANUARY 10	<ul style="list-style-type: none"> Top 100 stockholders for quarter ended December 31, 2012.
JANUARY 11	<ul style="list-style-type: none"> Certification on Compliance of Corporate Governance Manual (in conformity with SEC Memo Circular No. 6, Series of 2009).
JANUARY 15	<ul style="list-style-type: none"> Public Ownership Level for quarter ended December 31, 2013.
JANUARY 16	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – IGDela Peña.
JANUARY 17	<ul style="list-style-type: none"> Clarification of News Article: “Meralco met P16-B profit goal in 2012” published in the January 17, 2013 issue of Business Mirror.
JANUARY 21	<ul style="list-style-type: none"> Clarification of News Article: “Meralco eyes P4-B loans” posted in Philstar.com on January 21, 2013.
JANUARY 22	<ul style="list-style-type: none"> SEC Form 23-B –Statement of Changes in Beneficial Ownership of Securities – RLAndrada.
JANUARY 28	<ul style="list-style-type: none"> SEC Form 17-C – Results of the meeting of the Board of Directors of Meralco on January 28, 2013 (record date for the purpose of determining the stockholders entitled to notice and to vote at the Company’s SHs meeting; deadline for the submission of nominations for regular and independent director; deadline for the submission of proxies or instruments authorizing attorneys-in-fact to attend and vote in the annual stockholders meeting; registration of Meralco’s local RES; filing by Meralco of an application to secure a license as a DU-RES; execution of MOU between Meralco PowerGen Corporation and Global Business Power Corporation; and execution of a Tri-Partite Agreement⁹⁹between Meralco, Trans-Asia Oil and PEZA).

JANUARY 28	<ul style="list-style-type: none"> Clarification of News Article: “Meralco seeks partners for major SEA projects” published in the January 28, 2013 issue of the Philippine Star.
JANUARY 30	<ul style="list-style-type: none"> Clarification of New Article: “Meralco, Metro bank to put up four coal plants” published in the January 30, 2013 issue of Manila Standard Today.
JANUARY 30	<ul style="list-style-type: none"> SEC Form 23-B –Statement of Changes in Beneficial Ownership of Securities – RLAndrada.
JANUARY 30	<ul style="list-style-type: none"> SEC Form 23-B –Statement of Changes in Beneficial Ownership of Securities – NHao.

FEBRUARY 2013	
FEBRUARY 1	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – IGDela Peña.
FEBRUARY 5	<ul style="list-style-type: none"> Clarification of News Articles: (i) “Meralco bares P95-B 7year expansion” published in the February 5, 2013 issue of the Manila Bulletin; (ii) “Meralco to spend P95-B up to 2019, eyes Asian opportunities” posted in Business World Online on February 5, 2013.
FEBRUARY 6	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended January 31, 2013.
FEBRUARY 6	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended January 31, 2013.
FEBRUARY 7	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – IGDela Peña.
FEBRUARY 7	<ul style="list-style-type: none"> Addendum to previous disclosure - clarification of news article: “Meralco bares P95-B 7year expansion” published in the February 5, 2013 issue of the Manila Bulletin.
FEBRUARY 7	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – GFDelaPaz.
FEBRUARY 11	<ul style="list-style-type: none"> Clarification of News Article: “DMCI seeks partners for Calaca plant expansion” posted in Philstar.com on February 11, 2013.
FEBRUARY 12	<ul style="list-style-type: none"> Sec Form 17-C – Invitation to presentation and teleconference presentation on February 25, 2013 re: year end 2012 financial and operating results.
FEBRUARY 12	<ul style="list-style-type: none"> SEC 23-B - Statement of Changes in Beneficial Ownership of Securities – LSDiangson.
FEBRUARY 25	<ul style="list-style-type: none"> SEC Form 17-C – Results of the meeting of the Board of Directors of Meralco on February 25, 2013 (approval of 2012 Audited FS; declaration of cash dividends; execution of Power Supply Agreement with Therma Mobile, Inc.; press release re: financial and operating results for the year ended December 31, 2012).
FEBRUARY 26	<ul style="list-style-type: none"> Clarification of New Articles: (i) “Meralco net profit hits P16.3B”; and (ii) “2 MGEN plants running by 2018” published in the February 26, 2013 issue of the Philippine Daily Inquirer.
FEBRUARY 27	<ul style="list-style-type: none"> Clarification of News Article: “Meralco eyes Thailand,

	Myanmar” posted in businessmirror.com.ph on the February 26, 2013.

MARCH 2013	
MARCH 4	<ul style="list-style-type: none"> • Sec Form 17-C - Press Release: Meralco invest in Singapore Power Plant Joint Venture Company with First Pacific takes 70% ownership in GMR Energy Singapore Pte. Ltd.
MARCH 5	<ul style="list-style-type: none"> • Compliance Report on Corporate Governance Guidelines Disclosure Survey for year 2012 (PSE).
MARCH 5	<ul style="list-style-type: none"> • Total issued and outstanding shares/foreign ownership level for the month ended February 28, 2013.
MARCH 5	<ul style="list-style-type: none"> • Report on number of stockholders-boardlot for the month ended February 28, 2013.
MARCH 13	<ul style="list-style-type: none"> • Clarification of News Articles: (i) “We’re open, MVP says to Malaysia’s Petronas” posted in businessmirror.com.ph on March 12, 2013; (ii) “Summer, Solaire opening to spur electricity demand” published in the March 13, 2013 issue of The Philippine Star.
MARCH 19	<ul style="list-style-type: none"> • Clarification of News Article: “Meralco pursuing takeover of more power firms” published in the March 19, 2013 issue of the Malaya Business Insight.
MARCH 21	<ul style="list-style-type: none"> • List of Stockholders of Meralco as of March 15, 2013.
MARCH 22	<ul style="list-style-type: none"> • SEC Form 17-C- Results of the meeting of the Board of Directors of Meralco on March 22, 2013 (list of nominees to the Board of Directors and amendments to By-laws).

APRIL 2013	
APRIL 1	<ul style="list-style-type: none"> • Clarification of News Article: “First Pacific, Meralco seal power plant sale” published in the April 1, 2013 issue of the Manila Standard Today.
APRIL 4	<ul style="list-style-type: none"> • Total issued and outstanding shares/foreign ownership level for the month ended March 31, 2013.
APRIL 4	<ul style="list-style-type: none"> • Report on number of stockholders-boardlot for the month ended March 31, 2013.
APRIL 12	<ul style="list-style-type: none"> • Top 100 Stockholders for quarter ended March 31, 2013.
APRIL 15	<ul style="list-style-type: none"> • Public Ownership Report for the quarter ended March 31, 2013.
APRIL 15	<ul style="list-style-type: none"> • SEC Form 17-C – Invitation to presentation and teleconference presentation on April 22, 2013 re: first quarter 2013 financial and operating results.
APRIL 15	<ul style="list-style-type: none"> • 2012 Annual Report of Meralco.
APRIL 18	<ul style="list-style-type: none"> • SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – IGDela Peña.
APRIL 18	<ul style="list-style-type: none"> • Change in number of outstanding shares due to cancellation of shares under Employee Stock Purchase Plan.
APRIL 19	<ul style="list-style-type: none"> • Clarification of News Article: “Meralco clinches deals in Africa” posted in Inquirer.net on April 19, 2013.
APRIL 22	<ul style="list-style-type: none"> • SEC Form 17-C: Press Release: Financial and Operating Results for the First Quarter ended March 31, 2013.

APRIL 22	<ul style="list-style-type: none"> SEC Form 17-C: Amended Press Release: Financial and Operating Results for the First Quarter ended March 31, 2013.
APRIL 23	<ul style="list-style-type: none"> Clarification of News Article: "MVP group exploring power partnerships in Mindanao" published in the April 23, 2013 issue of The Philippine Star.
APRIL 24	<ul style="list-style-type: none"> Clarification of News Article: "Meralco eyes 2 Nigerian power firms" posted in Philstar.com on April 24, 2013.
APRIL 26	<ul style="list-style-type: none"> SEC Form 20-IS Definitive Information Statement – Definitive Information Statement for Annual Meeting of the Stockholders on May 28, 2013 with record date March 15, 2013.

MAY 2013	
MAY 6	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – IGDela Peña.
MAY 8	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended April 30, 2013.
MAY 8	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended April 30, 2013.
MAY 14	<ul style="list-style-type: none"> Clarification of News Article: "Meralco mulls Angat plant Equity" published in the May 13, 2013 issue of the Manila Bulletin.
MAY 16	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities – LSerrano-Diangson.
MAY 16	<ul style="list-style-type: none"> SEC Form 17-Q – Quarterly Report for the period ended March 31, 2013.
MAY 28	<ul style="list-style-type: none"> SEC Form 17-C – Results of the Annual Meeting of the Stockholders and Organizational Meeting of the Board of Directors 2013.
MAY 29	<ul style="list-style-type: none"> Clarification of News Article: "Meralco sales up 3.2% in 4 months" published in the May 29, 2013 issue of The Philippine Star.
MAY 31	<ul style="list-style-type: none"> Clarification of News Article: "Meralco eyeing equity increase in Nigerian venture" posted in Manila Bulletin internet edition on May 31, 2013.

JUNE 2013	
JUNE 6	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended May 31, 2013.
JUNE 6	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended May 31, 2013.
JUNE 10	<ul style="list-style-type: none"> Clarification of news articles: (i) "Meralco eyes nationwide distribution business", published in the June 10, 2013 issue of the Manila Bulletin; (ii) "3 Ph firms set sights on Myanmar" posted in abs-cbnnews.com on June 9, 2013.
JUNE 17	<ul style="list-style-type: none"> Clarification of news article: "Meralco still keen on tie-up with K-Water" published in the June 17, 2013 issue of Business Mirror.

JUNE 21	<ul style="list-style-type: none"> Standard & Poor's Ratings Services raised its long-term corporate credit rating to Meralco.
JUNE 26	<ul style="list-style-type: none"> Clarification of news article: "Philex, Meralco eye joint venture to build 80MW coal plant" published in the June 26, 2013 issue of the Manila Standard Today.
JUNE 26	<ul style="list-style-type: none"> SEC Form 23-B - Statement of Changes in Beneficial Ownership of Securities –RBSegismundo.
JUNE 26	<ul style="list-style-type: none"> General Information Sheet of Meralco for 2013.
JUNE 27	<ul style="list-style-type: none"> Annual Corporate Governance Report (SEC).

JULY 2013	
JULY 3	<ul style="list-style-type: none"> SEC Form 17-C- Receipt of ERC Order on ERC Case No. 2013-056 RC.
JULY 5	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended June 30, 2013.
JULY 5	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended June 30, 2013.
JULY 10	<ul style="list-style-type: none"> Top 100 stockholders for quarter ended June 30, 2013.
JULY 12	<ul style="list-style-type: none"> SEC Form 23-A – Initial Statement of Beneficial Ownership of Securities –FOGeluz.
JULY 15	<ul style="list-style-type: none"> Public Ownership Report for the quarter ended June 30, 2013.
JULY 15	<ul style="list-style-type: none"> SEC Form 17-C – Invitation to Presentation and Teleconference Presentation on July 29, 2013 re: First Half 2013 Financial and Operating Results.
JULY 18	<ul style="list-style-type: none"> Clarification of news article: "Meralco joins Quezon Power Expansion" posted in Manila Bulletin internet edition on the July 18, 2013.
JULY 29	<ul style="list-style-type: none"> SEC Form 17-C –Results of the meeting of the Board of Directors held on July 29, 2013 (declaration of cash dividends, press release re: Financial and Operating Results for the First Half 2013).
JULY 31	<ul style="list-style-type: none"> Clarification of news article: "Philex, Meralco in talks for power plant JV in Surigao" published in the July 31, 2013 issue of The Philippine Star.

AUGUST 2013	
AUGUST 1	<ul style="list-style-type: none"> Clarification of news article: "Meralco, SMC eye Albay Power co-op" posted in Inquirer.net on July 31, 2013.
AUGUST 5	<ul style="list-style-type: none"> Report on number of stockholders-boardlot for the month ended July 30, 2013.
AUGUST 5	<ul style="list-style-type: none"> Clarification of news articles: (i) "Meralco sees Entertainment City as new growth area" posted in philstar.com on August 5, 2013; (ii) "Meralco may buy ailing cooperatives" published in the August 5, 2013 issue of the Malaya Business Insight.
AUGUST 5	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities – SMC.
AUGUST 5	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level

	for the month ended July 30, 2013.
AUGUST 7	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities – Beacon Electric Assets Holdings, Inc.
AUGUST 7	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities – ASPanlilio.
AUGUST 8	<ul style="list-style-type: none"> Clarification of news article: “Entertainment City to raise Meralco sales” published in the August 8, 2013 issue of the Manila Standard.
AUGUST 12	<ul style="list-style-type: none"> Clarification of news article: “Manila Electric interested in San Miguel Power Assets” published in the August 9, 2013 issue of the Manila Bulletin.
AUGUST 14	<ul style="list-style-type: none"> SEC Form 17-Q – Quarterly Report for the period ended June 30, 2013.
AUGUST 15	<ul style="list-style-type: none"> Public Ownership Report for the month ended July 31, 2013.
AUGUST 23	<ul style="list-style-type: none"> SEC Form 17-C – Board authorization to Meralco PowerGen Corporation to execute agreements re: coal fired plant in Mauban, Quezon.
AUGUST 28	<ul style="list-style-type: none"> Clarification of news article: “Meralco Board gives go-signal on Quezon power expansion tie-up” published in the August 28, 2013 issue of the Manila Bulletin.
AUGUST 30	<ul style="list-style-type: none"> Clarification of news article: “Meralco seeking refund from suppliers” posted in Manila Bulletin internet edition on the August 30, 2013.
AUGUST 30	<ul style="list-style-type: none"> SEC Form 17-C – Press Release: Meralco PowerGen Corporation and New Growth B.V. sign Joint Development Agreement for 460-MW coal-fired power plant project.

SEPTEMBER 2013	
SEPTEMBER 2	<ul style="list-style-type: none"> SEC Form 17-C – Arrangement of series of fixed income investor meetings in Singapore and Hong Kong re: Reg S USD Offering.
SEPTEMBER 2	<ul style="list-style-type: none"> SEC Form 17-C – Supplement to previous disclosure re: Reg S USD Offering.
SEPTEMBER 2	<ul style="list-style-type: none"> Clarification of news article: “Meralco hikes long-term capacity” posted in Philstar.com on September 2, 2013.
SEPTEMBER 5	<ul style="list-style-type: none"> Report on number of stockholders/boardlot for the month ended August 31, 2013.
SEPTEMBER 6	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended August 31, 2013.
SEPTEMBER 20	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities – NPSarmiento.
SEPTEMBER 23	<ul style="list-style-type: none"> SEC Form 17-C –Results of the meeting of the Board of Directors on September 23, 2013 (approval of offering of Peso long-term bonds and signing of Power Supply Agreement with Therma Mobile, Inc.).
SEPTEMBER 24	<ul style="list-style-type: none"> Clarification of news articles: (i) “Meralco OKs P20B worth of bond sale” posted in Manila Standard Today internet edition on September 24, 2013; (ii) “Meralco looking to raise P20B”

	published in the September 24, 2013 issue of the Business World.
SEPTEMBER 27	<ul style="list-style-type: none"> Filing of Registration Statement with the Securities and Exchange Commission for the issuance of 7-year and 12-year corporate bonds in an aggregate amount of Fifteen Billion Pesos (PhP15,000,000,000.00) with an over-allotment option of up to Five Billion Pesos (PhP5,000,000,000.00).
SEPTEMBER 30	<ul style="list-style-type: none"> Clarification of news article: "Meralco plans to sell \$250-m debt overseas" published in the September 30, 2013 issue of the Manila Standard Today.

OCTOBER 2013	
OCTOBER 2	<ul style="list-style-type: none"> SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities – RCEspinosa.
OCTOBER 4	<ul style="list-style-type: none"> Report on number of stockholders/boardlot for the month ended September 30, 2013.
OCTOBER 4	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended September 30, 2013.
OCTOBER 8	<ul style="list-style-type: none"> Letter-Reply to SEC – CFD Re: compliance with SEC Memo Circular No. 18, Series of 2013 dated Oct 2, 2013, posting of ACGR in company website.
OCTOBER 8	<ul style="list-style-type: none"> SEC Form 17-C – Share Sale and Purchase Agreement of Meralco PowerGen Corporation and First Metro Pacific Investment Corporation re: acquisition of 20% stake in Global Business Power Corporation.
OCTOBER 9	<ul style="list-style-type: none"> Top 100 Stockholders for quarter ended September 30, 2013.
OCTOBER 14	<ul style="list-style-type: none"> Public Ownership Report for the quarter ended September 30, 2013.
OCTOBER 22	<ul style="list-style-type: none"> SEC Form 17-C – Press Release: Meralco PowerGen Corporation and First Metro Investment Corporation sign Shareholders' Agreement for 20% of Global Power.
OCTOBER 25	<ul style="list-style-type: none"> SEC Form 17-C – Press Release: 3Q 2013 Financial and Operating Results.
OCTOBER 29	<ul style="list-style-type: none"> Clarification of news article: "Meralco, JS Summit in talks for new power business" posted in philSTAR.com on October 28, 2013.

NOVEMBER 2013	
NOVEMBER 4	<ul style="list-style-type: none"> Clarification of News Articles: (i) "Meralco's Singapore plant defers opening to January" published in the November 1, 2013 issue of the Manila Standard Today; (ii) Meralco to bid out deal for Mauban facility" published in the November 4, 2013 issue of the Business Mirror.
NOVEMBER 7	<ul style="list-style-type: none"> Total issued and outstanding shares/foreign ownership level for the month ended October 31, 2013.
NOVEMBER 7	<ul style="list-style-type: none"> Report on number of stockholders/boardlot for the month ended October 31, 2013.
NOVEMBER 11	<ul style="list-style-type: none"> Clarification of News Article: "Meralco formalizes Nigerian

	expansion” published in the November 11, 2013 issue of the Manila Standard Today.
NOVEMBER 12	<ul style="list-style-type: none"> • SEC Form 17-C - Receipt of ERC Order re: approval of Power Supply Agreement with Therma Mobile, Inc.
NOVEMBER 13	<ul style="list-style-type: none"> • SEC Form 17- C - Press Release: Meralco’s Proposed Fixed Putable Bonds Receive Top PRS Aaa Credit rating.
NOVEMBER 15	<ul style="list-style-type: none"> • SEC Form 17-Q - Quarterly Report for the period ended September 30, 2013.
NOVEMBER 18	<ul style="list-style-type: none"> • Clarification of News Articles: (i) “Meralco sets P50-B Capex for LNG Project” posted in mb.com.ph on November 17, 2013; (ii) “Meralco spending P13B to improve distribution system” published in the November 18, 2013 issue of The Philippine Star.
NOVEMBER 18	<ul style="list-style-type: none"> • Amended Public Ownership Report for the Quarter ended September 30, 2013.
NOVEMBER 19	<ul style="list-style-type: none"> • Clarification of News Article: “Meralco, Egco seal partnership” posted in manilastandardtoday.com on November 19, 2013.

DECEMBER 2013	
DECEMBER 02	<ul style="list-style-type: none"> • Clarification of News Article: “Meralco gets SEC nod on P20-B bond issue” posted in philSTAR.com on November 30, 2013.
DECEMBER 02	<ul style="list-style-type: none"> • Advisement Letter: Receipt of SEC Certificate of Permit to Offer Securities for Sale in connection with Fixed Rate Bonds Total issued and outstanding shares/foreign.
DECEMBER 04	<ul style="list-style-type: none"> • Total issued and outstanding shares/foreign ownership level for the month ended November 30, 2013.
DECEMBER 04	<ul style="list-style-type: none"> • Report on number of stockholders/boardlot for the month ended November 30, 2013.
DECEMBER 06	<ul style="list-style-type: none"> • Clarification of News Article: “Quezon plant work starts 2014” published in the December 6, 2013 issue of the Business World.
DECEMBER 09	<ul style="list-style-type: none"> • Clarification of News Articles: (i) “Meralco raises ’14 capex to P15.6B” posted in philSTAR.com on December 9, 2013; (ii) “Meralco finalizing \$300-M bond issue” published in the December 9, 2013 issue of the Manila Standard Today.
DECEMBER 10	<ul style="list-style-type: none"> • SEC Form 17-C Press Release: Manila Electric Company 4.375% p.a. Fixed Rate Bonds due 2020 and 4.875% p.a. Fixed Rate Bonds due 2025.
DECEMBER 10	<ul style="list-style-type: none"> • SEC Form 17-C – Press Release: Ayala-First Pacific Consortium Wins LRT/MRT Contactless Fare System Project.
DECEMBER 10	<ul style="list-style-type: none"> • SEC Form 17-C – Approval of listing of PhP18.5Billion MER Fixed Rate Putable Bonds Due 2020 and Fixed Rate Putable Bonds due 2025.
DECEMBER 12	<ul style="list-style-type: none"> • SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities (Atty. RCEspinosa).
DECEMBER 13	<ul style="list-style-type: none"> • Clarification of News Article: “Electricity distributor eyes provincial acquisition” published in the December 13, 2013

	issue of the Business World”.
DECEMBER 16	<ul style="list-style-type: none"> • SEC Form 17-C – Election and Resignation of Directors (Messrs. James L. Go and Lance Y. Gokongwei in lieu of Messrs. Vicente L. Panlilio and Eric O. Recto).
DECEMBER 18	<ul style="list-style-type: none"> • SEC Form 23-A – Initial Statement of Beneficial Ownership of Securities (Messrs. James L. Go and Lance Y. Gokongwei).
DECEMBER 19	<ul style="list-style-type: none"> • SEC Form 17-C – Certificate of Attendance in Corporate Governance Seminar (Messrs. James L. Go and Lance Y. Gokongwei).
DECEMBER 20	<ul style="list-style-type: none"> • SEC Form 23-B – Statement of Changes in Beneficial Ownership of Securities (SMC’s ownership of shares in Meralco).
DECEMBER 20	<ul style="list-style-type: none"> • SEC Form 18-A - Amended Report by Owner of More than Five Percent (5%) SMC Global Power’s ownership of shares in Meralco).

SIGNATURES

Refer to the following page

SIGNATURES

Pursuant to the requirements of Section 17 of the Code and Section 141 of the Corporation Code, this report is signed on behalf of the issuer by the undersigned thereunto duly authorized, in the City of Pasig this 14 APR 2014 day of April 2014.

By:


OSCAR S. REYES
President


BENNETTE D. BACHOCO
Vice President


RAFAEL L. ANDRADA
First Vice President and
Treasurer


WILLIAM S. PAMINTUAN
First Vice President
Assistant Corporate Secretary and
Compliance Officer

SUBSCRIBED AND SWORN to before me this 14 APR 2014 April 2014 in Pasig City, by the above-named persons who exhibited to me their respective Tax Identification Numbers as follows:

NAME
Oscar S. Reyes
Rafael L. Andrada
Bennette D. Bachoco
William S. Pamintuan

Tax Identification Number
136-623-569
127-415-866
129-433-970
146-473-562

Doc. No. 156 ;
Page No. 33 ;
Book No. XXIX ;
Series of 2014.


ATTY. RAUL G. CORALDE
NOTARY PUBLIC
PASIG, PATEROS, TAGUIG AND SAN JUAN
ISSUED ON DECEMBER 20, 2012 AT PASIG CITY
UNTIL DECEMBER 31, 2014
ROLL NO. 35522/IBP NO. 947452/1-2-14 RSM CHAPTER
PTR NO. 9884656/1-21-14 PASIG CITY
8TH FLOOR LOPEZ BLDG. ORTIGAS AVENUE, PASIG CITY

INDEX TO FINANCIAL STATEMENTS AND SUPPLEMENTARY SCHEDULES

Index to Consolidated Financial Statements and Supplementary Schedules

- Statement of Management's Responsibility for Consolidated Financial Statements
- Report of Independent Auditors
- Consolidated Statement of Financial Position as at December 31, 2013 (With Comparative Figures as at December 31, 2012 and January 1, 2012)
- Consolidated Statement of Income for the Year Ended December 31, 2013 (With Comparative Figures for the Years Ended December 31, 2012 and 2011)
- Consolidated Statement of Comprehensive Income for the Year Ended December 31, 2013 (With Comparative Figures for the Years Ended December 31, 2012 and 2011)
- Consolidated Statement of Changes in Equity for the Year Ended December 31, 2013 (With Comparative Figures for the Years Ended December 31, 2012 and 2011)
- Consolidated Statement of Cash Flows for the Year Ended December 31, 2013 (With Comparative Figures for the Years Ended December 31, 2012 and 2011)
- Notes to Consolidated Financial Statements
- Supplementary Schedules
 - Report of Independent Auditors on Supplementary Schedules
 - Schedule A. Financial Assets*
 - Schedule B. Amounts Receivable From Directors, Officers, Employees Related Parties and Principal Stockholders (Other than Related Parties)*
 - Schedule C. Amounts Receivable From Related Parties which are Eliminated during the Consolidation of Financial Statements
 - Schedule D. The Movement of Intangible Assets - Other Assets
 - Schedule E. Long-term Debt
 - Schedule F. Indebtedness to Related Parties*
 - Schedule G. Guarantees of Securities of Other Issuers*
 - Schedule H. Capital Stock
 - Schedule I. List of Effective Standards and Interpretations
 - Schedule J. Reconciliation of Retained Earnings Available for Dividend Declaration
 - Schedule K. Map Showing the Relationships among the Companies within the Group
 - Financial Soundness Indicators
- Parent Company Financial Statements

**These schedules have been omitted because they are either not applicable or schedule is in the Consolidated Financial Statements.*



ORTIGAS AVENUE, PASIG CITY
0300 PHILIPPINES

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR CONSOLIDATED FINANCIAL STATEMENTS

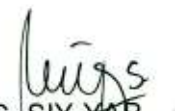
The Management of Manila Electric Company (the Company) is responsible for the preparation and fair presentation of the consolidated financial statements as at December 31, 2013 and 2012 and January 1, 2012, and for each of the three years in the period ended December 31, 2013, including the following components: a) Reconciliation of Retained Earnings Available for Dividend Declaration; b) Tabular Schedule of all the Effective Standards and Interpretations; c) Map showing the Relationships among the Companies within the Group; and d) Supplementary Schedules Required by Annex 68-E, in accordance with the prescribed financial reporting framework indicated therein. This responsibility includes designing and implementing internal controls relevant to the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies, and making accounting estimates that are reasonable in the circumstances.

The Board of Directors reviews and approves the consolidated financial statements and submits the same to the Stockholders.

SyCip Gorres Velayo & Co., as appointed by the Stockholders, has examined the consolidated financial statements of the Company in accordance with Philippine Standards on Auditing, and in its report to the Stockholders, has expressed its opinion on the fairness of presentation upon completion of such examination.


MANUEL V. PANGILINAN
Chairman of the Board


OSCAR S. REYES
President and Chief Executive Officer

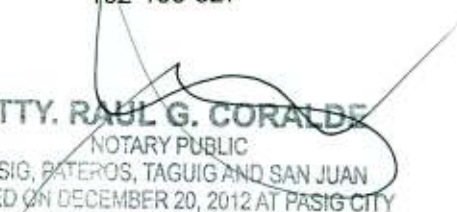

BETTY C. SIY-YAP
Chief Finance Officer

14 APR 2014

SUBSCRIBED AND SWORN to before me this ____ day of April 2014 in Pasig City, by the above-named persons who exhibited to me their respective Tax Identification Numbers as follows:

NAME	Tax Identification Number
Manuel V. Pangilinan	914-481-801
Oscar S. Reyes	136-623-569
Betty C. Siy-Yap	102-100-627

Doc. No. 158;
Page No. 32;
Book No. XXIX;
Series of 2014.


ATTY. RAUL G. CORALDE
NOTARY PUBLIC

PASIG, PATEROS, TAGUIG AND SAN JUAN
ISSUED ON DECEMBER 20, 2012 AT PASIG CITY
UNTIL DECEMBER 31, 2014

ROLL NO. 35523/IEP NO. 947452/1-2-14 RSM CHAPTER
PTR NO. 9884856/1-21-14 PASIG CITY
8TH FLOOR LOPEZ BLDG. ORTIGAS AVENUE, PASIG CITY

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Manila Electric Company
Lopez Building
Ortigas Avenue, Pasig City

Report on the Parent Company Financial Statements

We have audited the accompanying parent company financial statements of Manila Electric Company, which comprise the parent company statements of financial position as at December 31, 2013 and 2012, and the parent company statements of income, statements of comprehensive income, statements of changes in equity and statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Parent Company Financial Statements

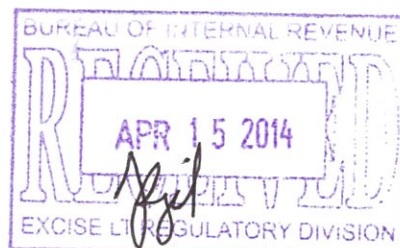
Management is responsible for the preparation and fair presentation of these parent company financial statements in accordance with Philippine Financial Reporting Standards, and for such internal control as management determines necessary to enable the preparation of parent company financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the parent company financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the parent company financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the parent company financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the parent company financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Manila Electric Company and Subsidiaries as at December 31, 2013 and 2012, and their financial performance and their cash flows for each of the three years in the period ended December 31, 2013 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.


Martin C. Guantes

Partner

CPA Certificate No. 88494

SEC Accreditation No. 0325-AR-2 (Group A),
March 15, 2012, valid until March 14, 2015

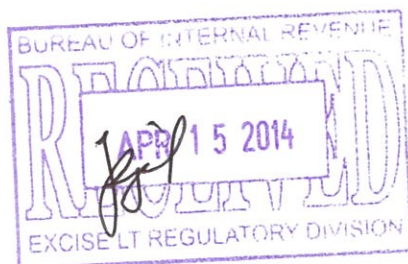
Tax Identification No. 152-884-272

BIR Accreditation No. 08-001998-52-2012,

April 11, 2012, valid until April 10, 2015

PTR No. 4225178, January 2, 2014, Makati City

March 17, 2014



MANILA ELECTRIC COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

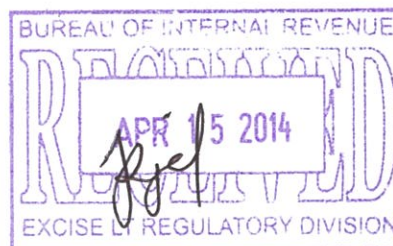
		December 31, 2012	January 1, 2012
	December 31, 2013	(As restated - see Note 4)	(As restated - see Note 4)
	Note		
(Amounts in millions)			
ASSETS			
Noncurrent Assets			
Utility plant and others	8 and 16	P112,586	P109,312
Investments in associates and joint ventures	9	13,422	1,815
Investment properties	10 and 16	1,526	1,634
Deferred tax assets - net	29	5,381	3,050
Other noncurrent assets - net	8, 11, 13, 28, 30 and 31	23,603	8,837
Total Noncurrent Assets		156,518	124,648
Current Assets			
Cash and cash equivalents	12 and 28	59,851	60,500
Trade and other receivables	11, 13, 19, 24 and 28	32,718	28,077
Inventories	14	2,750	1,371
Other current assets	15 and 28	12,167	2,295
		107,486	92,243
Assets of discontinued operations	6	-	-
Total Current Assets		107,486	92,243
Total Assets		P264,004	P216,891
EQUITY AND LIABILITIES			
Equity Attributable to Equity Holders of the Parent			
Common stock	16	P11,273	P11,273
Subscriptions receivable		(69)	(211)
Additional paid-in capital		4,111	4,111
Excess of acquisition cost over carrying value of non-controlling interest acquired		(328)	(328)
Employee stock purchase plan	17	1,049	1,049
Unrealized fair value gains on available-for-sale, or AFS, financial assets	11	105	120
Unrealized fair value gains on AFS financial assets of discontinued operations	6	-	-
Share in cumulative translation adjustments of a subsidiary and associates	9	389	3
Cumulative actuarial gains (losses)	4	1,446	289
Treasury shares	16	(11)	(11)
Retained earnings:	6 and 16		
Appropriated		11,000	6,000
Unappropriated		46,197	45,607
Equity Attributable to Equity Holders of the Parent		75,162	67,902
Non-controlling Interests		173	248
Total Equity		75,335	68,150

(Forward)



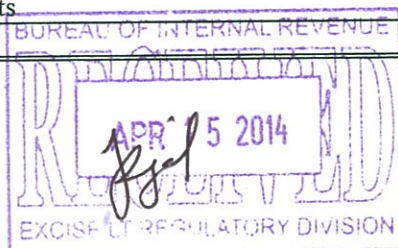
		December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
	Note			
<i>(Amounts in millions)</i>				
Noncurrent Liabilities				
Interest-bearing long-term financial liabilities - net of current portion	18, 26 and 28	₱20,756	₱20,466	₱19,816
Customers' deposits - net of current portion	19, 23 and 28	21,600	23,313	24,080
Long-term employee benefits	27	4,183	8,833	10,558
Provisions	20 and 30	24,729	19,411	16,919
Refundable service extension costs - net of current portion	23 and 28	5,782	4,357	3,794
Deferred tax liabilities - net	29	1	—	595
Other noncurrent liabilities	25 and 28	16,992	12,843	6,302
Total Noncurrent Liabilities		94,043	89,223	82,064
Current Liabilities				
Notes payable	22, 26 and 28	1,814	1,787	67
	16, 18, 19, 23, 24 and 28	73,892	47,576	40,011
Trade payables and other current liabilities				
Customers' refund	2, 21 and 28	6,013	6,127	6,250
Income tax payable		1,886	1,668	2,154
Current portion of interest-bearing long-term financial liabilities	18, 26 and 28	11,021	2,360	4,560
		94,626	59,518	53,042
Liabilities of discontinued operations	6	—	—	9,113
Total Current Liabilities		94,626	59,518	62,155
Total Liabilities		188,669	148,741	144,219
Total Liabilities and Equity		₱264,004	₱216,891	₱211,088

See accompanying Notes to Consolidated Financial Statements.



MANILA ELECTRIC COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

		Years Ended December 31		
			2012	2011
			(As restated -	(As restated -
	Note	2013	see Note 4)	see Note 4)
(Amounts in millions, except per share data)				
REVENUES				
Sale of electricity	24, 25 and 33	P294,849	P282,991	P253,989
Sale of other services	10 and 24	3,787	2,279	2,819
		298,636	285,270	256,808
COSTS AND EXPENSES				
Purchased power	25 and 31	238,198	232,068	205,674
Salaries, wages and employee benefits	17, 26 and 27	11,258	11,605	10,864
Provision for probable charges and expenses from claims	20	10,749	9,226	8,065
Depreciation and amortization	8, 10 and 11	6,118	5,576	5,504
Contracted services		3,719	2,702	3,333
Provision for doubtful accounts	13	504	832	2,243
Taxes, fees and permits		492	403	399
Other expenses	24 and 26	3,448	3,750	2,887
		274,486	266,162	238,969
OTHER EXPENSES (INCOME)				
Interest and other financial income	26	(1,172)	(2,569)	(2,264)
Interest and other financial charges	8, 18, 19, 22 and 26	1,479	1,528	1,445
Equity in net losses (earnings) of associates and joint ventures	9	259	15	(67)
Derivative mark-to-market loss (gain)		24	(40)	16
Foreign exchange loss (gain)		(353)	4	7
Others	2	(414)	(1,852)	(44)
		(177)	(2,914)	(907)
INCOME BEFORE INCOME TAX FROM CONTINUING OPERATIONS		24,327	22,022	18,746
PROVISION FOR (BENEFIT FROM) INCOME TAX				
	29			
Current		9,889	9,490	8,454
Deferred		(2,835)	(3,749)	(2,501)
		7,054	5,741	5,953
NET INCOME FROM CONTINUING OPERATIONS		17,273	16,281	12,793
INCOME FROM DISCONTINUED OPERATIONS, NET OF INCOME TAX				
	6	—	978	966
NET INCOME		P17,273	P17,259	P13,759
Attributable To				
Equity holders of the Parent	32	P17,211	P17,117	P13,260
Non-controlling interests		62	142	499
		P17,273	P17,259	P13,759



Years Ended December 31				
		2012	2011	
		(As restated - (As restated -		
	Note	2013	see Note 4)	see Note 4)
<i>(Amounts in millions, except per share data)</i>				
Earnings Per Share Attributable to Equity				
Holders of the Parent	32			
Basic		₱15.27	₱15.19	₱11.76
Diluted		15.27	15.19	11.76
Earnings Per Share Attributable to Equity				
Holders of the Parent of Continuing				
Operations	32			
Basic		₱15.27	₱14.40	₱11.31
Diluted		15.27	14.40	11.31

See accompanying Notes to Consolidated Financial Statements.



MANILA ELECTRIC COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

		Years Ended December 31		
		2012	2011	
		(As restated -	(As restated -	
		see Note 4)	see Note 4)	
Note	2013	(Amounts in millions)		
NET INCOME FOR THE YEAR	₱17,273	₱17,259	₱13,759	
OTHER COMPREHENSIVE INCOME				
Items that will be reclassified to profit or loss in subsequent periods:				
Unrealized fair value gain (loss) on available-for-sale financial assets	6 and 11	(21)	39	4
Income tax effect		6	(4)	(1)
		(15)	35	3
Share in cumulative translation adjustment of a subsidiary and associates	9	386	(9)	—
Items that will not be reclassified to profit or loss in subsequent periods:				
Actuarial gain		1,653	2,791	694
Income tax effect		(496)	(837)	(208)
		1,157	1,954	486
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX		1,528	1,980	489
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX		₱18,801	₱19,239	₱14,248
Total Comprehensive Income Attributable To				
Equity holders of the Parent		₱18,739	₱19,097	₱13,749
Non-controlling interests		62	142	499
		₱18,801	₱19,239	₱14,248

See accompanying Notes to Consolidated Financial Statements.



MANILA ELECTRIC COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 31, 2013, 2012 AND 2011

Equity Attributable to Equity Holders of the Parent

	Common Stock (Note 16)	Subscriptions Receivable	Additional Paid-in Capital	Excess of Acquisition Cost Over Carrying Value of Non- controlling Interest Acquired	Employee Stock Purchase Plan (Note 17)	Unrealized Fair Value Gains on Financial Assets (Note 11)	Unrealized Fair Value Gains on Financial Assets of Discontinued Operations (Note 6)	Share in Cumulative Translation Adjustments of a Subsidiary and Associates (Note 9)	Cumulative Actuarial Gains (Losses) (Note 4)	Treasury Shares (Note 16)	Appropriated Retained Earnings (Note 16)	Unappropriated Retained Earnings (Notes 6 and 16)	Equity Attributable to Equity Holders of the Parent	Non- controlling Interests (Note 6)	Total Equity
At January 1, 2013, as previously reported	₱11,273	(₱211)	₱4,111	(₱328)	₱1,049	₱120	₱-	₱3	₱-	(₱11)	₱6,000	₱45,473	₱67,479	₱248	₱67,727
Effect of adoption of PAS 19R	-	-	-	-	-	-	-	-	289	-	-	134	423	-	423
At January 1, 2013, as restated	11,273	(211)	4,111	(328)	1,049	120	-	3	289	(11)	6,000	45,607	67,902	248	68,150
Net income	-	-	-	-	-	(15)	-	386	1,157	-	-	17,211	17,211	62	17,273
Other comprehensive income (loss)	-	-	-	-	-	(15)	-	386	1,157	-	-	-	1,528	-	1,528
Total comprehensive income (loss)	-	-	-	-	-	(15)	-	386	1,157	-	-	17,211	18,739	62	18,801
Collection of subscriptions receivable	-	142	-	-	-	-	-	-	-	-	-	-	142	-	142
Dividends	-	-	-	-	-	-	-	-	-	-	-	(11,621)	(11,621)	(137)	(11,758)
Appropriation of unrestricted retained earnings	-	-	-	-	-	-	-	-	-	-	5,000	(5,000)	-	-	-
At December 31, 2013	₱11,273	(₱69)	₱4,111	(₱328)	₱1,049	₱105	₱-	₱389	₱1,446	(₱11)	₱11,000	₱46,197	₱75,162	₱173	₱75,335

At January 1, 2012, as previously reported	₱11,273	(₱521)	₱4,111	(₱328)	₱915	₱85	₱14	₱12	₱-	(₱9)	₱6,000	₱42,236	₱63,788	₱4,713	₱68,501
Effect of adoption of PAS 19R	-	-	-	-	-	-	-	-	(1,665)	-	-	33	(1,632)	-	(1,632)
As January 1, 2012, as restated	11,273	(521)	4,111	(328)	915	85	14	12	(1,665)	(9)	6,000	42,269	62,156	4,713	66,869
Net income	-	-	-	-	-	35	-	(9)	1,954	-	-	17,117	17,117	142	17,259
Other comprehensive income (loss)	-	-	-	-	-	35	-	(9)	1,954	-	-	-	1,980	-	1,980
Total comprehensive income (loss)	-	-	-	-	-	35	-	(9)	1,954	-	-	17,117	19,097	142	19,239
Collection of subscriptions receivable	-	310	-	-	-	-	-	-	-	-	-	-	310	-	310
Share-based payments	-	-	-	-	134	-	-	-	-	-	-	-	134	-	134
Purchase of treasury shares	-	-	-	-	-	-	-	-	-	(2)	-	-	(2)	-	(2)
Dividends	-	-	-	-	-	-	-	-	-	-	-	(9,129)	(9,129)	(15)	(9,144)
Deconsolidation of subsidiary through property dividend	-	-	-	-	-	-	(14)	-	-	-	-	(4,650)	(4,664)	(4,592)	(9,256)
At December 31, 2012	₱11,273	(₱211)	₱4,111	(₱328)	₱1,049	₱120	₱-	₱3	₱289	(₱11)	₱6,000	₱45,607	₱67,902	₱248	₱68,150

(Forward)



Equity Attributable to Equity Holders of the Parent

	Common Stock (Note 16)	Subscriptions Receivable	Additional Paid-in Capital	Excess of Acquisition Cost Over Carrying Value of Non- controlling Interest Acquired	Employee Stock Purchase Plan (Note 17)	Unrealized Fair Value Gains on Financial Assets (Note 11)	Unrealized Fair Value Gains on Financial Assets (Note 11)	Share in Cumulative Translation Adjustments of a Subsidiary and an Associate (Note 9)	Cumulative Actuarial Gains (Losses) (Note 4)	Treasury shares (Note 16)	Appropriated Retained Earnings (Note 16)	Unappropriated Retained Earnings (Notes 6 and 16)	Equity Attributable to Equity Holders of the Parent	Non- controlling Interests (Note 6)	Total Equity
<i>(Amounts in millions)</i>															
At January 1, 2011, as previously reported	P11,273	(P738)	P4,111	(P328)	P743	P96	P-	P12	P-	P-	P6,000	P37,800	P58,969	P4,227	P63,196
Effect of adoption of PAS 10R	-	-	-	-	-	-	-	-	(2,151)	-	-	-	(2,151)	-	(2,151)
At January 1, 2011, as restated	11,273	(738)	4,111	(328)	743	96	-	12	(2,151)	-	6,000	37,800	56,818	4,227	61,045
Net income	-	-	-	-	-	-	-	-	-	-	-	13,260	13,260	499	13,759
Other comprehensive income	-	-	-	-	-	3	-	-	486	-	-	-	489	-	489
Total comprehensive income	-	-	-	-	-	3	-	-	486	-	-	13,260	13,749	499	14,248
Collection of subscriptions receivable	-	217	-	-	-	-	-	-	-	-	-	-	217	-	217
Share-based payments	-	-	-	-	172	-	-	-	-	-	-	-	172	-	172
Purchase of treasury shares	-	-	-	-	-	-	-	-	-	(9)	-	-	(9)	-	(9)
Dividends	-	-	-	-	-	-	-	-	-	-	-	(8,791)	(8,791)	(13)	(8,804)
Discontinued operations	-	-	-	-	-	(14)	14	-	-	-	-	-	-	-	-
At December 31, 2011	P11,273	(P521)	P4,111	(P328)	P915	P85	P14	P12	(P1,665)	(9)	P6,000	P42,269	P62,156	P4,713	P66,869

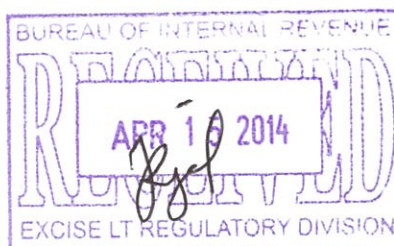
See accompanying Notes to Consolidated Financial Statements.



MANILA ELECTRIC COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

		Years Ended December 31		
	<i>Note</i>	2013	2012	2011
		<i>(Amounts in millions)</i>		
CASH FLOWS FROM OPERATING ACTIVITIES				
Income before income tax of continuing operations		₱24,327	₱22,022	₱18,746
Income before income tax of discontinued operations	6	—	1,061	1,288
Income before income tax		24,327	23,083	20,034
Adjustments for:				
Provision for probable charges and expenses from claims - net	20	10,736	8,948	7,869
Depreciation and amortization	8, 10 and 11	6,118	5,731	5,637
Interest and other financial charges	26	1,479	1,528	1,445
Interest and other financial income	26	(1,172)	(2,569)	(2,264)
Provision for doubtful accounts	13	504	832	2,243
Unrealized foreign exchange gain		(392)	—	—
Equity in net losses (earnings) of associates and joint ventures	9	259	15	(67)
Loss (gain) on disposal of utility plant and others - net		69	(12)	461
Gain on disposal of investment		—	(780)	(24)
Others		—	178	732
Operating income before working capital changes		41,928	36,954	36,066
Decrease (increase) in:				
Trade and other receivables		(20,985)	(2,248)	(5,484)
Inventories		(1,379)	357	323
Land development cost		—	—	(3,331)
Deferred pass-through fuel cost		—	—	1,222
Other current assets		(147)	285	(2,180)
Increase (decrease) in:				
Trade payables and other current liabilities		25,060	4,693	11,346
Customers' refund		(114)	(123)	(881)
Customers' deposits		2,983	2,487	1,967
Long-term employee benefits		(2,997)	1,067	(1,348)
Deposits of pre-selling of condominium units		—	—	(457)
Cash generated from operations		44,349	43,472	37,243
Income tax paid		(7,205)	(7,228)	(5,309)
Net cash flows from operating activities		37,144	36,244	31,934

(Forward)



		Years Ended December 31		
	Note	2013	2012	2011
		(Amounts in millions)		
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to:				
Investments in associates and a joint venture	9 and 15	(P16,383)	(P198)	(P517)
Utility plant and others	8	(9,311)	(9,353)	(8,343)
Short-term investments	15	(4,841)	—	—
Intangible assets	11	(876)	(315)	(209)
Investment properties		—	—	(42)
Interest and other financial income received		1,106	2,174	1,450
Dividends received		411	33	20
Proceeds from disposal of utility plant and others		127	155	107
Proceeds from disposal of investment properties		91	30	65
Decrease (increase) in other noncurrent assets		(716)	(2,075)	653
Net cash used in investing activities		(30,392)	(9,549)	(6,816)
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from:				
Issuances of bonds, net of issue costs	18	18,314	—	—
Availment of notes payable		4,705	1,720	2,150
Collection of subscriptions receivable		142	310	217
Availment of interest-bearing long-term financial liabilities, net of issue costs		—	3,000	11,720
Payments of:				
Dividends		(12,553)	(8,890)	(9,866)
Interest-bearing long-term financial liabilities		(9,424)	(4,565)	(5,620)
Notes payable		(4,678)	—	(2,082)
Interest and other financial charges		(4,036)	(2,882)	(1,960)
Acquisition of non-controlling interest		(27)	—	—
Acquisition of treasury shares		—	(2)	(9)
Decrease in other noncurrent liabilities		156	973	872
Net cash used in financing activities		(7,401)	(10,336)	(4,578)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(649)	16,359	20,540
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		60,500	44,141	24,370
CASH AND CASH EQUIVALENTS OF DISCONTINUED OPERATIONS AT END OF YEAR		—	—	(769)
CASH AND CASH EQUIVALENTS AT END OF YEAR	12	P59,851	P60,500	P44,141

See accompanying Notes to Consolidated Financial Statements.



MANILA ELECTRIC COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Corporate Information

Manila Electric Company or *MERALCO*, holds a congressional franchise under Republic Act or *RA* No. 9209 effective June 28, 2003. *RA* No. 9209 grants *MERALCO* a 25-year franchise valid through June 28, 2028 to construct, operate, and maintain the electric distribution system in the cities and municipalities of Bulacan, Cavite, Metro Manila, and Rizal and certain cities, municipalities, and barangays in the provinces of Batangas, Laguna, Pampanga, and Quezon. On October 20, 2008, the Energy Regulatory Commission or *ERC*, granted *MERALCO* a consolidated Certificate of Public Convenience and Necessity for the operation of electric service within its franchise coverage, effective until the expiration of *MERALCO*'s congressional franchise. *MERALCO* has a unit for its participation in retail electricity supply or *RES*. The *MERALCO* local *RES*, otherwise known as *MPower*, is a business unit within *MERALCO*.

The power segment, primarily power distribution, consists of operations of *MERALCO* and its subsidiary, Clark Electric Distribution Corporation or *CEDC*. *CEDC* is registered with Clark Development Corporation or *CDC*, under *RA* No. 9400, the *Bases Conversion Development Act of 1992*, as a Clark Special Economic Zone or *CSEZ*, enterprise, primarily engaged in the operation, and maintenance of a power distribution system within *CSEZ*.

MERALCO has a minority equity interest in a power generating company, Global Business Power Corporation or *GBPC*, and is developing power generation plants through its wholly owned subsidiary, *MERALCO* PowerGen Corporation or *MGen*. Through several subsidiaries in the service segment, it provides engineering, design, construction and consulting services, bill collection services, distribution and energy management services and information systems and technology services.

MERALCO's investment in common equity shares of Rockwell Land Corporation or *Rockwell Land*, was declared as property dividends on February 27, 2012 to stockholders of record as at March 23, 2012. On April 25, 2012, the Securities and Exchange Commission or *SEC*, approved the property dividend declaration. Consequently, *MERALCO* distributed the *Rockwell Land* shares on May 11, 2012. The details of the declaration are in *Note 6 – Discontinued Operations*. *MERALCO* and its subsidiaries are collectively referred to as the *MERALCO Group*.

The single largest shareholder of *MERALCO* as at December 31, 2013 is Beacon Electric Asset Holdings, Inc. or *Beacon Electric*, which owns 49.96% of the common shares. *Beacon Electric* is jointly owned by Metro Pacific Investments Corporation or *Metro Pacific*, and PLDT Communications and Energy Ventures, Inc., or *PCEV*, both of which are domestic corporations and are affiliates of First Pacific Company Limited or *First Pacific*, a Hong Kong-based investment and management company. In December 2013, JG Summit Holdings, Inc. or *JG Summit*, completed the purchase of the remaining 27.12% equity interest of San Miguel Corporation or *SMC*, San Miguel Pure Foods Company, Inc. and San Miguel Global Power Holdings Corp. in *MERALCO*. In July 2013, *SMC* sold its 5.71%-interest in *MERALCO* through the market. First Philippine Holdings Corporation or *First Holdings*, and First Philippine Utilities Corporation, collectively own 3.95%. The balance of *MERALCO*'s common shares is held by the public.

The common shares of *MERALCO* are listed on and traded in the Philippine Stock Exchange or *PSE*, with security symbol, *MER*.



The registered office address of *MERALCO* is Lopez Building, Ortigas Avenue, Pasig City, Philippines.

The accompanying consolidated financial statements as at December 31, 2013 and 2012 and for each of the three years in the period ended December 31, 2013, were reviewed and recommended for approval by the Audit and Risk Management Committee to the Board of Directors or *BOD* on March 17, 2014. On the same date, these consolidated financial statements were approved and authorized for issue by the *BOD*.

2. Rate Regulations

As distribution utilities or *DUs*, *MERALCO* and *CEDC* are subject to the rate-making regulations and regulatory policies of the *ERC*. Billings of *MERALCO* and *CEDC* to customers are itemized or “unbundled” into a number of bill components that reflect the various activities and costs incurred in providing electric service. The adjustment to each bill component is governed by mechanisms promulgated and enforced by the *ERC*, mainly: [i] the “Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities”, which govern the recovery of pass-through costs, including over- or under-recoveries of the bill components, namely, (a) generation charge, (b) transmission charge, (c) system loss or *SL*, charge, (d) lifeline subsidy, and (e) local franchise tax or *LFT*, and (f) business tax; and [ii] the “Rules for the Setting of Distribution Wheeling Rates” or *RDWR*, as modified by *ERC* Resolution No. 20, Series of 2008, which govern the determination of *MERALCO*’s distribution, supply, and metering charges.

The rate-setting mechanism of *CEDC* is likewise in accordance with the *ERC* regulations. The following is a discussion of matters related to rate-setting of *MERALCO* and *CEDC*:

Rate Application

CEDC Rate Unbundling

On August 19, 2011, *CEDC* received an *ERC* Order to implement certain revisions of its schedule of rates effective on its August 2010 billing cycle, after the *ERC* approved *CEDC*’s unbundling application pursuant to Section 36 of *RA* No. 9136, *Electric Power Industry Reform Act of 2001* or *EPIRA*.

Thereafter, on June 21, 2012, *CEDC* received an Order from the *ERC* (docketed on May 28, 2012) directing *CEDC* to refund to its customers the amount of ₱0.8 million (the difference between its then existing rates and the rates approved by the *ERC*) at a rate equivalent to ₱0.0067 per kilowatt hour or *kWh*, for a period of five (5) months or until the said amount shall have been fully refunded. The refund process was completed by *CEDC* in October 2012.

Performance-Based Regulations or PBR

MERALCO

MERALCO was among the Group A entrants to the *PBR*, together with two other private *DUs*.

Rate-setting under *PBR* is governed by the *RDWR*. The *PBR* scheme sets tariffs based on the regulated asset base of the *DUs*, and the required operating and capital expenditures once every regulatory period or *RP*, to meet operational performance and service level requirements responsive to the needs for adequate, reliable and quality power, efficient service, and growth of



all customer classes in the franchise area as approved by the *ERC*. *PBR* also employs a mechanism that penalizes or rewards a *DU* depending on its network and service performance.

Rate filings and settings are done on an *RP* basis. One (1) *RP* consists of four (4) Regulatory Years or *RYs*. An *RY* for *MERALCO* begins on July 1 and ends on June 30 of the following year. As at December 31, 2013, *MERALCO* is operating in the first half of the third *RY* of the third *RP*. The third *RP* is from July 1, 2011 to June 30, 2015.

Maximum Average Price or MAP for RY 2008 and RY 2009

On January 11 and April 1, 2008, *MERALCO* filed separate applications for the approval of its proposed translation of the *MAP* for *RY 2008* and *RY 2009*, respectively, into different rate schedules for its various customer segments. A portion of the distribution charge under-recoveries as a result of the delayed implementation of the *PBR* was incorporated in the proposed *MAP* for *RY 2009*.

In April 2009, the *ERC* approved the implementation of *MERALCO*'s average distribution rate of ₱1.2227 per kilowatt-hour or *kWh* effective billing period of May 2009. This rate is inclusive of the under-recoveries for calendar year 2007 of ₱0.1285 per *kWh*.

On May 28, 2009, certain electricity consumer groups filed a Petition with the Court of Appeals, or *CA*, questioning the decision and Order of the *ERC* on *MERALCO*'s rate translation application for *RY 2008* and *RY 2009*. In a decision dated January 27, 2010, the *CA* denied the Petition. Consequently, the consumer groups brought the case to the Supreme Court of the Philippines or *SC*. Comments and responses were filed by both parties with a Manifestation filed by *MERALCO* on January 26, 2011. As at March 17, 2014, the *SC* has yet to render its decision on this case.

MAP for RY 2012

On June 21, 2011, *MERALCO* filed an application for the approval of its *MAP* for *RY 2012* and translation into rate tariffs by customer category. On October 6, 2011, the *ERC* provisionally approved the *MAP* for *RY 2012* of ₱1.6012 per *kWh* and the rate translation per customer class was reflected commencing with the October 2011 customer bills. Hearings for the final approval of the application have been completed and all parties have submitted their respective memoranda. As at March 17, 2014, the application is pending final approval by the *ERC*.

MAP for RY 2013

On June 11, 2012, the *ERC* provisionally approved the *MAP* for *RY 2013* of ₱1.6303 per *kWh* which was reflected starting with the July 2012 customer bills. Hearings on this case have been completed and *MERALCO* is awaiting the final decision of the *ERC*.

MAP for RY 2014

On April 1, 2013, *MERALCO* filed its application for the approval of its *MAP* for *RY 2014* of ₱1.6510 per *kWh* and the translation thereof into rate tariffs by customer category. Hearing was completed on May 9, 2013. *MERALCO* filed its Formal Offer of Evidence or *FOE* on May 10, 2013. On June 10, 2013, the *ERC* provisionally approved the *MAP* for *RY 2014* of ₱1.6474 per *kWh* and the rate translation per customer class. As at March 17, 2014, the application is pending final approval by the *ERC*.



CEDC

CEDC was among the four (4) Group D entrants to the *PBR*. Similar to *MERALCO*, it is subject to operational performance and service level requirements approved by the *ERC*. The *RP* of *CEDC* began on October 1, 2011 and ends on September 30, 2015.

Reset Application and MAP for RY 2012

In compliance with the *ERC*'s *PBR* rate setting mechanism, *CEDC* filed a reset application for the approval of its *ARR* and *PIS* with the *ERC*. *CEDC* filed its revised application on November 3, 2010, which underwent a series of hearings and public consultations in 2011. The *ERC* issued *CEDC*'s Final Determination on August 5, 2011. Subsequently, *CEDC* filed with the *ERC* its application for *RY 2012* Rate Translation into the different customer classes.

On April 10, 2012, the *ERC* approved with modification, *CEDC*'s application for the approval of the translation into distribution rates of different customer classes for the first *RY* of the approved *ARR* under the *PBR* for the *RP* October 1, 2011 to September 30, 2015. *CEDC* implemented the approved distribution, supply and metering charges of ₱0.8527 per *kWh* and the new customer segments in its June 2012 billing.

MAP for RY 2013

On August 30, 2012, *CEDC* filed its application for the approval of its *MAP* for *RY 2013*. The *ERC*, on December 17, 2012, approved a *MAP* of ₱0.8953 per *kWh*. The revised rates based on the approved *MAP 2013* were implemented by *CEDC* starting January 2013.

SC Decision on Unbundling Rate Case

On May 30, 2003, the *ERC* issued an Order approving *MERALCO*'s unbundled tariffs that resulted in a total increase of ₱0.17 per *kWh* over the May 2003 tariff levels. However, on August 4, 2003, certain consumer and civil society groups filed a Petition for Review of the *ERC*'s ruling with the *CA*. On July 22, 2004, the *CA* set aside the *ERC*'s ruling on *MERALCO*'s rate unbundling and remanded the case to the *ERC*. Further, the *CA* opined that the *ERC* should have asked the Commission on Audit or *COA*, to audit the books of *MERALCO*. The *ERC* and *MERALCO* subsequently filed separate motions asking the *CA* to reconsider its decision. On January 24, 2005, as a result of the denial by the *CA* of the motions, the *ERC* and *MERALCO* elevated the case to the *SC*.

In an En Banc decision promulgated on December 6, 2006, the *SC* set aside and reversed the *CA* ruling saying that a *COA* audit was not a prerequisite in the determination of a utility's rates. However, while the *SC* affirmed *ERC*'s authority in rate-fixing, the *SC* directed the *ERC* to request *COA* to undertake a complete audit of the books, records and accounts of *MERALCO*. On January 15, 2007, in compliance with the directive of the *SC*, the *ERC* requested *COA* to conduct an audit of the books, records and accounts of *MERALCO* using calendar years 2004 and 2007 as test years.

The *COA* audit, which began in September 2008, was completed in August 2009.

On February 17, 2010, the *ERC* issued its Order directing *MERALCO* and all intervenors in the case to submit, within 15 days from receipt of the Order, their respective comments on the *COA*'s "Report No. 2009-01 Rate Audit Unbundled Charges."



On July 1, 2011, the *ERC* maintained and affirmed its findings and conclusions in its Order dated March 20, 2003. The *ERC* stated that the *COA* recommendation to apply disallowances under *PBR* to rate unbundling violates the principle against retroactive rate-making. An intervenor group filed a motion for reconsideration of the said Order. On September 5, 2011, *MERALCO* filed its comment to the intervenor's motion for reconsideration. On February 4, 2013, the *ERC* denied the intervenor's motion for reconsideration. The intervenor filed a petition for review before the *CA*. *MERALCO* is awaiting further action of the *CA* on this matter.

Applications for the Recovery of Generation Costs and SL Charges

MERALCO filed separate applications for the full recovery of generation costs, including value-added tax or *VAT*, incurred for the supply months of August 2006 to May 2007 or total under-recoveries of ₱12,679 million for generation charges and ₱1,295 million for *SL* charges.

The separate applications for the full recovery of generation charges have been approved by the *ERC* in its decisions released on January 18, 2008, September 3, 2008 and August 16, 2010.

As at December 31, 2013, the remaining balance of ₱137 million of such unrecovered generation costs will be billed subsequent to December 2013 at the rate of ₱0.0314 per *kWh* until fully recovered. The amount is recoverable within 12 months and included in the "Trade and other receivables" account.

With respect to the ₱1,295 million *SL* charge under-recoveries, the *ERC* ordered *MERALCO* to file a separate application for the recovery of *SL* adjustments after the *ERC* confirms the transmission rate to be used in the calculation of the *SL* rate in accordance with the *SL* rate formula of the Automatic Generation Rate Adjustments Guidelines or *AGRA*. *MERALCO* has filed the application for recovery of the ₱1,295 million *SL* charge under-recoveries with the *ERC*. This was included in the Consolidated Application of over- or under- recoveries in generation, transmission, *SL* and lifeline subsidies filed on March 31, 2011 with the *ERC*. Hearings were completed on October 25, 2011. On December 12, 2011, *MERALCO* filed for the admission of its Supplemental Application. An expository hearing was conducted on February 1, 2012. As at March 17, 2014, *MERALCO* has already filed its *FOE* and is awaiting the final resolution by the *ERC*.

Inter-Class Cross Subsidies and Lifeline Subsidies

MERALCO filed separate applications to recover inter-class cross subsidies (on November 14, 2007) and lifeline subsidies (on February 19, 2008).

In a decision dated November 16, 2009, the *ERC* authorized *MERALCO* to recover the inter-class cross subsidy under-recoveries covering the period June 2003 to October 2006 amounting to ₱1,049 million and total lifeline subsidy under-recoveries covering the period June 2003 to December 2007 amounting to ₱856 million.

In December 2009, *MERALCO* implemented the decisions of the *ERC* on the inter-class cross and lifeline subsidies. The balances of inter-class cross subsidies and lifeline subsidies were fully recovered in April 2013 and December 2013, respectively.

Consolidated Applications for the Confirmation of Over/Under-recoveries of Pass-through Charges

On August 12, 2009, the *ERC* issued Resolution No. 16, Series of 2009, adopting the "Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding



Confirmation Process for Distribution Utilities.” These rules govern the recovery of pass-through costs, including over- or under-recoveries with respect to the following bill components: generation charge, transmission charge, *SL* charge, lifeline and interclass rate subsidies, *LFT* and business tax. On October 18, 2010, the *ERC* promulgated *ERC* Resolution No. 21, Series of 2010, amending certain formula contained in *ERC* Resolution No. 16, Series of 2009, and setting March 31, 2011 (covering adjustments implemented until the billing month of December 2010) and March 31, 2014 (covering adjustments from January 2011 to December 2013) as the new deadlines for *DUs* in Luzon to file their respective applications. Subsequent filings shall be made every three (3) years thereafter.

On March 31, 2011, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries accumulated from June 2003 to December 2010 in compliance with Resolution No. 16, Series of 2009, as subsequently amended by Resolution No. 21, Series of 2010. Hearings were completed on October 25, 2011. On December 8, 2011, *MERALCO* filed an Omnibus Motion praying for, among other things, the admission of the Supplemental Application. In an Order dated December 12, 2011, the *ERC* granted *MERALCO*’s Omnibus Motion and admitted its Supplemental Application. Accordingly, hearings for the Supplemental Application were conducted where *MERALCO* presented additional evidence. *MERALCO* filed its *FOE* on September 13, 2012. The consolidated filing includes net generation charge under-recoveries of ₱1,000 million, net transmission charge over-recoveries of ₱111 million, net lifeline subsidy under-recoveries of ₱9 million and net *SL* over-recoveries of ₱425 million, excluding any applicable carrying charges.

On July 6, 2012, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries for the calendar year 2011. The consolidated filing includes net generation charge under-recoveries of ₱1,826 million, transmission charge under-recoveries of ₱253 million, net lifeline subsidy under-recoveries of ₱39 million and *SL* over-recoveries of ₱445 million, excluding any applicable carrying charges. Hearings on the application have been completed and *MERALCO* has submitted its *FOE* on January 25, 2013. As at March 17, 2014, the application is pending approval by the *ERC*.

Deferred PPA

On October 14, 2009, the *ERC* released its findings on *MERALCO*’s implementation of the collection of the approved pass-through cost under-recoveries in 2004. *ERC* directed *MERALCO* to refund ₱268 million of deferred *PPA* transmission line costs related to Quezon Power (Philippines) Limited Company or *QPPL* and deferred accounting adjustments or *DAA* incurred to customers, along with ₱184 million in carrying charges, or an equivalent of ₱0.0169 per *kWh*. *MERALCO* implemented the refund beginning November 2009 until September 2010. However, the *ERC* has yet to rule on *MERALCO*’s deferred *PPA* under-recoveries of ₱106 million, which does not represent the transmission line fee. As at March 17, 2014, *MERALCO* has filed a Motion for Reconsideration, which is pending decision by the *ERC*.

Application for Recovery of LFT

On March 25, 2011, *MERALCO* filed with the *ERC* an application for recovery of *LFT* paid but not yet billed to customers for the period beginning first quarter of 1993 up to the second quarter of 2004 for five (5) provinces, namely: Bulacan, Batangas, Cavite, Laguna and Rizal; and 14 cities, namely: San Jose Del Monte, Batangas, San Pablo, Tagaytay, Lucena, Mandaluyong, Marikina, Quezon, Caloocan, Pasay, Las Piñas, Manila, Pasig and Calamba. The *LFT* is recognized as a valid and reasonable *DU* expense in the *ERC*’s unbundling decision.



In a Decision dated February 27, 2012, the *ERC* released its Order approving with modifications *MERALCO*'s application. The *ERC* approved recovery of *LFT* amounting to ₱1,571 million plus carrying charges of ₱730 million. As directed by the *ERC*, the recovery was reflected as a separate item in the *MERALCO* billing statement to its customers beginning April 2012. As at December 31, 2013, a total of ₱856 million *LFT* and carrying charges have been billed to affected customers. The amount recoverable within 12 months is included in the "Trade and other receivables" account while the long-term portion is included in the "Other noncurrent assets" account.

SC Decision on the ₱0.167 per kWh Refund

Following the *SC*'s final ruling that directed *MERALCO* to refund affected customers ₱0.167 per *kWh* for billings made from February 1994 to April 2003, the *ERC* approved the release of the refund in four phases. The refund is still ongoing.

See *Note 21 – Customers' Refund*.

3. Basis of Preparation and Statement of Compliance

The accompanying consolidated financial statements have been prepared on a historical cost basis, except for *MERALCO*'s utility plant and others and investment properties acquired before January 1, 2004, which are carried at deemed cost, and for derivative financial instruments and available-for-sale, or *AFS*, financial assets, which are measured at fair value. Derivative financial instruments are shown as part of "Other current assets" or "Trade payables and other current liabilities" accounts, as applicable, in the consolidated statement of financial position. *AFS* financial assets are included as part of "Other noncurrent assets" account in the consolidated statement of financial position.

The consolidated financial statements provide comparative information in respect of the previous year. In addition, the *MERALCO Group* presents an additional consolidated statement of financial position at the beginning of the earliest year presented when there is a retrospective application of an accounting policy, a retrospective restatement, or a reclassification of items in the consolidated financial statements. An additional consolidated statement of financial position as at January 1, 2012 is presented in these consolidated financial statements due to retrospective application of certain accounting policies.

See *Note 4 – Significant Accounting Policies, Changes and Improvements*.

All values are rounded to the nearest million peso, except when otherwise indicated.

Statement of Compliance

The consolidated financial statements of *MERALCO* and its subsidiaries have been prepared in compliance with Philippine Financial Reporting Standards or *PFRS*.



Basis of Consolidation

The consolidated financial statements comprise the financial statements of *MERALCO* and the following directly and indirectly-owned subsidiaries as at December 31 of each year.

Subsidiaries	Place of Incorporation	Principal Business Activity	2013		2012	
			Percentage of Ownership			
			Direct	Indirect	Direct	Indirect
Corporate Information Solutions, Inc., or <i>CIS</i>	Philippines	e-Transactions	100	—	100	—
<i>CIS Bayad Center, Inc., or Bayad Center</i>	Philippines	Bills payment collection	—	100	—	100
<i>Customer Frontline Solutions, Inc. or CFSI</i>	Philippines	Teller services	—	100	—	100
Meralco Energy, Inc., or <i>MEI</i>	Philippines	Energy systems management	100	—	100	—
eMERALCO Ventures, Inc., or <i>e-MVT</i>	Philippines	e-Business development	100	—	100	—
<i>Paragon Vertical Corporation</i>	Philippines	Information technology and multi-media services	—	100	—	100
<i>MGen</i>	Philippines	Development of power generation plants	100	—	100	—
<i>Calamba Aero Power Corporation¹</i>	Philippines	Power generation	—	100	—	100
<i>Atimonan Land Ventures Development Corporation</i>	Philippines	Real estate	—	100	—	100
<i>Luzon Natural Gas Energy Corporation²</i>	Philippines	Power generation	—	100	—	—
<i>MPG Asia Limited</i>	British Virgin Island	Holding company	—	100	—	—
Meralco Financial Services Corporation or <i>Finserve</i>	Philippines	Financial services provider	100	—	100	—
Republic Surety and Insurance Company, Inc. or <i>RSIC</i>	Philippines	Insurance	100	—	100	—
Lighthouse Overseas Insurance Limited or <i>LOIL</i>	Bermuda	Insurance	100	—	100	—
<i>MIESCOR</i>	Philippines	Engineering, construction and consulting services	99	—	99	—
<i>MIESCOR Builders Inc. or MBI</i>	Philippines	Electric transmission and distribution operation and maintenance services	—	100	—	100
<i>MIESCOR Logistics Inc. or MLI</i>	Philippines	General services, manpower/maintenance	—	100	—	100
<i>Miescorrail, Inc. or Miescorrail³</i>	Philippines	Engineering, construction and maintenance of mass transit system	100	—	—	100
<i>CEDC</i>	Philippines	Power distribution	65	—	65	—

¹ Incorporated February 15, 2011 and has not started commercial operations as at December 31, 2013.

² Incorporated January 11, 2013 and has not started commercial operations as at December 31, 2013.

³ On December 26, 2013, MIESCOR assigned its entire shareholdings in Miescorrail to MERALCO.

Control is achieved when the *MERALCO Group* is exposed, or has the right, to variable returns from its involvement with the investee. Specifically, the *MERALCO Group* controls an investee if and only if the *MERALCO Group* has (a) power over the investee; (b) exposure, or rights, to variable returns from its involvement with the investee, and; (c) the ability to use its power over the investee to affect its returns.

When the *MERALCO Group* has less than a majority of the voting or similar rights of an investee, it considers all relevant facts and circumstances in assessing whether it has power over an investee, including (a) the contractual arrangement with the other vote holders of the investee; (b) rights arising from other contractual arrangements (c) *MERALCO Group's* voting rights and potential voting rights.

The *MERALCO Group* re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the *MERALCO Group* obtains control over the



subsidiary and ceases when it loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the date it gains control until the date it ceases to control the subsidiary.

The consolidated financial statements are prepared using uniform accounting policies for like transactions and other events with similar circumstances. All intra-group balances, income and expenses, unrealized gains and losses and dividends resulting from intra-group transactions are eliminated in full.

Non-controlling interests represent the portion of profit or loss and net assets in *CEDC* and *MIESCOR* and its subsidiaries not held by *MERALCO* and are presented separately in the consolidated statement of income, consolidated statement of comprehensive income and within equity in the consolidated statement of financial position, separately from equity attributable to equity holders of the parent.

Total comprehensive income within a subsidiary is attributed to the non-controlling interest even if such results in a deficit.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction.

If the *MERALCO Group* loses control over a subsidiary, it: (a) derecognizes the assets (including goodwill) and liabilities of the subsidiary; (b) derecognizes the carrying amount of any non-controlling interest; (c) derecognizes the cumulative translation adjustments deferred in equity; (d) recognizes the fair value of the consideration received; (e) recognizes the fair value of any investment retained; (f) recognizes any surplus or deficit in profit or loss; and (g) reclassifies *MERALCO*'s share of components previously recognized in the consolidated statement of comprehensive income to the consolidated statement of income.

4. Significant Accounting Policies, Changes and Improvements

Changes in Accounting Policies and Disclosures

The accounting policies adopted in the preparation of consolidated financial statements are consistent with those of the previous financial year except for the adoption of the following amendments and improvements to existing standards, which were effective beginning January 1, 2013.

PAS 1, Presentation of Financial Statements – Presentation of Items of Other Comprehensive Income or OCI

The amendments to *PAS 1* change the grouping of items presented in *OCI*. Items that can be reclassified (or “recycled”) to profit or loss at a future point in time (for example, upon derecognition or settlement) will be presented separately from items that will never be recycled. The amendments are applicable to the *MERALCO Group*. However, the adoption did not have significant effect on the consolidated financial statements. The amendments affected the presentation in the consolidated statement of comprehensive income only and had no impact on the *MERALCO Group*'s financial position or performance.



PAS 19, Employee Benefits (Amendments)

For defined benefit plans, the Revised *PAS 19* requires all actuarial gains and losses to be recognized in other comprehensive income and unvested past service costs previously recognized over the average vesting period to be recognized immediately in profit or loss when incurred.

Prior to adoption of the Revised *PAS 19*, the *MERALCO Group* recognized actuarial gains and losses as income or expense when the net cumulative unrecognized gains and losses for each individual plan at the end of the previous period exceeded 10% of the higher of the defined benefit obligation and the fair value of the plan assets, and recognized unvested past service costs as an expense on a straight-line basis over the average vesting period until the benefits become vested. Upon adoption of the Revised *PAS 19*, the *MERALCO Group* changed its accounting policy to recognize all actuarial gains and losses in other comprehensive income and all past service costs in profit or loss in the period they occur.

The Revised *PAS 19* replaced the interest cost and expected return on plan assets with the concept of net interest on defined benefit liability or asset, which is calculated by multiplying the net balance sheet defined benefit liability or asset by the discount rate used to measure the employee benefit obligation, each as at the beginning of the annual period.

The Revised *PAS 19* also amended the definition of short-term employee benefits and requires employee benefits to be classified as short-term based on expected timing of settlement rather than the employee's entitlement to the benefits. In addition, the Revised *PAS 19* modifies the timing of recognition for termination benefits. The modification requires the termination benefits to be recognized at the earlier of when the offer cannot be withdrawn or when the related restructuring costs are recognized.

The *MERALCO Group* reviewed its existing employee benefits and determined that the amended standard has significant impact on its accounting for retirement benefits. The *MERALCO Group* obtained the services of an independent actuary to compute the impact on the consolidated financial statements. The effects are detailed below:

	As at December 31, 2013	As at December 31, 2012	As at January 1, 2012
<i>(Amounts in millions)</i>			
<u>Consolidated statements of</u>			
<u>financial position</u>			
Increase (decrease) in:			
Net defined benefit liability	(P2,294)	(P605)	P2,332
Deferred tax assets	(688)	(182)	700
Other comprehensive income	1,446	289	(1,665)
Retained earnings	160	134	33



	Years ended December 31		
	2013	2012	2011
	<i>(Amounts in millions, except per share data)</i>		
<u>Consolidated statements of income</u>			
Increase (decrease) in:			
Net benefit cost	(P37)	(P145)	(P47)
Provision for income tax	11	44	14
Profit for the year attributable to:			
Equity holders of the			
Parent	26	101	33
Non-controlling interests	—	—	—
Earnings per share - basic and diluted	P0.02	P0.09	P0.03
<u>Consolidated statements of comprehensive income</u>			
Increase in other comprehensive income	P1,157	P1,954	P486

The adoption of the Revised *PAS 19* had no impact on the consolidated statements of cash flows.

Philippine Interpretation IFRIC 20, Stripping Costs in the Production Phase of a Surface Mine

This interpretation applies to waste removal (stripping) costs incurred in surface mining activity, during the production phase of the mine. The interpretation addresses the accounting for the benefit from the stripping activity. This new interpretation is not applicable to the *MERALCO Group*.

PFRS 7, Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities

These amendments require an entity to disclose information about rights of set-off and related arrangements (such as collateral agreements). The new disclosures are required for all recognized financial instruments that are set off in accordance with *PAS 32, Financial Instruments: Presentation*. These disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or ‘similar agreement’, irrespective of whether they are set off in accordance with *PAS 32*. The amendments require entities to disclose, in a tabular format unless another format is more appropriate, the following minimum quantitative information. These are presented separately for financial assets and financial liabilities recognized at the end of the reporting period:

- a) The gross amounts of those recognized financial assets and recognized financial liabilities;
- b) The amounts that are set off in accordance with the criteria in *PAS 32* when determining the net amounts presented in the statement of financial position;
- c) The net amounts presented in the statement of financial position;



- d) The amounts subject to an enforceable master netting arrangement or similar agreement that are not otherwise included in (b) above, including:
 - i. Amounts related to recognized financial instruments that do not meet some or all of the offsetting criteria in *PAS 32*; and
 - ii. Amounts related to financial collateral (including cash collateral); and
- e) The net amount after deducting the amounts in (d) from the amounts in (c) above.

The amendments are applicable to the *MERALCO Group* and based on the evaluation, the amendments have no impact on its financial position or performance.

PFRS 10, Consolidated Financial Statements

PFRS 10 replaces the portion of *PAS 27, Consolidated and Separate Financial Statements*, that addresses the accounting for consolidated financial statements. It also includes the issues raised in Standing Interpretations Committee or *SIC 12, Consolidation - Special Purpose Entities*. *PFRS 10* establishes a single control model that applies to all entities including special purpose entities. The changes introduced by *PFRS 10* will require management to exercise significant judgment to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in *PAS 27*. A reassessment of control was performed by *MERALCO* on all its subsidiaries and associates in accordance with the provisions of *PFRS 10*. Based on the reassessment made, *MERALCO* has not determined any change in the control or significant influence in any of its subsidiaries and associates.

PFRS 11, Joint Arrangements

PFRS 11 replaces *PAS 31, Interests in Joint Ventures*, and *SIC 13, Jointly Controlled Entities - Non-Monetary Contributions by Venturers*. *PFRS 11* removes the option to account for jointly controlled entities using proportionate consolidation. Instead, jointly controlled entities that meet the definition of a joint venture must be accounted for using the equity method. The standard is applicable to the *MERALCO Group* and based on its evaluation, the application of this new standard has no impact on its consolidated financial statements.

PFRS 12, Disclosure of Interests in Other Entities

PFRS 12 includes all of the disclosures related to consolidated financial statements that were previously in *PAS 27*, as well as all the disclosures that were previously included in *PAS 31* and *PAS 28, Investments in Associates*. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. The standard is applicable to the *MERALCO Group* and based on the evaluation, the standard has no impact on its financial position or performance but affects disclosures only.

PFRS 13, Fair Value Measurement

PFRS 13 establishes a single source of guidance under *PFRS* for all fair value measurements. *PFRS 13* does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under *PFRS* when fair value is required or permitted. The standard is applicable to the *MERALCO Group* and based on its evaluation, the standard has no impact on the *MERALCO Group's* financial position or performance but affects disclosures only.



PAS 27, Separate Financial Statements (as revised in 2011)

As a consequence of the issuance of the new *PFRS 10* and *PFRS 12*, what remains of *PAS 27* is limited to accounting for subsidiaries, jointly controlled entities, and associates in the separate financial statements. The standard is applicable to the *MERALCO Group* and based on its evaluation, the application of this new standard has no impact on its consolidated financial statements.

PAS 28, Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the issuance of the new *PFRS 11* and *PFRS 12*, *PAS 28* has been renamed *PAS 28, Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. The standard is applicable to the *MERALCO Group* and based on its evaluation, the application of this new standard has no impact on its consolidated financial statements.

Annual Improvements to PFRS (2009-2011 cycle)

The *Annual Improvements to PFRS (2009-2011 cycle)* contain non-urgent but necessary amendments to *PFRS*. The amendments are effective for annual periods beginning on or after January 1, 2013 and to be applied retrospectively.

PFRS 1, First-time Adoption of PFRS – Borrowing Costs

The amendment clarifies that, upon adoption of *PFRS*, an entity that capitalized borrowing costs in accordance with its previous generally accepted accounting principles, may carry forward, without any adjustment, the amount previously capitalized in its opening statement of financial position at the date of transition. Subsequent to the adoption of *PFRS*, borrowing costs are recognized in accordance with *PAS 23, Borrowing Costs*. The amendment does not apply to the *MERALCO Group* as it is not a first-time adopter of *PFRS*.

PAS 1, Presentation of Financial Statements - Clarification of the Requirements for Comparative Information

The amendment clarifies the requirements for comparative information that are disclosed voluntarily and those that are mandatory due to retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The additional comparative period does not need to contain a complete set of financial statements. On the other hand, supporting notes for the third balance sheet (mandatory when there is a retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements) are not required. The amendments affect disclosures only and have no impact on the *MERALCO Group's* financial position or performance.

PAS 16, Property, Plant and Equipment - Classification of Servicing Equipment

The amendment clarifies that spare parts, stand-by equipment and servicing equipment should be recognized as property, plant and equipment when they meet the definition of property, plant and equipment and should be recognized as inventory if otherwise. The amendment has no impact on the *MERALCO Group's* financial position or performance.



PAS 32, Financial Instruments: Presentation - Tax Effect of Distribution to Holders of Equity Instruments

The amendment clarifies that income taxes relating to distributions to equity holders and to transaction costs of an equity transaction are accounted for in accordance with *PAS 12, Income Taxes*. The amendment has no impact on the *MERALCO Group's* financial position or performance.

PAS 34, Interim Financial Reporting - Interim Financial Reporting and Segment Information for Total Assets and Liabilities

The amendment clarifies that the total assets and liabilities for a particular reportable segment need to be disclosed only when the amounts are regularly provided to the chief operating decision maker and there has been a material change from the amount disclosed in the entity's previous annual financial statements for that reportable segment. The amendment has no impact on the *MERALCO Group's* financial position or performance.

New Accounting Standards, Interpretations and Amendments to Existing Standards Effective Subsequent to December 31, 2013

The *MERALCO Group* will adopt the following new standards, interpretations and amendments to existing standards enumerated below when these become effective. Except as otherwise indicated, the *MERALCO Group* does not expect the adoption of these revised standards and amendments to *PFRS* to have a significant impact on the *MERALCO Group's* consolidated financial statements.

Effective 2014

PAS 36, Impairment of Assets - Recoverable Amount Disclosures for Non-Financial Assets (Amendments)

These amendments remove the unintended consequences of *PFRS 13* on the disclosures required under *PAS 36*. In addition, these amendments require disclosure of the recoverable amounts for the assets or cash-generating units for which impairment loss has been recognized or reversed during the period. These amendments are effective retrospectively for annual periods beginning on or after January 1, 2014 with earlier application permitted, provided *PFRS 13* is also applied. The amendments affect disclosures only and will have no impact on the *MERALCO Group's* financial position or performance.

Investment Entities (Amendments to PFRS 10, PFRS 12 and PAS 27)

These amendments provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under *PFRS 10*. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. It is not expected that this amendment would be relevant to the *MERALCO Group* since none of the entities in the *MERALCO Group* would qualify to be an investment entity under *PFRS 10*.

Philippine Interpretation IFRIC 21, Levies (IFRIC 21)

IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated



before the specified minimum threshold is reached. The *MERALCO Group* does not expect that *IFRIC 21* will have material financial impact in future financial statements.

PAS 39, Financial Instruments: Recognition and Measurement - Novation of Derivatives and Continuation of Hedge Accounting (Amendments)

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. The *MERALCO Group* has not novated its derivatives during the current period. However, these amendments would be considered for future any novations.

PAS 32, Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities

The amendments clarify the meaning of “currently has a legally enforceable right to set-off” and also clarify the application of the *PAS 32* offsetting criteria to settlement systems (such as central clearing house systems), which apply gross settlement mechanisms that are not simultaneous. The amendments affect presentation only and have no impact on the *MERALCO Group*’s financial position or performance. The amendments to *PAS 32* are to be applied retrospectively for annual periods beginning on or after January 1, 2014.

Effective 2015

PAS 19, Employee Benefits – Defined Benefit Plans: Employee Contributions (Amendments)

The amendments apply to contributions from employees or third parties to defined benefit plans. Contributions that are set out in the formal terms of the plan shall be accounted for as reductions to current service costs if they are linked to service or as part of the remeasurements of the net defined benefit asset or liability if they are not linked to service. Contributions that are discretionary shall be accounted for as reductions of current service cost upon payment of these contributions to the plans. The amendments to *PAS 19* are to be retrospectively applied for annual periods beginning on or after July 1, 2014.

Annual Improvements to PFRSs (2010-2012 cycle)

The *Annual Improvements to PFRS (2010-2012 cycle)* contain non-urgent but necessary amendments to the following standards:

PFRS 2, Share-based Payment – Definition of Vesting Condition

The amendment revised the definitions of vesting condition and market condition and added the definitions of performance condition and service condition to clarify various issues. This amendment shall be prospectively applied to share-based payment transactions for which the grant date is on or after July 1, 2014. This amendment does not apply to the *MERALCO Group* as it has no share-based payments.

PFRS 3, Business Combinations – Accounting for Contingent Consideration in a Business Combination

The amendment clarifies that a contingent consideration that meets the definition of a financial instrument should be classified as a financial liability or as equity in accordance with *PAS 32*.



Contingent consideration that is not classified as equity is subsequently measured at fair value through profit or loss whether or not it falls within the scope of *PFRS 9* (or *PAS 39*, if *PFRS 9* is not yet adopted). The amendment shall be prospectively applied to business combinations for which the acquisition date is on or after July 1, 2014. The *MERALCO Group* shall consider this amendment for future business combinations.

*PFRS 8, Operating Segments – Aggregation of Operating Segments and
Reconciliation of the Total of the Reportable Segments' Assets to the Entity's
Assets*

The amendments require entities to disclose the judgment made by management in aggregating two or more operating segments. This disclosure should include a brief description of the operating segments that have been aggregated in this way and the economic indicators that have been assessed in determining that the aggregated operating segments share similar economic characteristics. The amendments also clarify that an entity shall provide reconciliations of the total of the reportable segments' assets to the entity's assets if such amounts are regularly provided to the chief operating decision maker. These amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments affect disclosures only and have no impact on the *MERALCO Group's* financial position or performance.

PFRS 13, Fair Value Measurement – Short-term Receivables and Payables

The amendment clarifies that short-term receivables and payables with no stated interest rates can be held at invoice amounts when the effect of discounting is immaterial.

*PAS 16, Property, Plant and Equipment – Revaluation Method – Proportionate
Restatement of Accumulated Depreciation*

The amendment clarifies that, upon revaluation of an item of property, plant and equipment, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated depreciation at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated depreciation is eliminated against the gross carrying amount of the asset.

The amendment is effective for annual periods beginning on or after July 1, 2014. The amendment shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendment has no impact on *MERALCO Group's* financial position or performance.

PAS 24, Related Party Disclosures – Key Management Personnel

The amendments clarify that an entity is a related party of the reporting entity if the said entity, or any member of a group for which it is a part of, provides key management personnel services to the reporting entity or to the parent company of the reporting entity. The amendments also clarify that a reporting entity that obtains management personnel services from another entity (also referred to as management entity) is not required to disclose the compensation paid or payable by the management entity to its employees or directors. The reporting entity is required to disclose



the amounts incurred for the key management personnel services provided by a separate management entity. The amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments affect disclosures only and have no impact on *MERALCO Group's* financial position or performance.

PAS 38, Intangible Assets – Revaluation Method – Proportionate Restatement of Accumulated Amortization

The amendments clarify that, upon revaluation of an intangible asset, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated amortization at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated amortization is eliminated against the gross carrying amount of the asset.

The amendments also clarify that the amount of the adjustment of the accumulated amortization should form part of the increase or decrease in the carrying amount accounted for in accordance with the standard.

The amendments are effective for annual periods beginning on or after July 1, 2014. The amendments shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendments have no impact on the *MERALCO Group's* financial position or performance.

Annual Improvements to PFRSs (2011-2013 cycle)

The *Annual Improvements to PFRSs (2011-2013 cycle)* contain non-urgent but necessary amendments to the following standards:

PFRS 1, First-time Adoption of Philippine Financial Reporting Standards – Meaning of 'Effective PFRSs'

The amendment clarifies that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but that permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first *PFRS* financial statements. This amendment is not applicable to the *MERALCO Group's* as it is not a first-time adopter of *PFRS*.

PFRS 3, Business Combinations – Scope Exceptions for Joint Arrangements

The amendment clarifies that *PFRS 3* does not apply to the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively.



PFRS 13, Fair Value Measurement – Portfolio Exception

The amendment clarifies that the portfolio exception in *PFRS 13* can be applied to financial assets, financial liabilities and other contracts. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on *MERALCO Group's* financial position or performance.

PAS 40, Investment Property

The amendment clarifies the interrelationship between *PFRS 3* and *PAS 40* when classifying property as investment property or owner-occupied property. The amendment states that judgment is needed when determining whether the acquisition of investment property is the acquisition of an asset or a group of assets or a business combination within the scope of *PFRS 3*. This judgment is based on the guidance of *PFRS 3*. This amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on *MERALCO Group's* financial position or performance.

Deferred Effectivity

Philippine Interpretation IFRIC 15, Agreements for the Construction of Real Estate

This interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. The interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under *PAS 11* or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and rewards of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The *SEC* and the Financial Reporting Standards Council or *FRSC* have deferred the effectivity of this interpretation until the final "Revenue" standard is issued by the International Accounting Standards Board or *IASB* and an evaluation of the requirements of the final "Revenue" standard against the practices of the Philippine real estate industry is completed. Adoption of the interpretation when it becomes effective will not have any impact on the financial statements of *MERALCO*.

PFRS 9, Financial Instruments: Classification and Measurement

PFRS 9, as issued, reflects the first and third phases of the project to replace *PAS 39* and applies to the classification and measurement of financial assets and financial liabilities and hedge accounting, respectively. Work on second phase, which relates impairment of financial instruments, and the limited amendments to the classification and measurement model is still ongoing, with a view to replace *PAS 39* in its entirety. *PFRS 9* requires all financial assets to be measured at fair value at initial recognition. A debt financial asset may, if the fair value option or *FVO*, is not invoked, be subsequently measured at amortized cost if it is held within a business model that has the objective to hold the assets to collect the contractual cash flows and its contractual terms give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal outstanding. All other debt instruments are subsequently measured at fair value through profit or loss. All equity financial assets are measured at fair value either through *OCI* or profit or loss. All equity financial assets held for trading must be measured at fair value through profit or loss. For liabilities designated as at *FVPL* using the fair value option, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in *OCI*. The remainder of the change in fair value is presented in profit or loss, unless



presentation of the fair value change relating to the entity's own credit risk in *OCI* would create or enlarge an accounting mismatch in profit or loss. All other *PAS 39* classification and measurement requirements for financial liabilities have been carried forward into *PFRS 9*, including the embedded derivative separation rules and the criteria for using the *FVO*. The *MERALCO Group* conducted an evaluation of the early adoption of *PFRS 9* and has assessed that the first phase of *PFRS 9* will have an effect on the classification and measurement of financial assets. The *MERALCO Group* will quantify the effect on the consolidated financial statements in conjunction with the other phases, when issued, to present a comprehensive picture.

On hedge accounting, *PFRS 9* replaces the rules-based hedge accounting model of *PAS 39* with a more principles-based approach. Changes include replacing the rules-based hedge effectiveness test with an objectives-based test that focuses on the economic relationship between the hedged item and the hedging instrument, and the effect of credit risk on that economic relationship; allowing risk components to be designated as the hedged item, not only for financial items, but also for non-financial items, provided that the risk component is separately identifiable and reliably measurable; and allowing the time value of an option, the forward element of a forward contract and any foreign currency basis spread to be excluded from the designation of a financial instrument as the hedging instrument and accounted for as costs of hedging. *PFRS 9* also requires more extensive disclosures for hedge accounting.

PFRS 9 currently has no mandatory effective date. *PFRS 9* may be applied before the completion of the limited amendments to the classification and measurement model and impairment methodology. The *MERALCO Group* will not adopt the standard before the completion of the limited amendments and the second phase of the project.

Significant Accounting Policies

The principal accounting policies adopted in the preparation of the consolidated financial statements are as follows:

Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition-date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the *MERALCO Group* elects whether to measure the non-controlling interest in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs in a business combination are expensed.

When a business is acquired, an assessment is made of the identifiable assets acquired and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic and other pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquirer's previously held equity interest in the acquiree is remeasured at fair value as at acquisition date and any resulting gain or loss is recognized in profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration, which is deemed to be an asset or liability will be recognized in accordance with *PAS 39*, either in profit or



loss or other comprehensive income. If the contingent consideration is classified as equity, it shall not be remeasured until it is finally settled within equity.

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred, any non-controlling interest in the acquiree and, in a business combination achieved in stages, the acquisition-date fair value of the previously held equity interest in the acquiree, over the fair value of net identifiable assets acquired. If the difference is negative, such difference is recognized as gain in the consolidated statement of income.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the business combination occurs, the provisional amounts of the items for which the accounting is incomplete are reported in the consolidated financial statements. During the measurement period which is no longer than one year from the acquisition date, the provisional amounts recognized at acquisition date are retrospectively adjusted to reflect new information obtained about facts and circumstances that existed as at the acquisition date and, if known, would have affected the measurement of the amounts recognized as of that date. During the measurement period, additional assets or liabilities are also recognized if new information is obtained about facts and circumstances that existed as at the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as at that date.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from acquisition date, allocated to each of the cash generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units, beginning on the acquisition date.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in such circumstance is measured based on relative values of the operation disposed and the portion of the cash-generating unit retained.

Business combinations involving entities under common control are accounted for similar to the pooling-of-interest method. The assets and liabilities of the combining entities are reflected at their carrying amounts reported in the consolidated financial statements of the controlling holding company. Any difference between the consideration paid and the share capital of the “acquired” entity is reflected within equity as additional paid-in capital. The consolidated statement of income reflects the results of the combining entities for the full period, irrespective of when the combination takes place. Comparatives are presented as if the entities had always been combined since the date the entities were under common control.

Utility Plant and Others

Utility plant and others, except land, are stated at cost, net of accumulated depreciation and amortization and accumulated impairment losses, if any. Costs include the cost of replacing part of such utility plant and other properties when such cost is incurred, if the recognition criteria are met. All other repair and maintenance costs are recognized as incurred in the consolidated statement of income. The present value of the expected cost for the decommissioning of the asset after use is included in the cost of the respective asset if the recognition criteria for a provision are met.

Land is stated at cost less any impairment in value.



MERALCO's utility plant and others are stated at deemed cost. The revalued amount recorded as at January 1, 2004 was adopted as deemed cost as allowed by the transitional provisions of *PFRS 1*. The balance of revaluation increment was closed to retained earnings. See *Note 16 – Equity* for the related discussion.

Depreciation and amortization of utility plant and others are computed using the straight-line method (except for certain subtransmission and distribution assets, which use straight-line functional group method) over the following estimated useful lives:

Asset Type	Estimated Useful Lives
Subtransmission and distribution	10-50 years, depending on the life of the significant parts
Buildings and improvements	15-40 years
Communication equipment	10 years
Office furniture, fixtures and other equipment	5-15 years
Transportation equipment	5-10 years
Others	5-20 years

An item of utility plant and others is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising as a result of the derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statement of income in the period the asset is derecognized.

The asset's residual values, useful lives and methods of depreciation and amortization are reviewed, and adjusted prospectively if appropriate, at each reporting date to ensure that the residual values, periods and methods of depreciation and amortization are consistent with the expected pattern of economic benefits from items of utility plant and others.

Construction in Progress

Construction in progress is stated at cost, which includes cost of construction, plant and equipment, capitalized borrowing costs and other direct costs. Construction in progress is not depreciated until such time that the relevant assets are substantially completed and available for their intended use.

Borrowing Costs

Borrowing costs are capitalized if they are directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. Capitalization of borrowing costs commences when the activities necessary to prepare the qualifying asset for its intended use or sale have been undertaken and expenditures and borrowing costs have been incurred. Borrowing costs are capitalized until the asset is substantially available for its intended use.

Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds, as well as any exchange differences arising from any foreign currency-denominated borrowings used to finance the projects, to the extent that they are regarded as an adjustment to interest costs.

All other borrowing costs are expensed as incurred.



Investment Properties

Investment properties, except land, are stated at cost, net of accumulated depreciation and accumulated impairment loss, if any. The carrying amount includes transaction costs and costs of replacing part of an existing investment property at the time such costs are incurred if the recognition criteria are met and excludes the costs of day-to-day servicing of an investment property.

Investment properties include properties that are being constructed or developed for future use as investment property.

Land classified as investment property is carried at cost less any impairment in value.

MERALCO's investment properties acquired before January 1, 2004 are stated at deemed cost. See *Note 16 – Equity* for the related discussions.

Investment properties, except land, are being depreciated on a straight-line basis over the useful life of 5 to 35 years.

Investment properties are derecognized either when they have been disposed of or when these are permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss from the derecognition of the investment properties are recognized in the consolidated statement of income in the period these are disposed or retired.

Transfers are made to investment property when and only when there is a change in use, evidenced by ending of owner-occupation or commencement of an operating lease to another party. If owner-occupied property becomes an investment property, the *MERALCO Group* accounts for such property in accordance with the policy stated under utility plant and others up to the date of the change in use. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale. Transfers from investment property are recorded using the carrying amount of the investment property at the date of change in use.

Asset Retirement Obligations

Under the terms of certain lease contracts, the *MERALCO Group* is required to dismantle the installations made in leased sites and restore such sites to their original condition at the end of the term of the lease contracts. The *MERALCO Group* recognizes a liability measured at the present value of the estimated costs of these obligations and capitalizes such costs as part of the balance of the related item of utility plant and others and investment properties. The amount of asset retirement obligations is accreted and such accretion is recognized as interest expense.

Intangible Assets

Intangible assets acquired separately are initially measured at cost. Following initial recognition, intangible assets are carried at cost less accumulated amortization and any accumulated impairment loss. The useful lives of intangible assets are assessed at the individual asset level as having either finite or indefinite useful lives.

Intangible assets with finite lives are amortized over the useful economic lives of five years using the straight-line method and assessed for impairment whenever there is an indication that the intangible assets may be impaired. At a minimum, the amortization period and the amortization



method for an intangible asset with a finite useful life are reviewed at each reporting date. Changes in the expected useful life or the expected consumption pattern of future economic benefit embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and treated as change in accounting estimates. The amortization expense of intangible assets with finite lives is recognized in the consolidated statement of income.

Intangible assets with indefinite useful lives are not amortized, but are assessed for impairment annually either individually or at the cash-generating unit level. The assessment of indefinite useful life is done annually at every reporting date to determine whether such indefinite useful life continues to exist. Otherwise, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset, and are recognized in the consolidated statement of income.

Intangible assets generated within the business are not capitalized and expenditures are charged to profit or loss in the period these are incurred.

Investments in Associates and Joint Ventures

An associate is an entity over which *MERALCO* has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The considerations made in determining significant influence or joint control are similar to those necessary to determine control over subsidiaries.

Investments in associates and joint ventures are accounted for using the equity method of accounting and are initially recognized at cost.

Under the equity method, the investment in an associate or a joint venture is initially recognized at cost. The carrying amount of the investment is adjusted to recognize changes in the *MERALCO Group's* share of net assets of the associate or joint venture since the acquisition date. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortized nor individually tested for impairment.

The consolidated statement of income reflects the *MERALCO Group's* share of the results of operations of the associate or joint venture. Any change in *OCI* of those investees is presented as part of *MERALCO Group's OCI*. In addition, when there has been a change recognized directly in the equity of the associate or joint venture, the *MERALCO Group* recognizes its share of any changes, when applicable, in the consolidated statement of changes in equity. Unrealized gains and losses resulting from transactions between the *MERALCO Group* and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.



The aggregate of the *MERALCO Group*'s share of profit or loss of an associate and a joint venture is shown on the face of the consolidated statement of income outside operating income and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate or joint venture.

The financial statements of the associate or joint venture are prepared for the same reporting period as the *MERALCO Group*. When necessary, adjustments are made to bring the accounting policies in line with those of the *MERALCO Group*.

After application of the equity method, the *MERALCO Group* determines whether it is necessary to recognize an impairment loss on its investment in its associate or joint venture. At each reporting date, the *MERALCO Group* determines whether there is objective evidence that the investment in the associate or joint venture is impaired. If there is such evidence, the *MERALCO Group* calculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying value, then recognizes the loss as equity in net earnings of an associate and a joint venture in the consolidated statement of income.

Upon loss of significant influence over the associate or joint control over the joint venture, the *MERALCO Group* measures and recognizes any retained investment at its fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognized in profit or loss.

Impairment of Nonfinancial Assets

The *MERALCO Group* assesses at each reporting date whether there is an indication that a nonfinancial asset (utility plant and others, investment properties, investments in and advances to associates and joint ventures, receivable from the *BIR* and intangible assets), other than goodwill and intangible assets with indefinite useful life, may be impaired. If any such indication exists, the *MERALCO Group* makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an individual asset's or a cash generating unit's fair value less costs to sell and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. The fair value is the amount obtainable from the sale of the asset in an arm's-length transaction. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation factors/parameters, quoted share prices for publicly traded securities or other available fair value indicators. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognized in the consolidated statement of income.

An assessment is also made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the *MERALCO Group* estimates the individual asset's or cash generating unit's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If a reversal of impairment loss is to be recognized, the carrying amount of the asset is increased to its recoverable amount. The increased amount cannot exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the consolidated statement of income. After such reversal, the depreciation and amortization expense are adjusted in future periods to allocate the



asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Intangible assets with indefinite useful lives are tested for impairment annually at every reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired, either individually or at the cash generating unit level, as appropriate. The amount of impairment is calculated as the difference between the recoverable amount of the intangible asset and its carrying amount. The impairment loss is recognized in the consolidated statement of income. Impairment losses relating to intangible assets may be reversed in future periods.

Goodwill is reviewed for impairment annually at every reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Impairment is determined for goodwill by assessing the recoverable amount of the cash-generating unit or group of cash generating units, to which the goodwill relates. Where the recoverable amount of the cash generating unit or group of cash-generating units is less than the carrying amount of the cash generating unit or group of cash generating units to which goodwill has been allocated, an impairment loss is recognized. Impairment losses relating to goodwill cannot be reversed in future periods.

If there is incomplete allocation of goodwill acquired in a business combination to cash generating units or group of cash generating units, an impairment testing of goodwill is only carried out when impairment indicators exist. Where impairment indicators exist, impairment testing of goodwill is performed at a level at which the acquirer can reliably test for impairment.

Fair Value Measurement

The *MERALCO Group* measures financial instruments at fair value at each reporting date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transactions between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either (a) in the principal market for the asset or liability, or (b) in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible to the *MERALCO Group*.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a nonfinancial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The *MERALCO Group* uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- i. Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities;



- ii. Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and
- iii. Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognized in the consolidated financial statements on a recurring basis, the *MERALCO Group* determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting year.

For the purpose of fair value disclosures, the *MERALCO Group* has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy.

Inventories

Inventories are stated at the lower of cost or net realizable value. Costs of acquiring materials and supplies including costs incurred in bringing each item to their present location and condition are accounted using the moving average cost method. Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost to sell or the current replacement cost of the asset.

Financial Assets

Initial Recognition

Financial assets are classified as at fair value through profit or loss or *FVPL*, loans and receivables, held-to-maturity or *HTM* investments, *AFS* financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The classification of financial assets is determined at initial recognition and, where allowed and appropriate, re-evaluated at each reporting date.

Financial assets are recognized initially at fair value. Transaction costs are included in the initial measurement of all financial assets, except for financial instruments measured at *FVPL*.

Purchases or sales of financial assets that require delivery of assets within a timeframe established by regulation or convention in the market place (regular way purchase) are recognized on the trade date, which is the date the *MERALCO Group* commits to purchase or sell the asset.

The *MERALCO Group's* financial assets include cash and cash equivalents, trade and non-trade receivables, advance payments to a supplier, quoted and unquoted equity securities and embedded derivatives that are not accounted for as effective accounting hedges.

Subsequent Measurement

The subsequent measurement of financial assets depends on the classification as follows:



Financial Assets at FVPL

Financial assets at *FVPL* include financial assets held-for-trading and financial assets designated upon initial recognition as at *FVPL*. Financial assets are classified as held-for-trading if they are acquired for the purpose of selling in the near term. Derivative assets, including separated embedded derivatives are also classified as held-for-trading unless they are designated as effective hedging instruments.

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

Financial assets at *FVPL* are carried in the consolidated statement of financial position at fair value with gains or losses on fair value changes recognized in the consolidated statement of income under “Interest and other financial income” or “Interest and other financial charges” account, respectively. Interest earned and dividends received from investment at *FVPL* are also recognized in the consolidated statement of income under “Interest and other financial income” account.

Derivatives embedded in host contracts are accounted for as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value. These embedded derivatives are measured at fair value with gains and losses arising from changes in fair value recognized in the consolidated statement of income. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required under the contract.

Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such financial assets are carried at amortized cost using the effective interest method. This method uses an effective interest rate that discounts estimated future cash receipts through the expected life of the financial asset to the net carrying amount of the financial asset. Gains or losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as when these are amortized. Interest earned or incurred is recorded in “Interest and other financial income” or “Interest and other financial charges” account, respectively, in the consolidated statement of income. Assets in this category are included under current assets except for assets with maturities beyond 12 months from the reporting date, which are classified as noncurrent assets.

HTM Investments

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as *HTM* when the *MERALCO Group* has the positive intention and ability to hold these assets to maturity. After initial measurement, *HTM* investments are measured at amortized cost using the effective interest method. Gains or losses are recognized in the consolidated statement of income. Assets in this category are included in the current assets except for maturities beyond 12 months from the reporting date, which are classified as noncurrent assets.



AFS Financial Assets

AFS financial assets are non-derivative financial assets that are designated as *AFS* or are not classified in any of the three foregoing categories. They are purchased and held indefinitely and may be sold in response to liquidity requirements or changes in market conditions. After initial measurement, *AFS* financial assets are measured at fair value with unrealized gains or losses recognized in other comprehensive income until the investment is derecognized, at which time the cumulative gain or loss recorded in other comprehensive income is recognized in the consolidated statement of income, or determined to be impaired, at which time the cumulative loss recorded in other comprehensive income is recognized in the consolidated statement of income. Interest earned on holding *AFS* debt securities are included under “Interest and other financial income” account in the consolidated statement of income. Dividends earned on holding *AFS* equity are recognized in the consolidated statement of income under “Interest and other financial income” account when the right of the payment has been established. These are included under noncurrent assets unless there is an intention to dispose of the investment within 12 months from the reporting date.

Financial Liabilities

Initial Recognition

Financial liabilities are classified as financial liabilities at *FVPL*, other financial liabilities, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The classification of the financial liability is determined at initial recognition.

Financial liabilities are recognized initially at fair value inclusive of directly attributable transaction costs, except for financial liabilities at *FVPL*.

The *MERALCO Group*’s financial liabilities include notes payable, interest-bearing long-term financial liabilities, trade payables and other current liabilities (excluding output *VAT*, accrued taxes, reinsurance liabilities and deferred lease income), customers’ deposits, refundable service extension costs, customers’ refund and other noncurrent liabilities.

Subsequent Measurement

The subsequent measurement of financial liabilities depends on their classification as follows:

Financial Liabilities at FVPL

Financial liabilities at *FVPL* include financial liabilities held-for-trading and financial liabilities designated upon initial recognition as at *FVPL*. Financial liabilities are classified as held-for-trading if they are incurred for the purpose of repurchasing in the near term. Derivative liabilities, including separated embedded liabilities are also classified as held-for-trading unless they are designated as effective hedging instruments. Financial liabilities at *FVPL* are carried in the consolidated statement of financial position at fair value with gains or losses recognized in the consolidated statement of income under “Interest and other financial income” or “Interest and other financial charges” account, respectively. Interest incurred on financial liabilities designated as at *FVPL* is recognized in the consolidated statement of income under “Interest and other financial charges” account.



Financial liabilities may be designated at initial recognition as at *FVPL*, if any of the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the liabilities or recognizing gains or losses on them on a different bases; (ii) the financial liabilities are part of a group which are managed and their performance are evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial liabilities contain one or more embedded derivatives that would need to be recorded separately. The *MERALCO Group* does not have financial liabilities designated as at *FVPL* as at December 31, 2013 and 2012.

Other Financial Liabilities

After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method.

Gains and losses are recognized in the consolidated statement of income when the liabilities are derecognized as when these are amortized. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are integral part of the effective interest rate. The effective interest amortization is included under "Interest and other financial charges" account in the consolidated statement of income.

Derivative Financial Instruments

Initial Recognition and Subsequent Measurement

MERALCO has separated embedded foreign currency forwards which are derivative financial instruments used to hedge risks associated with foreign currency fluctuations.

Derivative instruments, including separated embedded derivatives, are initially recognized at fair value on the date at which a derivative transaction is entered into or separated, and are subsequently re-measured at fair value. Changes in fair value of derivative instruments, other than those accounted for as effective hedges, are recognized immediately in the consolidated statement of income. Changes in fair value of derivative instruments accounted as effective hedges are recognized in other comprehensive income. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. *MERALCO Group* does not have derivatives accounted for under hedge accounting.

An embedded derivative is separated from the hybrid or combined contract if all the following conditions are met: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the hybrid instrument is not recognized as at *FVPL*.

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

See Note 28 – *Financial Assets and Financial Liabilities*.



Offsetting of Financial Instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statement of financial position if, and only if, there is currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Amortized Cost of Financial Instruments

Amortized cost is computed using the effective interest method less any allowance for impairment and principal repayment, plus or minus the cumulative amortization of premium or discount. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of effective interest.

'Day 1' Profit or Loss

Where the transaction price in a non-active market is different from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the *MERALCO Group* recognizes the difference between the transaction price and fair value (a 'Day 1' profit or loss) in the consolidated statement of income, unless it qualifies for recognition as some other type of asset or liability. In cases where data used are not observable, the difference between the transaction price and model value is only recognized in the consolidated statement of income when the inputs become observable or when the instrument is derecognized. For each transaction, the *MERALCO Group* determines the appropriate method of recognizing the 'Day 1' profit or loss amount.

Impairment of Financial Assets

The *MERALCO Group* assesses at each reporting date whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial Assets Carried at Amortized Cost

For financial assets carried at amortized cost, the *MERALCO Group* first assesses whether objective evidence of impairment exists individually. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment based on historical loss experience. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment. *MERALCO* and *CEDC* consider termination or disconnection of service and significant financial difficulties of debtors as objective evidence that a financial asset or group of financial assets is impaired. For both specific and collective assessments, any deposits, collateral and credit enhancement are considered in determining the amount of impairment loss.



If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). If a loan is subject to variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The carrying amount of the asset is reduced either directly or through the use of an allowance account and the amount of the loss is recognized in the consolidated statement of income. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. The financial asset together with associated allowance is written off when there is no realistic prospect of future recovery and all collateral or deposits has been realized or has been transferred to the *MERALCO Group*.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If an asset written off is recovered, the recovery is recognized in the consolidated statement of income. Any reversal of an impairment loss is recognized in the consolidated statement of income, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

AFS Financial Assets

In the case of equity instruments classified as *AFS*, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. When a decline in the fair value of an *AFS* financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from equity to profit or loss even though the financial asset has not been derecognized. The amount of the cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on the financial asset previously recognized in profit or loss. Impairment losses recognized in profit or loss for investment in equity instruments are not reversed in the consolidated statement of income. Subsequent increases in fair value after impairment are recognized directly in other comprehensive income.

In the case of debt instruments classified as *AFS*, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued based on the rate of interest used to discount future cash flows for the purpose of measuring impairment loss. Such accrual is recorded as part of "Interest and other financial income" in the consolidated statement of income. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the consolidated statement of income, the impairment loss is reversed in the consolidated statement of income.

Assets Carried at Cost

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



Derecognition of Financial Instruments

Financial Assets

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

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

Where the *MERALCO Group* has transferred its right to receive cash flows from an asset or has entered into a “pass-through” arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, a new asset is recognized to the extent of the *MERALCO Group*’s continuing involvement in the asset.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that the *MERALCO Group* could be required to repay.

Financial Liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or has expired.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the carrying amount of a financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed is recognized in the consolidated statement of income.

Redeemable Preferred Stock

MERALCO’s peso-denominated redeemable preferred stock has characteristics of a liability and is thus recognized as a liability in the consolidated statement of financial position. The corresponding dividends on those shares are recognized as part of “Interest and other financial charges” account in the consolidated statement of income. Dividends are no longer accrued when such shares have been called for redemption.

Provisions

Provisions are recognized when the *MERALCO Group* has a present obligation, legal or constructive, as a result of a past event, and when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the *MERALCO Group* expects a provision, or a portion, to be reimbursed, for example under an insurance contract, the reimbursement is



recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statement of income, net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liabilities.

Retirement Benefits

MERALCO and substantially all of its subsidiaries have distinct, funded, noncontributory defined benefit retirement plans covering all permanent employees. *MERALCO*'s retirement plan provides for post-retirement benefits in addition to a lump sum payment to employees hired as at December 31, 2003. Retirement benefits for employees hired commencing January 1, 2004 were amended to provide for a defined lump sum payment only. *MERALCO* also has a contributory Provident Plan introduced in January 2009 whereby employees hired commencing January 1, 2004 may elect to participate.

The net defined benefit liability or asset is the aggregate of the present value of the defined benefit obligation at the end of the reporting period reduced by the fair value of plan assets (if any), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling. The asset ceiling is the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The cost of providing benefits under the defined benefit plans is actuarially determined using the projected unit credit method.

Defined benefit costs comprise the following:

- Service cost
- Net interest on the net defined benefit liability or asset

Service costs, which include current service costs, past service costs and gains or losses on non-routine settlements are recognized as expense in profit or loss. Past service costs are recognized when plan amendment or curtailment occurs. These amounts are calculated periodically by independent qualified actuaries.

Net interest on the net defined benefit liability or asset is the change during the period in the net defined benefit liability or asset that arises from the passage of time, which is determined by applying the discount rate based on government bonds to the net defined benefit liability or asset. Net interest on the net defined benefit liability or asset is recognized as expense or income in profit or loss.

Remeasurements comprising actuarial gains and losses, return on plan assets and any change in the effect of the asset ceiling (excluding net interest on defined benefit liability) are recognized immediately in other comprehensive income in the period in which they arise. Remeasurements are not reclassified to profit or loss in subsequent periods.

Plan assets are assets that are held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the creditors of the *MERALCO Group*, nor can they be paid directly to the *MERALCO Group*. Fair value of plan assets is based on market price information. When no market price is available, the fair value of plan assets is estimated by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligations). If the fair value of the plan assets is higher than the present value of the defined benefit obligation, the measurement of



the resulting defined benefit asset is limited to the present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The *MERALCO Group's* right to be reimbursed of some or all of the expenditure required to settle a defined benefit obligation is recognized as a separate asset at fair value when and only when reimbursement is virtually certain.

The retirement costs under the defined contribution plan are recorded based on *MERALCO's* contribution to the defined contribution plan as services are rendered by the employee.

Termination Benefits

Termination benefits are employee benefits provided in exchange for the termination of an employee's employment as a result of either an entity's decision to terminate an employee's employment before the normal retirement date or an employee's decision to accept an offer of benefits in exchange for the termination of employment.

A liability and expense for a termination benefit is recognized at the earlier of when the entity can no longer withdraw the offer of those benefits and when the entity recognizes related restructuring costs. Initial recognition and subsequent changes to termination benefits are measured in accordance with the nature of the employee benefit, as either post-employment benefits, short-term employee benefits, or other long-term employee benefits.

Employee Leave Entitlements

Employee entitlements to annual leave are recognized as a liability when they are accrued to the employees. The undiscounted liability for leave expected to be settled wholly before 12 months after the end of the annual reporting period is recognized for services rendered by employees up to the end of the reporting period.

Long-term Incentive Plan

The liability relating to the long-term incentive plan comprises the present value of the defined benefit obligation at the end of the reporting period.

Employee Stock Purchase Plan or ESPP

Up to 2009, *MERALCO* had an employee stock purchase plan, which covered active and retired employees. Under the plan, the qualified participant may purchase fixed number of shares of stock at a pre-agreed price. The plan features include vesting requirements and payment terms.

The cost of equity-settled transactions with employees is measured by reference to the difference between the fair value of the shares on the grant date and the price at which the share may be purchased under the award or offer. In valuing equity-settled transactions, no account is taken of any performance conditions other than market conditions.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date at which the relevant employees become fully entitled to the award ('the vesting date'). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and *MERALCO's* best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or



credit for a period represents the movement in cumulative expense recognized as at the beginning and end of the reporting period.

No expense is recognized for awards that do not ultimately vest.

When the terms of the equity-settled awards are modified and the modification increases the fair value of the equity instruments granted, as measured immediately before and after the modification, the entity shall include the incremental fair value granted in the measurement of the amount recognized for services received as consideration for the equity instrument granted. The incremental fair value granted is the difference between the fair value of the modified equity instrument and that of the original equity instrument, both estimated as at the date of the modification. If the modification occurs during the vesting period, the incremental fair value granted is included in the measurement of the amount recognized for services received over the period from the modification date until the date when the modified equity instruments vest, in addition to the amount based on the grant date fair value of the original equity instruments, which is recognized over the remainder of the original vesting period. If the modification occurs after vesting date, the incremental fair value granted is recognized immediately or over the vesting period if the employee is required to complete an additional period of service before becoming unconditionally entitled to those modified equity instruments.

Revenue Recognition

Revenues are stated at amounts invoiced to customers, inclusive of pass-through components, net of discounts, rebates, *VAT* and other taxes, where applicable. Revenue is recognized to the extent that it is probable that the economic benefits will flow to the *MERALCO Group* and the revenue can be reliably measured. In addition, collectability is reasonably assured and the delivery of the goods or rendering of the service has occurred. The *MERALCO Group* assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent. The *MERALCO Group* concluded that it is acting as principal in all of its revenue arrangements. The following specific recognition criteria must also be met before revenue is recognized:

Sale of Electricity

Revenues are recognized upon supply of power to the customers. The Uniform Filing Requirements or *UFR*, on the rate unbundling released by the *ERC* on October 30, 2001 specified the following bill components: (a) generation charge, (b) transmission charge, (c) *SL* charge, (d) distribution charge, (e) supply charge, (f) metering charge, (g) Currency Exchange Rate Adjustment or *CERA* I and II, where applicable and (h) interclass and lifeline subsidies. *VAT*, *LFT*, the Power Act Reduction (for residential customers) adjustment and universal charges are also separately presented in the customer's billing statement. *VAT*, *LFT* and universal charges are billed and collected on behalf of the national and local governments and do not form part of *MERALCO* and *CEDC*'s revenues.

Sale of Services

Revenues from construction contracts are recognized and measured using the percentage-of-completion method of accounting for the physical portion of the contract work, determined based on the actual costs incurred in relation to the total estimated costs of the contract. Revenue from contracts to manage, supervise or coordinate construction activity for others and contracts where materials and services are supplied by project owners are recognized only to the extent of the contracted fees.



Contract costs principally include subcontracted costs related to contract performance. Expected losses on contracts are recognized immediately when it is probable that the total contract costs will exceed total contract revenues. The amount of such loss is determined irrespective of whether or not work has commenced on the contract; the stage of completion of contract activity; or the amount of profits expected to arise on other contracts, which are not treated as a single construction contract. Changes in contract performance, contract conditions and estimated profitability, including those arising after final contract settlements and after gross margins are recognized in the period in which the changes are determined.

Service and consulting fees are recognized when the services are rendered.

Interest Income

Revenue is recognized as interest accrues, using the effective interest method. The effective interest rate is the rate that discounts estimated future cash receipts through the expected life of the financial instrument.

Dividends

Revenue is recognized when the *MERALCO Group*'s right to receive the payment is established.

Lease Income

Income arising from lease of investment properties and poles is accounted for on a straight-line basis over the lease term.

Lease income is included under "Revenues - Sale of other services" account in the consolidated statement of income.

Expense Recognition

Expenses are decreases in economic benefits during the financial reporting period in the form of outflows or decrease of assets or incurrence of liabilities that result in decrease in equity, other than those relating to distributions to equity participants. These are recognized when incurred.

Leases

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

Company as Lessee

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

Company as Lessor

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



Foreign Currency-Denominated Transactions and Translations

The consolidated financial statements are presented in Philippine peso, which is also *MERALCO*'s functional and presentation currency. The Philippine peso is the currency of the primary economic environment in which *MERALCO Group* operates, except for *LOIL* and *MPG Asia*. This is also the currency that mainly influences the revenue from and cost of rendering services. Each entity in *MERALCO Group* determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

The functional currency of *LOIL* and *MPG Asia* is the United States or *U.S.* dollar.

Transactions in foreign currencies are initially recorded in the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated using functional currency closing rate of exchange prevailing at the end of the reporting period. All differences are recognized in the consolidated statement of income except for foreign exchange differences that relate to capitalizable borrowing costs on qualifying assets. Nonmonetary items that are measured in terms of historical cost in foreign currency are translated using the exchange rate as at the date of the initial transactions.

As at the reporting date, the monetary assets and liabilities of associates, *LOIL* and *MPG Asia* whose functional currency is other than Philippine peso, are translated into Philippine peso at the rate of exchange prevailing at the end of the reporting period, and income and expenses of an associate are translated monthly using the weighted average exchange rate for the month. The exchange differences arising on translation are recognized as a separate component of other comprehensive income as cumulative translation adjustments. On disposal of the associate, the amount of cumulative translation adjustments recognized in other comprehensive income is recognized in the consolidated statement of income.

Income Taxes

Current Income Tax

Current income tax assets and liabilities for the current and prior period are measured at the amount expected to be recovered from or paid to the taxation authority. The tax rate and tax laws used to compute the amount are those that are enacted or substantively enacted as at the reporting date.

Deferred Income Tax

Deferred income tax is provided using the balance sheet liability method on all temporary differences at the reporting date between the income tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.



Deferred income tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized except:

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

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realized or the liability is settled, based on tax rates and tax laws that are enacted or substantively enacted as at the reporting date.

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

Deferred income tax items are recognized in correlation to the underlying transaction either in profit or loss or directly in equity.

Earnings per Share

Basic earnings per share is calculated by dividing the net income for the period attributable to equity holders of the parent by the weighted average number of common shares outstanding during the period.

Diluted earnings per share is calculated by dividing the net income for the period attributable to equity holders of the parent by the weighted average number of shares outstanding, adjusted for the effects of any dilutive potential common shares.

Contingencies

Contingent liabilities are not recognized in the consolidated financial statements. These are disclosed in the notes to consolidated financial statements unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized unless the realization of the assets is virtually certain. These are disclosed in the notes to consolidated financial statements when an inflow of economic benefits is probable.



Events After the Reporting Date

Post reporting date events that provide additional information about the *MERALCO Group's* financial position at the reporting date (adjusting events) are reflected in the consolidated financial statements. Post reporting date events that are not adjusting events are disclosed in the notes to consolidated financial statements, when material.

Equity

Common stock is measured at par value for all shares issued. Incremental costs incurred directly attributable to the issuance of new shares are shown as a deduction from equity, net of any related tax. The amount of proceeds and/or fair value of consideration received, net of incremental costs incurred directly attributable to the issuance of new shares in excess of par value is recognized as additional paid-in capital.

Employee stock purchase plan cost represents the cumulative compensation expense recognized based on the amount determined using an option pricing model. The 14th and last *ESPP*, which was awarded in 2009 fully vested in October 2012. Since 2009, there have been no *ESPPs* implemented.

Change in the ownership interest of a subsidiary, without loss of control, is accounted for as an equity transaction and presented as "Excess of acquisition cost over carrying value of non-controlling interest acquired".

Other comprehensive income comprises items of income and expense, which are not recognized in profit or loss as required or permitted by *PFRS*.

Retained earnings includes net income attributable to the equity holders of the Parent and is reduced by dividends declared on common stock. Dividends are recognized as a liability and deducted from retained earnings when they are declared. Dividend declarations approved after the financial reporting date are disclosed as events after the financial reporting date.

Non-controlling interests represent the equity interests in *CEDC* and *MIESCOR* and its subsidiaries, which are not held by *MERALCO*.

5. Management's Use of Significant Judgments, Accounting Estimates and Assumptions

The preparation of the *MERALCO Group's* consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent assets and liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Judgments

In the process of applying the *MERALCO Group's* accounting policies, management has made the following judgments, which have the most significant effect on the amounts recognized in the consolidated financial statements.



Determination of Functional Currency

The functional currencies of the entities under the *MERALCO Group* are the currencies of the primary economic environment in which each entity operates. It is the currency that mainly influences the revenue and cost of rendering services.

Based on the economic substance of the underlying circumstances, the functional and presentation currency of *MERALCO* and its subsidiaries, except *LOIL* and *MPG Asia*, is the Philippine peso. The functional and presentation currency of *LOIL* and *MPG Asia* is the U.S. dollar.

Operating Lease Commitments

As Lessor

As a lessor, the *MERALCO Group* has several lease arrangements. Based on the terms and conditions of the arrangements, it has evaluated that the significant risks and rewards of ownership of such properties are retained by the *MERALCO Group*. The lease agreements do not transfer ownership of the assets to the lessees at the end of the lease term and do not give the lessees a bargain purchase option over the assets. Consequently, the lease agreements are accounted for as operating leases.

As Lessee

As a lessee, *MERALCO Group* has commercial lease arrangements covering certain office spaces, payment offices and substation sites and towers. The *MERALCO Group* has determined, based on the evaluation of the terms and conditions of the arrangements, that it has not acquired any significant risks and rewards of ownership of such properties because the lease arrangements do not transfer to the *MERALCO Group* the ownership over the assets at the end of the lease term and do not provide the *MERALCO Group* a bargain purchase option over the leased assets. Consequently, the lease agreements are accounted for as operating leases.

Arrangement that Contains a Lease

MERALCO's Purchased Power Agreements or *PPAs* and Purchase Supply Agreements or *PSAs* with certain power generating companies qualify as leases on the basis that *MERALCO* and these power generating companies have 'take or pay' or *TOP* arrangements where payments for purchased power are made on the basis of the availability of the power plant and not based solely on actual consumption. In determining the lease classification, it is judged that substantially all the risks and rewards incident to the ownership of the power plants are with these power generating companies'. Thus, the *PPAs* and *PSAs* are classified as operating leases. Accordingly, capacity fees, fixed operating and maintenance, and transmission line fees that form part of purchased power expense are accounted for similar to a lease.

Components of purchased power expense, which have been accounted for similar to a lease, amounted to ₱46,170 million, ₱18,946 million and ₱20,135 million in 2013, 2012 and 2011 respectively. These are recognized as "Purchased Power" in the consolidated statements of income.



See Note 25 – Revenues and Purchased Power.

Entity in which the MERALCO Group Holds More Than the Majority of the Voting Rights Accounted for as joint Venture

MERALCO has 51% equity in San Buenaventura Power Ltd. Co. or SBPL. While MERALCO owns majority of the voting rights in SBPL, it does not have sole control over SBPL. MERALCO's investment in SBPL is accounted for as a joint venture since key operating and financial decisions of SBPL require the unanimous vote and consent of the parties sharing control.

Contingencies

The MERALCO Group has possible claims from or obligation to other parties from past events and whose existence may only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within its control. Management has determined that the present obligations with respect to contingent liabilities and claims with respect to contingent assets do not meet the recognition criteria, and therefore has not recorded any such amounts.

See Note 30 – Contingencies and Legal Proceedings.

Estimates and Assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty as at the reporting date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed in the following:

Estimating Useful Lives of Utility Plant and Others, Intangible Assets with Finite Lives and Investment Properties

The MERALCO Group estimates the useful lives of utility plant and others, intangible assets with finite lives and, investment properties based on the periods over which such assets are expected to be available for use. The estimate of the useful lives of the utility plant and others, intangible assets with finite lives and investment properties is based on management's collective assessment of industry practice, internal technical evaluation and experience with similar assets. The estimated useful lives are reviewed at least at each financial year-end and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limitations on the use of such assets. It is possible, however, that future results of operations could be materially affected by changes in estimates brought about by changes in the factors mentioned in the foregoing. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of utility plant and others, intangible assets with finite lives and investment properties would increase recorded operating expenses and decrease noncurrent assets.

The total depreciation and amortization expense of utility plant and others amounted to ₱5,941 million, ₱5,474 million and ₱5,466 million for the years ended December 31, 2013, 2012 and 2011, respectively. Total carrying values of utility plant and others, net of accumulated depreciation and amortization, amounted to ₱112,586 million and ₱109,312 million as at December 31, 2013 and 2012, respectively.

Total depreciation of investment properties amounted to ₱8 million, ₱8 million and ₱138 million for the years ended December 31, 2013, 2012 and 2011, respectively. Total carrying value of investment properties, net of accumulated depreciation, amounted to ₱1,526 million and ₱1,634 million as at December 31, 2013 and 2012, respectively.



Total amortization of intangible assets with finite lives amounted to ₱169 million, ₱94 million and ₱33 million for the years ended December 31, 2013, 2012 and 2011, respectively. Total carrying value of intangible assets with finite lives, net of accumulated amortization, amounted to ₱1,728 million and ₱1,021 million as at December 31, 2013 and 2012, respectively.

See Note 8 – *Utility Plant and Others*, Note 10 – *Investment Properties* and Note 11 – *Other Noncurrent Assets*.

Impairment of Nonfinancial Assets

PFRS requires that an impairment review be performed when certain impairment indicators are present. These conditions include obsolescence, physical damage, significant changes in the manner by which an asset is used, worse than expected economic performance, drop in revenues or other external indicators, among others. In the case of goodwill, at a minimum, such asset is subject to an annual impairment test and more frequently whenever there is an indication that such asset may be impaired. This requires an estimation of the value in use of the cash generating unit to which the goodwill is allocated. Estimating the value in use requires preparation of an estimate of the expected future cash flows from the cash generating unit and choosing an appropriate discount rate in order to calculate the present value of those cash flows.

Determining the recoverable amount of utility plant and others, investment properties, investments in and advances to associates and joint ventures, goodwill and other noncurrent assets, requires (i) the determination of future cash flows expected to be generated from the continued use as well as ultimate disposition of such assets and (ii) making estimates and assumptions that can materially affect the consolidated financial statements. Future events may cause management to conclude that utility plant and others, construction in progress, investment properties, investments in and advances to associates and joint ventures, and other noncurrent assets are impaired. Any resulting impairment loss could have a material adverse impact on the *MERALCO Group's* consolidated financial position and results of operations.

The preparation of estimated future cash flows involves significant estimations and assumptions. While management believes that the assumptions are appropriate and reasonable, significant changes in the assumptions may materially affect the assessment of recoverable values and may lead to future impairment charges under *PFRS*.

The carrying values of nonfinancial assets as at December 31, 2013 and 2012 subject to impairment review are as follows:

Account	2013	2012
	<i>(Amounts in millions)</i>	
Utility plant and others	₱112,586	₱109,312
Investments in associates and joint ventures	13,422	1,815
Investment properties	1,526	1,634
Intangible assets	1,728	1,021
Receivable from the <i>BIR</i>	577	577
Goodwill	36	36

See Note 8 – *Utility Plant and Others*, Note 9 – *Investments in Associates and Joint Ventures*, Note 10 – *Investment Properties* and Note 11 – *Other Noncurrent Assets*.



Goodwill

The *MERALCO Group's* consolidated financial statements and the results of operations reflect acquired businesses after the completion of the respective acquisition. The *MERALCO Group* accounts for the acquisition of businesses using the acquisition method of accounting, which requires extensive use of accounting judgments and estimates to allocate the purchase price to the fair market values of the acquiree's identifiable assets and liabilities and contingent liabilities, if any, at the acquisition date. Any excess in the purchase price over the estimated fair market values of the net assets acquired is recorded as goodwill in the consolidated statement of financial position. Thus, the number of items, which involve judgments made in estimating the fair market value to be assigned to the acquiree's assets and liabilities can materially affect the *MERALCO Group's* financial position.

Realizability of Deferred Tax Assets

The *MERALCO Group* reviews the carrying amounts of deferred tax assets at the end of each reporting period and reduces these to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred income tax assets to be utilized.

Assessment on the recognition of deferred tax assets on deductible temporary differences is based on the level and timing of forecasted taxable income for the subsequent reporting periods. This forecast is based on past results and future expectations on revenues and expenses as well as future tax planning strategies. Management believes that sufficient taxable profit will be generated to allow all or part of the deferred tax assets to be utilized. The amounts of the deferred tax assets considered realizable could be adjusted in the future if estimates of taxable income are revised.

Based on the foregoing assessment, following are the relevant consolidated information with respect to deferred tax assets:

	2013	2012
	<i>(Amounts in millions)</i>	
Recognized deferred tax assets	₱15,391	₱13,338
Unrecognized deferred tax assets	215	154

See *Note 29 – Income Taxes and Local Franchise Taxes*.

Determination of Fair Values of Financial Assets and Financial Liabilities

Where fair value of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using valuation techniques including the discounted cash flows model. The inputs to these models are taken from observable markets where possible, but when this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

See *Note 28 – Financial Assets and Financial Liabilities*.



Estimating Allowance for Doubtful Accounts

If there is objective evidence that an impairment loss has been incurred in the trade and other receivables balance of the *MERALCO Group*, an estimate of the allowance for doubtful accounts related to trade and other receivables that are specifically identified as doubtful of collection is made. The amount of allowance is evaluated by management on the basis of factors that affect the collectability of the accounts. In such case, use of judgment based on the best available facts and circumstances, including but not limited to, the length of the *MERALCO Group's* relationship with the customer and the customer's credit status based on third party credit reports and known market factors, to record specific reserves for customers against amounts due in order to reduce the *MERALCO Group's* receivables to amounts that management expects to collect is applied. These specific reserves are reevaluated and adjusted as additional information received affect the amounts estimated.

In addition to specific allowance against individually significant receivables, an assessment for collective impairment allowance against credit exposures of the customers, which were grouped based on common credit characteristics, although not specifically identified as requiring a specific allowance, have a greater risk of default than when the receivables were originally granted to customers is done. This collective allowance is based on historical loss experience using various factors, such as historical performance of the customers within the collective group, deterioration in the markets in which the customers operate, and identified structural weaknesses or deterioration in the cash flows of customers.

Total asset impairment provision for trade and other receivables and other current assets recognized in the consolidated statements of income amounted to ₱504 million, ₱832 million and ₱2,243 million for the years ended December 31, 2013, 2012 and 2011, respectively. Trade and other receivables, net of asset impairment, amounted to ₱32,718 million and ₱28,077 million as at December 31, 2013 and 2012, respectively.

See *Note 13 – Trade and Other Receivables* and *Note 15 – Other Current Assets*.

Estimating Net Realizable Value of Inventories

Inventories consist of materials and supplies used in the power distribution and services segments. The excess of cost over net realizable value relating to inventories consists of collective and specific provisions. The cost of inventories is written down whenever the net realizable value of inventories becomes lower than the cost due to damage, physical deterioration, obsolescence, change in price levels or other causes. The lower of cost or net realizable value of inventories is reviewed on a periodic basis. Inventory items identified to be obsolete and unusable are written-off and charged as expense in the consolidated statement of income.

The carrying values of inventories amounted to ₱2,750 million and ₱1,371 million as at December 31, 2013 and 2012, respectively.

See *Note 14 – Inventories*.

Estimation of Retirement Benefit Costs

The cost of defined benefit pension plans and other post-employment benefits as well as the present value of the pension obligation are determined using actuarial valuations. The actuarial valuation involves making various assumptions. These include the determination of the discount rates, future salary increases, mortality rates and future pension increases. Due to the complexity



of the valuation, the underlying assumptions and its long-term nature, defined benefit obligations are highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date. The pension benefit liability and other post-employment benefit as at December 31, 2013 and 2012 amounted to ₱2,978 million and ₱6,241 million, respectively.

In determining the appropriate discount rate, management considers the interest rates of government bonds in the respective currencies, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation. The underlying bonds are further reviewed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, on the basis that they do not represent high quality bonds.

The mortality rate is based on publicly available mortality tables for the specific country and is modified accordingly with estimates of mortality improvements. Future salary increases and pension increases are based on expected future inflation rates for the specific country.

See *Note 26 – Expenses and Income* and *Note 27 – Long-term Employee Benefits*.

Insurance Liabilities Arising from Insurance Contracts

RSIC estimates the expected ultimate costs of claims reported and claims incurred but not yet reported at reporting date. It takes a significant period of time to establish with certainty the ultimate cost of claims.

The primary technique adopted by RSIC's management in estimating the cost of claims incurred but not yet reported is using the past claims settlement trend to predict the future claims settlement trend. At each reporting date, estimates of prior period claims are reassessed for adequacy and any changes are charged to provisions. Insurance contract liabilities are not discounted for the time value of money.

As at December 31, 2013 and 2012, gross carrying values of insurance liabilities arising from insurance contracts, included in "Other noncurrent liabilities" account, amounted to ₱725 million and ₱625 million, respectively.

Provision for Asset Retirement Obligations

Provision for asset retirement obligations is recognized in the period in which they are incurred if a reasonable estimate of fair value can be made. This requires an estimation of the cost to restore or dismantle, on a per area basis, depending on the location, and is based on the best estimate of the expenditure required to settle the obligation at the future restoration/dismantlement date, discounted using a pre-tax rate that reflects the current market assessment of the time value of money and, where appropriate, the risk specific to the liability.

No asset retirement obligation was recognized since the amount is immaterial.

Provisions

MERALCO Group is involved in various legal proceedings as discussed in Note 30 – *Contingencies and Legal Proceedings*. MERALCO Group's estimate for probable costs for the resolution of these claims, assessments and cases has been developed in consultation with external counsels handling the defense in these claims, assessments and cases and is based upon thorough analysis of potential outcome.



MERALCO, in consultation with its external legal counsels, does not believe that these proceedings will have a material adverse effect in the consolidated financial statements. It is possible, however, that future financial performance could be materially affected by changes in the estimates or the effectiveness of management's strategies and actions relating to these proceedings.

MERALCO recognized provisions amounting to ₱10,749 million, ₱9,226 million and ₱8,065 million for the years ended December 31, 2013, 2012 and 2011, respectively.

See *Note 20 – Provisions*.

Revenue Recognition

The *MERALCO Group's* revenue recognition policies require the use of estimates and assumptions that may affect the reported amounts of its revenues and receivables.

Revenues from sale of electricity by *MERALCO* and *CEDC* are billed based on customer-specific billing cycle cut-off date for each customer, while recording of related purchased power cost in the accounts is based on calendar month as provided in the terms of the *PSAs*. The recognition of unbilled revenues for billing cycles with earlier than month-end cut-off dates requires the use of estimates.

The difference between the amount initially recognized based on provisional invoices and the settlement of the actual billings by the generators is taken up in the subsequent period. Management believes that such use of estimates will not result in material adjustments in future periods.

Revenues and costs from construction contracts of *MIESCOR* are recognized based on the percentage of completion method. This is measured principally on the basis of the estimated completion of a physical proportion of the contract work as determined from the reports of the contractors and project consultants.

6. Discontinued Operations

In 2011, upon approval by the *BOD* of *MERALCO* of the divestment plan by *MERALCO* of its investment in common shares of *Rockwell Land* through the declaration of property dividends, *MERALCO* reclassified the related assets, liabilities and cumulative other comprehensive income of *Rockwell Land* as "Assets of discontinued operations", "Liabilities of discontinued operations" and "Unrealized fair value gains on *AFS* investments of discontinued operations", respectively, in the consolidated statement of financial position as at January 1, 2012.

On April 25, 2012, the *SEC* approved the property dividend declaration by the *BOD* of *MERALCO* (on February 27, 2012) of *MERALCO's* investment in common shares of *Rockwell Land* in favor of all Filipino common stockholders as at March 23, 2012. Foreign common stockholders were paid the cash equivalent of the property dividends at the time of declaration. Such property dividends were paid on May 14, 2012, within five (5) trading days after approval of the property dividend by the *SEC* and registration of the *Rockwell Land* shares under the Securities Regulation Code and the listing thereof with the *PSE* on May 11, 2012. As at the date of declaration, *MERALCO* owned 3,176,474,995 common shares at ₱1.46 per share with a total cost of ₱4,638 million.



The assets and liabilities of *Rockwell Land* classified as “Assets of discontinued operations” and “Liabilities of discontinued operations”, respectively, in the consolidated statement of financial position as at January 1, 2012 are as follows:

	Amount (In millions)
<i>Noncurrent Assets:</i>	
Property and equipment	P465
Investment properties	6,297
Other noncurrent assets	362
<i>Current Assets:</i>	
Cash and cash equivalents	769
Trade and other receivables	2,782
Land and development costs	5,950
Other current assets	1,724
	P18,349
<i>Noncurrent Liabilities:</i>	
Interest-bearing long-term financial liabilities	P2,867
Deposits from pre-selling condominium units	284
Deferred tax liabilities - net	146
Other noncurrent liabilities	470
<i>Current Liabilities:</i>	
Trade and other payables	5,258
Income tax payable	88
	P9,113

The financial performance of *Rockwell Land* for the four months ended April 30, 2012 and the year ended December 31, 2011 are presented as “Income from discontinued operations, net of income tax” in the consolidated statements of income. The details are presented as follows:

	2012 (Amounts in Millions)	2011
Revenues	P1,501	P5,834
Cost and expenses	1,288	4,887
Gross profit	213	947
Interest and other financial income	114	520
Interest and other financial expenses	(71)	(183)
Others	805	4
Income before income tax	1,061	1,288
Provision for income tax	(83)	(322)
Net income from discontinued operations	P978	P966

The net cash flows for the four months ended April 30, 2012 and the year ended December 31, 2011 are as follows:

	2012 (Amounts in Millions)	2011
Operating activities	P104	P398
Investing activities	(5)	(214)
Financing activities	1,085	(58)
Net cash flows	P1,184	P126

Included in accumulated other comprehensive income as at January 1, 2012 are unrealized fair value gains on *AFS* financial assets amounting to P14 million.



7. Segment Information

Each operating segment of the *MERALCO Group* engages in business activities from which revenues are earned and expenses are incurred (including revenue and expenses relating to transactions with other business segments within the *MERALCO Group*). The operating results of each of the operating segments are regularly reviewed by *MERALCO*'s chief operating decision-maker (Management Committee) to determine how resources are to be allocated to the operating segments and to assess their performances for which discrete financial information is available.

For management purposes, the *MERALCO Group*'s operating businesses are organized and managed separately according to the nature of services provided, with each segment representing a strategic business unit that offers different products and/or services, as follows:

- Power

The Power segment consists of (a) electricity distribution, (b) power generation and (c) *RES*.

Electricity distribution – This is principally electricity distribution and supply of power on a pass-through basis covering all captive customers in the *MERALCO* franchise area and the *CEDC* franchise area in the Luzon Grid. Electricity distribution within the *MERALCO* franchise area accounts for approximately 55% of the power requirements of the country. *CEDC*'s service area covers the *CSEZ*.

Power generation – The *MERALCO Group*'s re-entry in the power generation business is through investment in operating companies or participation in the development of power generation projects. *MGen*, the power generation arm of the *MERALCO Group* acquired a 20% equity interest in *GBPC*. *GBPC* operates a total of 627 *MW* gross capacity of coal and diesel-fired power plants. In addition, it has 232 *MW* of coal-fired power plants under construction in the Visayas.

In March 2013, *MGen* acquired an effective 28% equity in PacificLight Power Pte Ltd. or *PacificLight Power*, in Jurong Island, Singapore.

MGen is currently developing a 500 *MW* gross capacity of supercritical coal-fired power plant in Mauban, Quezon. On the other hand, land development for its 2 x 300 *MW* Circulating Fluidized Bed or *CFB*, coal-fired power generation plant in the Subic Freeport Zone under Redondo Peninsula Energy, Inc. or *RP Energy* is ongoing.

Further, *MGen* is in various stages of pre-development of other power generation projects in the Philippines.

See Note 9 – *Investments in Associates and Joint Ventures*.

RES – This covers the sourcing and supply of electricity to qualified contestable customers. The *MERALCO Group* serves as a local *RES* within its franchise area only under the brand, *MPower*. Starting June 26, 2013, certain qualified contestable customers sourced their electricity supply from *MPower*.



- Other Services

The other services segment is involved principally in electricity-related services such as electro-mechanical engineering, construction, consulting and related manpower as well as light rail- related maintenance services, e-transaction and bills collection, insurance and e-business development and distribution and energy systems management. These services are provided by *MIESCOR*, *MBI* and *MLI* (collectively known as “*MIESCOR Group*”), *CIS*, *Bayad Center* and *CFSI* (collectively referred to as “*CIS Group*”), *Miescorrail*, *RSIC*, *LOIL*, *Finserve*, *e-MVI* and *MEI*.

MERALCO’s real estate segment, which was provided by *Rockwell Land*, is involved in luxury residential and commercial real estate development and leasing. In 2012, the accounts of *Rockwell Land* were deconsolidated from those of *MERALCO* as discussed in Note 6 – *Discontinued Operations*.

The Management Committee monitors the operating results of each business unit separately for the purpose of determining resource allocation and assessing performance. Performance is evaluated based on (i) net income for the year, (ii) consolidated core earnings before interest, taxes, and depreciation and amortization or consolidated core *EBITDA*; and (iii) consolidated core net income or *CCNI*. Net income for the year is measured consistent with reported consolidated net income in the consolidated financial statements.

Core *EBITDA* is measured as *CCNI* excluding depreciation and amortization, interest and other financial charges, interest and other financial income, equity in net earnings or losses of associates and joint ventures and provision for income tax.

CCNI for the year is measured as consolidated net income attributable to equity holders of the parent adjusted for foreign exchange gain or loss, mark-to-market gain or loss, impairment or reversal of impairment of noncurrent assets and other non-recurring gain or loss, if any, net of tax effect of the foregoing adjustments.

Billings between operating segments are done on an arm’s-length basis in a manner similar to transactions with third parties. Segment revenues, segment expenses and segment results include transfers among business segments. Those transfers are eliminated upon consolidation.



The *MERALCO Group* operates and generates substantially all of its revenues in the Philippines (i.e., one geographical location). Thus, geographical segment information is not presented. The *MERALCO Group* has no revenues from transactions with a single external customer accounting for 10% or more of its revenues from external customers.

Note	Power		Other Services		Inter-segment Transactions			Total	
	2013	2012*	2011*	2013	2012*	2011*	2013	2012*	2011*

The inter-segment revenues mainly represent revenues of other services segment earned from the power segment.



The following table shows the reconciliation of the consolidated *EBITDA* to net income:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Consolidated <i>EBITDA</i>	₱30,682	₱27,690	₱24,649
<i>EBITDA</i> of discontinued operations	–	(1,154)	(1,262)
<i>EBITDA</i> of continuing operations	30,682	26,536	23,387
Depreciation and amortization	(6,118)	(5,576)	(5,504)
Interest and other financial income	1,172	2,569	2,264
Interest and other financial charges	(1,479)	(1,528)	(1,445)
Equity in net earnings (losses) of associates and joint ventures	(259)	(15)	67
Derivative mark-to-market gain (loss)	(24)	40	(16)
Foreign exchange gain (loss)	353	(4)	(7)
Consolidated income before income tax	24,327	22,022	18,746
Provision for income tax	(7,054)	(5,741)	(5,953)
Net income from continuing operations	17,273	16,281	12,793
Income from discontinued operations, net of income tax	–	978	966
Net income	₱17,273	₱17,259	₱13,759

The following table shows the reconciliation of the *CCNI* to the net income:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
<i>CCNI</i>	₱17,023	₱16,265	₱14,887
Add (deduct) non-core items, net of tax:			
Foreign exchange gain (loss)	366	(1)	(2)
Investment acquisition transaction costs	(156)	–	–
Mark-to-market gain (loss)	(17)	28	(12)
Gain (loss) on sale of investment properties	(5)	–	17
Gain on divestment from <i>Rockwell Land</i>	–	780	–
Non-core expense	–	(56)	(1,568)
Effect of revised <i>PAS 19</i>	–	101	33
Day “1” loss of advance payments to a supplier	–	–	(95)
Net income for the year attributable to equity holders of the Parent	17,211	17,117	13,260
Net income for the year attributable to non-controlling interests	62	142	499
Net income	₱17,273	₱17,259	₱13,759



A significant portion of *MERALCO*'s and *CEDC*'s utility plant and others are purchased from foreign suppliers. Such transactions are concluded in currencies other than the Philippine peso, principally, the *U.S.* dollar. *MERALCO* and *CEDC* record the assets and liabilities in Philippine peso using the exchange rate at the date of the transaction. The outstanding amount of foreign currency-denominated liabilities is restated at each reporting date.

Construction in progress mainly pertains to on-going electric capital projects or *ECPs* and non-electric capital projects or *NEPs*. *ECPs* are capital projects involving construction of new electric distribution-related facilities and the upgrade and major rehabilitation of existing electrical facilities. Total interest capitalized amounted to ₱122 million, ₱127 million and ₱82 million for the years ended December 31, 2013, 2012 and 2011, respectively.

The average annual interest rates used for capitalization in 2013, 2012 and 2011 ranged from 4.6% to 5.9%, 5.5% to 6.2% and 5.3% to 6.2%, respectively.

9. Investments in Associates and Joint Ventures

This account consists of the following as at December 31, 2013 and 2012:

	Place of Incorporation	Principal Activity	2013 Percentage of Ownership	2012
Associates				
<i>RP Energy</i>	Philippines	Power generation	47	47
<i>FPM Power Holdings Limited or FPM Power</i>	British Virgin Islands	Power generation	40	–
<i>Bauang Private Power Corporation or BPPC</i>	Philippines	Power generation	38	38
<i>General Electric Philippines Meter and Instrument Company, Inc. or GEPMICI</i>	Philippines	Sale of metering products and services	35	35
<i>GBPC</i>	Philippines	Power generation	20	–
Joint Ventures				
<i>SBPL</i>	Philippines	Power generation	51	–
<i>Indra Philippines</i>	Philippines	Management and information technology, or IT, consultancy	50	50
<i>Rockwell Business Center</i>	Philippines	Real estate	30	30

The movements in investments in associates and joint ventures account are as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Acquisition costs:		
Balance at beginning of year	₱1,563	₱538
Additions	11,898	1,025
Balance at end of year	13,461	1,563
Accumulated equity in net earnings (losses):		
Balance at beginning of year	249	294
Equity in net losses	(259)	(15)
Dividends	(411)	(30)
Balance at end of year	(421)	249
Share in cumulative translation adjustments of associates:		
Balance at beginning of year	3	12
Translation adjustments	379	(9)
Balance at end of year	382	3
	₱13,422	₱1,815



The additions of ₱1,025 million in 2012 include ₱827 million investment in Rockwell Business Center.

FPM Power

FPM Power is 40%-owned by *MERALCO* through *MPG Asia Limited*, a subsidiary of *MGen*, and 60% owned by *First Pacific*. On March 28, 2013, *FPM Power* acquired a 70% interest in *PacificLight Power*, which owns and operates a 2 x 400 MW liquefied natural gas or *LNG*-fired power plant in Jurong Island, Singapore. *PacificLight Power*'s wholly owned subsidiary, *PacificLight Energy Pte. Ltd.*, is engaged in energy trading.

RP Energy

On July 22, 2011, *MGen* signed a Shareholders' Agreement with *Therma Power, Inc.* or *TPI*, and *Taiwan Cogeneration International Corporation – Philippine Branch* or *TCIC*, for the construction and operation of a 2 x 300 MW *CFB* independent, coal-fired power plant to be located in the Subic Bay Freeport Zone. *RP Energy* is a partnership among *TPI*, *MGen* and *TCIC*.

As at March 17, 2014, site preparation work is almost complete and *RP Energy* has commissioned its contractor to conduct preliminary engineering works on the power plant in order to reduce the overall construction period. The Department of Environment and Natural Resources or *DENR*, has issued the Environmental Compliance Certificate or *ECC* for the 2 x 300 MW coal-fired power plant following a rigorous review and public consultation process.

A Writ of Kalikasan was filed with the *SC* by certain parties opposing the *RP Energy* project. The case was remanded by the *SC* to the *CA* for hearing on the merits thereof. A decision has been issued by the *CA* denying the Writ of Kalikasan, but noting certain deficiencies in the process of the *DENR* in its issuance of the original *ECC* for the 300 MW coal-fired power plant and in the process of the Subic Bay Metropolitan Authority or *SBMA* in the conclusion of the original Lease and Development Agreement or *LDA* with *RP Energy*, and declaring these invalid. *DENR*, *SBMA* and *RP Energy* have filed their respective Motions to the *SC* for review the *CA* decision. On December 19, 2013, *RP Energy* filed a manifestation and Motion requesting that the *SC* deem the petitioners to have waived their rights to file their comments and requested that *RP Energy*'s Petition for Review of Certiorari which was filed with the *SC* on July 17, 2013, be submitted for resolution without the need for further submissions. As at March 17, 2014, no resolution has been issued by the *SC*. Meanwhile, *RP Energy* is proceeding with certain development activities that are not hampered by the *SC* proceedings.

While the original *LDA* was declared invalid by the *CA*, the *SBMA* is also set to ratify an Amended and Restated *LDA* to reflect additional terms.

SBPL

On August 29, 2013, *MGen* signed a Joint Development Agreement with *New Growth B.V.*, a 100% subsidiary of *Electricity Generating Public Company Limited* of Thailand or *EGCO*, for the development of a new 460 MW (net) supercritical coal-fired power plant in Mauban, Quezon. *MGen*'s equity in the joint venture company, *SBPL*, is 51%, with the option to assign or transfer 2% thereof to a party or investor of its preference. *SBPL*, together with their consultants are evaluating the Engineering, Procurement and Construction or *EPC*, tenders and is expected to award the same by the second quarter of 2014. Simultaneously with its financial advisors, *SBPL* is in discussions with several banks for the financing of the project. A *PSA* is currently being negotiated between the



representatives of *EGCO* and *MERALCO*, with the intent of submitting the same to the *ERC* for approval.

GBPC

On October 7, 2013, *MGen* executed a Share Sale and Purchase Agreement with First Metro Investment Corporation or *FMIC*, and signed a Shareholders Agreement on October 22, 2013, for the sale by *FMIC* of a 20% equity interest in *GBPC* to *MGen*. *GBPC* owns an aggregate of 627 *MW* (gross) capacity of combined coal and diesel power plants in operation in the Visayas region. An 82 *MW* (gross) coal power plant in Cebu and a 150 *MW* (gross) coal power plant in Panay are under construction and are expected to be in commercial operation by late 2014.

BPPC

BPPC was organized in October 1992 to engage in the power generation business.

In accordance with the Build-Operate-Transfer or *BOT*, Agreement signed in 1993, First Private Power Corporation or *FPPC*, then parent company, constructed the 215 *MW* Bauang Power Plant or *Bauang Plant*, and operated the same under a 15-year Cooperation Period up to July 25, 2010.

The *Bauang Plant* has since been turned over to the National Power Corporation or *NPC*, without any compensation and free of any liens. Thereafter, *FPPC* and *BPPC* were legally merged, with *BPPC* as the surviving entity. *BPPC* is in the process of winding down operations.

GEPMICI

GEPMICI was established in 1979 together with General Electric Company of U.S.A., to serve the Philippine market for ANSI-type Watt-hour meters.

Indra Philippines

Indra Philippines is an *IT* service provider in the country and in the Asia Pacific region, with a wide range of services across various industries. *Indra Philippines* supports *MERALCO*'s information technology requirements in the area of system development, outsourcing of *IS* and *IT* operations and management consulting.

Rockwell Business Center

The Rockwell Business Center is a joint venture between *Rockwell Land* and *MERALCO*, where *Rockwell Land* shall construct three (3) Business Process Outsourcing or *BPO*, enabled buildings in a non-regulatory asset base property of *MERALCO* over a pre-agreed cooperation period. Investment in Rockwell Business Center represents *MERALCO*'s 30% interest in the joint venture, accounted for using the equity method. *Rockwell Land* owns 70% interest in Rockwell Business Center.

MERALCO and *Rockwell Land* share in earnings before depreciation and amortization at 80% and 20%, respectively until 2014 or until certain operational indicators are reached, whichever comes first. Sharing of depreciation and amortization is proportionate to their contribution.



The carrying values of investments in associates and joint ventures follow:

	2013	2012
	<i>(Amounts in millions)</i>	
<i>GBPC</i>	₱6,820	₱—
<i>FPM Power</i>	4,522	—
<i>Rockwell Business Center</i>	917	847
<i>RP Energy</i>	660	648
<i>Indra Philippines</i>	291	253
<i>SBPL</i>	140	—
<i>GEPMICI</i>	62	58
<i>BPPC</i>	10	9
	₱13,422	₱1,815

The condensed statements of financial position of material associates follow:

	2013			2012
	<i>GBPC</i>	<i>FPM Power</i>	<i>RP Energy</i>	<i>RP Energy</i>
	<i>(Amounts in millions)</i>			
Current assets	₱17,276	₱4,901	₱323	₱612
Noncurrent assets	42,599	48,052	1,055	723
Current liabilities	(10,763)	(14,245)	(80)	(63)
Noncurrent liabilities	(25,369)	(26,070)	(1)	—
Non-controlling interests	(4,002)	(1,333)	—	—
Total net assets	₱19,741	₱11,305	₱1,297	₱1,272

The condensed statements of comprehensive income of material associates are as follows:

	2013			2012	2011
	<i>GBPC</i>	<i>FPM Power</i>	<i>RP Energy</i>	<i>RP Energy</i>	<i>RP Energy</i>
	<i>(Amounts in millions)</i>				
Revenues	₱2,824	₱262	₱11	₱8	₱—
Costs and expenses	(2,329)	(1,212)	(191)	(149)	(39)
Net income (loss)	495	(950)	(180)	(141)	(39)
Non-controlling interests	(172)	82	—	—	—
Net income attributable to equity holders of the parent	323	(868)	(180)	(141)	(39)
Other comprehensive income	—	378	—	—	—
Total comprehensive income (loss)	₱323	(₱490)	(₱180)	(₱141)	(₱39)
Dividends received	₱400	₱—	₱—	₱—	₱—



The reconciliation of the net assets of the foregoing material associates to the carrying amounts of the interest in these associates recognized in the consolidated statements of financial position is as follows:

	2013			2012
	<i>GBPC</i>	<i>FPM Power</i>	<i>RP Energy</i>	<i>RP Energy</i>
	(Amounts in millions)			
Net assets of associates	₱19,741	₱11,305	₱1,297	₱1,272
Proportionate ownership in associates in %	20	40	47	47
	3,948	4,522	610	598
Goodwill	2,872	—	50	50
	₱6,820	₱4,522	₱660	₱648

The following is the aggregate information of *GEPMICI* and *BPPC* that are not individually material:

	2013	2012	2011
	(Amounts in millions)		
Share in net income (loss)	₱4	₱1	(₱41)
Share in other comprehensive income	1	—	—
Share in total comprehensive income (loss)	₱5	₱1	(₱41)

Joint Ventures

The condensed statements of financial position of Rockwell Business Center, a material joint venture, follow:

	2013	2012
	(Amounts in millions)	
Current assets	₱613	₱465
Noncurrent assets	2,566	2,586
Current liabilities	(166)	(139)
Noncurrent liabilities	(7)	(8)
Net assets	₱3,006	₱2,904

Current assets include cash and cash equivalents of ₱594 million and ₱372 million as at December 31, 2013 and 2012, respectively. Noncurrent assets represent substantially the two (2) *BPO* towers for lease and the costs of ongoing construction of the third building of Rockwell Business Center. Current liabilities represent trade payables.

The condensed statements of comprehensive income of Rockwell Business Center for the years ended December 31, 2013, 2012 and 2011 are as follows:

	2013	2012	2011
	(Amounts in millions)		
Revenues	₱301	₱226	₱224
Costs and expenses	(142)	(98)	(104)
Provision for income tax	(57)	(44)	(44)
Net income	102	84	76
Other comprehensive income	—	—	—
Total comprehensive income	₱102	₱84	₱76



The foregoing condensed statements of comprehensive income include the following:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Depreciation	₱136	₱96	₱101
Interest income	(6)	(6)	(7)

The reconciliation of the net assets of the Rockwell Business Center to the carrying amount of the interest in Rockwell Business Center recognized in the consolidated financial statements is as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Net assets	₱3,006	₱2,904
Proportionate ownership in %	30	30
	902	871
Effect of the difference between <i>MERALCO</i> 's percentage share in net income and proportionate ownership	15	(24)
	₱917	₱847

The following is the condensed financial information of *Indra Philippines* and *SBPL*, which are not considered material joint ventures:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Share in net income	₱125	₱34	₱14
Share in other comprehensive income	—	—	—
Share in total comprehensive income	₱125	₱34	₱14
Dividends received	₱11	₱—	₱—

10. Investment Properties

The movements in investment properties are as follows:

	2013		
	Land	Buildings and Improvements	Total
	<i>(Amounts in millions)</i>		
Cost:			
Balance at beginning of year	₱1,535	₱206	₱1,741
Disposals	(89)	(25)	(114)
Balance at end of year	1,446	181	1,627
Less accumulated depreciation:			
Balance at beginning of year	—	107	107
Depreciation	—	8	8
Disposals	—	(14)	(14)
Balance at end of year	—	101	101
	₱1,446	₱80	₱1,526



	2012		
	Land	Buildings and Improvements	Total
	<i>(Amounts in millions)</i>		
Cost	₱1,535	₱206	₱1,741
Less accumulated depreciation:			
Balance at beginning of year	—	99	99
Depreciation	—	8	8
Balance at end of year	—	107	107
	₱1,535	₱99	₱1,634

Investment properties are stated at cost. These consist of real properties held for capital appreciation, former substation sites and other non-regulatory asset base real properties, some of which are being leased out.

The aggregate fair values of the investment properties as at December 31, 2013 and 2012 are as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Land	₱1,863	₱1,853
Buildings and improvements	131	173

Land pertains primarily to properties where the *BPO* building and “Strip” mall are located and other non-regulated asset base properties.

The fair values of investment properties were determined by independent, professionally qualified appraisers. The fair value represents the price that would be received to sell an investment property in an orderly transaction between market participants at the measurement date.

The fair value disclosures of the investment properties are categorized as Level 3 as there is no active market for identical or similar properties. The inputs include price per square meter ranging from ₱500 to ₱94,000. There have been no changes in the valuation techniques used.

In conducting the appraisal, the independent professional appraisers used any of the following approaches:

a. Market Data or Comparative Approach

Under this approach, the value of the property is based on sales and listings of comparable property registered within the vicinity. This approach requires the establishment of a comparable property by reducing comparative sales and listings to a common denominator with the subject. This is done by adjusting the differences between the subject property and those actual sales and listings regarded as comparables. The properties used are either situated within the immediate vicinity or at different floor levels of the same building, whichever is most appropriate to the property being valued. Comparison was premised on the factors of location, size and physical attributes, selling terms, facilities offered and time element.



b. Depreciated Replacement Cost Approach

This method of valuation considers the cost to reproduce or replace in new condition the assets appraised in accordance with current market prices for similar assets, with allowance for accrued depreciation based on physical wear and tear and obsolescence.

11. Other Noncurrent Assets

This account consists of:

	Note	2013	2012
		(Amounts in millions)	
Unbilled receivables	13	₱18,394	₱4,954
Intangible assets	8	1,728	1,021
Deferred input VAT		1,702	1,148
Receivable from the BIR	30	577	577
Advance payments to a supplier	31	474	325
Deferred reinsurance premium		231	209
AFS financial assets	28	161	331
HTM investments		129	123
Goodwill		36	36
Others		171	113
		₱23,603	₱8,837

Unbilled Receivables

This account represents generation and other pass-through costs incurred by MERALCO and CEDC as DUs, which are still to be billed and which are covered by the approved recovery mechanism of the ERC. The balance also includes other unbilled generation and pass-through charges of current and prior periods, which are the subject of various applications for recovery and approval by the ERC.

Intangible Assets

The movements of intangible assets are as follows:

	2013		
	Software	Franchise	Total
	(Amounts in millions)		
Cost:			
Balance at beginning of year	₱1,525	₱49	₱1,574
Additions	876	—	876
Balance at end of year	2,401	49	2,450
Less accumulated amortization:			
Balance at beginning of year	553	—	553
Amortization	169	—	169
Balance at end of year	722	—	722
	₱1,679	₱49	₱1,728



		2012	
	Note	Software	Franchise
		(Amounts in millions)	
Cost:			
Balance at beginning of year		₱734	₱49
Additions		315	—
Reclassification	8	476	—
Balance at end of year		1,525	49
Less accumulated amortization:			
Balance at beginning of year		94	—
Amortization		94	—
Reclassification	8	365	—
Balance at end of year		553	—
		₱972	₱49
			₱1,021

12. Cash and Cash Equivalents

This account consists of:

	2013	2012
	(Amounts in millions)	
Cash on hand and in banks	₱5,129	₱3,256
Cash equivalents	54,722	57,244
	₱59,851	₱60,500

Cash in banks earns interest at prevailing bank deposit rates. Cash equivalents are temporary cash investments, which are made for varying periods up to three (3) months depending on the *MERALCO Group's* immediate cash requirements, and earn interest at the prevailing short-term investment rates.

13. Trade and Other Receivables

This account consists of:

	Note	2013	2012
		(Amounts in millions)	
Trade:			
Electricity:			
Billed		₱27,281	₱23,338
Unbilled	11	4,175	4,630
Service contracts		1,490	816
Insurance receivable		453	383
Cost and estimated earnings in excess of billings on uncompleted contracts		455	258
Nontrade		2,016	1,358
		35,870	30,783
Less allowance for doubtful accounts		3,152	2,706
		₱32,718	₱28,077



Billed receivables from sale of electricity of *MERALCO* and *CEDC* consist of the following:

	2013	2012
	<i>(Amounts in millions)</i>	
Commercial	₱12,179	₱10,688
Residential	9,446	6,184
Industrial	5,128	6,094
Flat streetlights	528	372
	27,281	23,338
Less allowance for doubtful accounts	2,969	2,559
	₱24,312	₱20,779

Movements in allowance for doubtful accounts for trade and other receivables are as follows:

	2013			
	Balance at beginning of year	Provisions (Reversals)	Write-offs	Balance at end of year
	<i>(Amounts in millions)</i>			
Billed trade receivables:				
Commercial	₱1,028	₱175	(₱38)	₱1,165
Residential	556	743	(231)	1,068
Industrial	772	(201)	(38)	533
Flat streetlights	203	5	(5)	203
	2,559	722	(312)	2,969
Nontrade receivables	147	36	–	183
	₱2,706	₱758	(₱312)	₱3,152

	2013				
	Commercial	Residential	Industrial	Flat Streetlights	Nontrade Receivables
	<i>(Amounts in millions)</i>				
Individually impaired	₱123	₱763	₱298	₱31	₱183
Collectively impaired	1,042	305	235	172	–
	₱1,165	₱1,068	₱533	₱203	₱183

	2012			
	Balance at beginning of year	Provisions (Reversals)	Write-offs	Balance at end of year
	<i>(Amounts in millions)</i>			
Billed trade receivables:				
Commercial	₱911	₱159	(₱42)	₱1,028
Residential	528	272	(244)	556
Industrial	74	702	(4)	772
Flat streetlights	439	(139)	(97)	203
	1,952	994	(387)	2,559
Nontrade receivables	180	12	(45)	147
	₱2,132	₱1,006	(₱432)	₱2,706



2012						
	Commercial	Residential	Industrial	Flat Streetlights	Nontrade Receivables	Total
<i>(Amounts in millions)</i>						
Individually impaired	₱142	₱345	₱207	₱64	₱147	₱905
Collectively impaired	886	211	565	139	—	1,801
	₱1,028	₱556	₱772	₱203	₱147	₱2,706

Trade Receivables – Electricity

Trade receivables of *MERALCO* and *CEDC* include charges for pass-through costs. Pass-through costs consist largely of generation and transmission charges, which represent 57% and 9%, respectively, of the total billed amount in 2013 and 58% and 10%, respectively, of the total billed amount in 2012. Billed receivables are due 10 days after bill date.

Unbilled receivables represent electricity consumed after the meter reading cut-off dates, which will be billed to customers in the immediately following billing period. This also includes the current portion of pass-through cost under-recoveries, net of over-recoveries, which are billed to the customers over the period approved by the *ERC*. *MERALCO*'s and *CEDC*'s trade receivables are noninterest-bearing and are substantially secured by bill deposits.

See *Note 19 – Customers' Deposits* and *Note 28 – Financial Assets and Financial Liabilities*.

Trade Receivables – Service Contracts

Service contracts receivables arise from contracts entered into by *MIESCOR* and subsidiaries, *e-MVI* and subsidiary, *CIS*, *Bayad Center*, *Miescorrail* and *MEI* for construction, engineering, related manpower, consulting, light rail maintenance, data transport, bills collection, tellering and e-business development and energy management services to third parties.

Receivables from service contracts and others are noninterest-bearing and are generally on 30- to 60-day terms.

14. Inventories

	2013	2012
<i>(Amounts in millions)</i>		
Materials and supplies:		
At net realizable value	₱2,750	₱1,371
At cost	2,953	1,578
Total inventories at the lower of cost or net realizable value	₱2,750	₱1,371



15. Other Current Assets

	Note	2013	2012
<i>(Amounts in millions)</i>			
Advances to an associate	9 and 24	₱4,884	₱—
Short-term investments	19 and 28	4,841	—
Pass-through VAT - net		1,116	1,389
Prepaid tax		734	475
Prepaid expenses		290	60
Creditable withholding tax		99	127
Input VAT		77	47
Derivative assets	28	—	24
Others		126	173
		₱12,167	₱2,295

Pass-through VAT pertains to VAT on generation and transmission costs, as DU. Remittance of such deferred VAT to the generation companies is based on collection of billed receivables from the customers.

Short-term investments are temporary cash placements which are made for varying periods beyond three (3) months but not exceeding 12 months, and earn interest at the prevailing short-term placement investment rates.

16. Equity

Common Stock

The movement in the number of shares of MERALCO's common stock is as follows:

	2013	2012
<i>(In millions, except par value)</i>		
Authorized - ₱10 par value a share	1,250	1,250
Issued and outstanding:		
Balance at beginning and end of year	1,127	1,127

The common shares of MERALCO were listed in the PSE on January 8, 1992. There are 46,409 and 47,892 shareholders of MERALCO's common shares as at December 31, 2013 and 2012, respectively.

Unappropriated Retained Earnings

The unappropriated retained earnings include undeclared accumulated earnings of subsidiaries, associates and joint ventures, and the balance of MERALCO's revaluation increment in utility plant and others and investment properties carried at deemed cost, deferred tax assets and derivative assets amounting to ₱34,684 million and ₱33,019 million as at December 31, 2013 and 2012, respectively. These amounts are restricted for dividend declaration purposes as of the close of the respective reporting periods.



The following are cash dividends declared on common shares in 2013 and 2012:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount (In millions)
July 29, 2013	August 27, 2013	September 20, 2013	₱4.10	₱4,621
February 25, 2013	March 26, 2013	April 24, 2013	6.10	6,875
July 30, 2012	August 29, 2012	September 24, 2012	4.00	4,508
February 27, 2012	March 23, 2012	April 23, 2012	4.10	4,621

MERALCO pays regular cash dividends equivalent to 50% of consolidated core net income for the year, which may be supplemented by a special dividend determined on a “look-back” basis. Declaration and payment of special dividend are dependent on the availability of unrestricted retained earnings and availability of free cash. The declaration, record and payment dates shall be consistent with the guidelines and regulations of the *SEC*.

Appropriated Retained Earnings

On February 22, 2010, retained earnings of ₱6,000 million have been appropriated specifically for the *MERALCO Group*’s business expansion into power generation. The amount appropriated was increased by ₱5,000 million to cover the new development projects and investments in power generation initiatives. The additional appropriation was approved on March 22, 2013 by the *BOD*. As at March 17, 2014, the development of the first project, a 2 x 300 *MW CFB* coal-fired plant through *RP Energy*, is ongoing. *MERALCO* signed a Joint Development Agreement and Shareholders Agreement to develop a supercritical coal-fired power plant, which has a target completion by the end of 2017.

The commercial operations date of the 600 *MW* power plant of *RP Energy* is dependent on the *SC* decision on the appeal filed by *RP Energy* and other parties in connection with the decision reached by the *CA* on the Writ of *Kalikasan* case filed against the *RP Energy* project. On the other hand, the 2 x 400 *MW LNG* plant of *PacificLight Power* was fully synchronized to the Singapore power grid in January 2014.

See Note 9 – *Investments in Associates and Joint Ventures*.

Treasury Shares

Treasury shares represent subscribed shares and the related rights of employees who have opted to withdraw from the *ESPP* in accordance with the provisions of the *ESPP* and which *MERALCO* purchased. For the years ended December 31, 2013 and 2012, a total of 559 shares and 25,830 shares, respectively, were acquired from employees who have opted to cancel their participation in the *ESPP*.



17. Employee Stock Purchase Plan

MERALCO has an *ESPP*, which entitles participants to purchase *MERALCO*'s common shares subject to certain terms and conditions during a nominated offer period. Movements in the number of common shares subscribed by employees under the *ESPP* are as follows:

	2013			
	13 th	13 th A	14 th	Total
Balance at beginning of year	3,309	135,703	7,753,272	7,892,284
Fully paid	(3,309)	(67,370)	(2,045,911)	(2,116,590)
Cancelled	—	—	(559)	(559)
Balance at end of year	—	68,333	5,706,802	5,775,135

	2012			
	13 th	13 th A	14 th	Total
Balance at beginning of year	1,189,306	389,355	12,284,290	13,862,951
Fully paid	(1,185,997)	(251,747)	(4,507,093)	(5,944,837)
Cancelled	—	(1,905)	(23,925)	(25,830)
Balance at end of year	3,309	135,703	7,753,272	7,892,284

MERALCO allotted a total of 55 million common shares for *ESPP* awards. As at December 31, 2013, 12 million common shares are available for future offerings. There were no other *ESPP* awards since October 2009.

The fair value of the offerings was estimated at the dates of the grant using the Black-Scholes Option Pricing Model.

Total expense arising from the employee stock purchase plan is nil, ₱134 million and ₱172 million for the years ended December 31, 2013, 2012 and 2011, respectively.

See Note 26 – *Expenses and Income*.

18. Interest-bearing Long-term Financial Liabilities

This account consists of the following:

	2013	2012
	(Amounts in millions)	
Long-term portion of interest-bearing financial liabilities -		
Long-term debt	₱20,756	₱20,466
Current portion of interest-bearing financial liabilities:		
Long-term debt	9,459	766
Redeemable preferred stock	1,562	1,594
	11,021	2,360
	₱31,777	₱22,826

All of the redeemable preferred shares have been called for redemption as at June 30, 2011, consistent with the terms of the Preferred Shares Subscription Agreement. The accrued interests amounted to ₱250 million and ₱256 million as at December 31, 2013 and December 31, 2012, respectively. Interest is no longer accrued when the preferred shares have been called for redemption.



The details of interest-bearing long-term financial liabilities are as follows:

Description	2013	2012
	<i>(Amounts in millions)</i>	
<i>Bonds</i>		
₱11.5 Billion 7-year Bonds	₱11,500	₱—
₱7.0 Billion 12-year Bonds	7,000	—
<i>Fixed Rate Loans</i>		
₱5.0 Billion Note Facility Agreement	4,900	4,950
₱4.8 Billion Note Facility Agreement	3,417	4,776
₱3.0 Billion Note Facility Agreement	530	3,000
₱5.0 Billion Note Facility Agreement	—	4,900
<i>Floating Rate Loans</i>		
₱2.5 Billion Term Loan Facility	2,475	2,488
₱3.0 Billion Term Loan Facility	600	1,200
Total long-term debt	30,422	21,314
Less unamortized debt issuance costs	207	82
	30,215	21,232
<i>Redeemable Preferred Stock</i>	1,562	1,594
	31,777	22,826
Less current portion	11,021	2,360
Long-term portion of interest-bearing financial liabilities	₱20,756	₱20,466

All of *MERALCO*'s interest-bearing long-term financial liabilities as at December 31, 2013 and 2012 are denominated in Philippine pesos. The scheduled maturities of *MERALCO*'s outstanding long-term debt at nominal values as at December 31, 2013 are as follows:

	Amount
	<i>(In millions)</i>
December 31, 2014	₱9,459
December 31, 2015	13
December 31, 2016	12
December 31, 2017	12
After December 31, 2017	20,926
	₱30,422

Bonds

₱18.5 Billion Fixed Rate Putable Bonds

On September 23, 2013, the *BOD* of *MERALCO* authorized the offer, sale and issuance by way of public offering in the Philippines, 7- and 12-year corporate bonds, putable in 5 and 10 years, respectively, with an aggregate principal amount of up to ₱15 billion with an overallotment option of up to ₱5.0 billion. The 12-year corporate bonds also include a call option, where *MERALCO* may redeem (in whole but not in part only) the outstanding bonds on the 7th year from issue date at the early redemption price of 101.0%. The put and call options are clearly and closely related to the host instruments, thus, were not recognized separately.

On December 12, 2013, the ₱11.5 Billion Fixed Rate Putable Bonds due in 2020 and ₱7.0 Billion Fixed Rate Putable Bonds due in 2025, were listed on the Philippine Dealing and Exchange Corporation.



The net proceeds of the bonds will be utilized for refinancing certain loans including principal payments, accrued interest, prepayment penalties and other financing costs.

Fixed Rate Loans

₱5.0 Billion Note Facility Agreement

In June 2011, *MERALCO* entered into a Fixed Rate Note Facility Agreement for its ₱500 million, 7-year notes and ₱4,500 million, 10-year notes due in 2018 and 2021, respectively. The principal is payable in nominal annual amortizations with a balloon payment on each of the two final maturity dates.

₱4.8 Billion Note Facility Agreement

In November 2010, *MERALCO* signed a Fixed Rate Note Facility Agreement for its ₱1,997 million, 7-year fixed rate notes and ₱2,803 million, 10-year fixed rate notes. The notes were issued on December 2, 2010 and are payable in nominal annual amortizations with a balloon payment on each of the two maturity dates in December 2018 and December 2020.

In December 2013, *MERALCO* pre-terminated and settled the principal amount of ₱1,334 million. In January 2014, *MERALCO* pre-terminated and settled the remaining principal of ₱3,417 million.

₱3.0 Billion Note Facility Agreement

On January 5, 2012, *MERALCO* signed a ₱3,000 million Fixed Rate Note Facility Agreement for its ₱1,000 million, 7-year notes and ₱2,000 million, 10-year notes due in 2019 and 2022, respectively. The notes were priced off the relevant 7-year and 10-year benchmarks plus a spread and were issued on January 9, 2012. Principal repayments are through annual nominal amortizations and a balloon payment on maturity date. In December 2013, *MERALCO* pre-terminated and settled the principal amount of ₱2,440 million. In March 2014, *MERALCO* pre-terminated and settled the remaining principal of ₱530 million.

₱5.0 Billion Note Facility Agreement

In December 2010, *MERALCO* entered into a Fixed Rate Note Facility Agreement for the issuance of ₱23 million, 5-year fixed rate notes maturing in December 2015 and ₱4,977 million, 5.5-year fixed rate notes due in June 2016. The 5-year fixed rate notes are payable in full at maturity date while the 5.5-year fixed rate notes are payable in nominal annual amortizations with a balloon payment on maturity date. In December 2013, *MERALCO* pre-terminated and settled the entire principal amount of ₱4,900 million.

Floating Rate Loans

₱2.5 Billion Term Loan Facility

The ₱2,500 million, 7-year Floating Rate Term Loan Facility, was drawn in January 2011 from a local bank. Interest rate is repriced every six months based on 6-month *PDST-F* plus a spread. The principal is payable in nominal annual amortizations with a balloon payment on final maturity in January 2018.

₱3.0 Billion Term Loan Facility

The ₱3,000 million, 5-year bilateral Floating Rate Term Loan Facility, was drawn in October 2009. The principal is payable over five years with final maturity in October 2014.



Long-term debt totaling ₱3,947 million, pre-terminated between January to March 17, 2014 and ₱4,850 million to be pre-terminated in June 2014, were classified as part of the current portion of the long-term interest-bearing financial liabilities as at December 31, 2013.

The annual interest rates for the interest-bearing financial liabilities are as follows:

	2013	2012
Bonds	4.38% to 4.88%	—
Fixed Rate Loans	5.23% to 6.89%	5.23% to 7.47%
Floating Rate Loans	0.80% to 1.74%	2.63% to 2.99%

Debt Covenants

MERALCO's loan agreements require compliance with debt service coverage of 1.2 times calculated on specific measurement dates. The agreements also contain restrictions with respect to the creation of liens or encumbrances on assets, issuance of guarantees, mergers or consolidations, disposition of a significant portion of its assets and related party transactions.

As at December 31, 2013 and 2012, MERALCO is in compliance with all covenants of the loan agreements.

Unamortized Debt Issuance Costs

Unamortized debt issuance costs amounted to ₱207 million and ₱82 million as at December 31, 2013 and 2012, respectively.

The following presents the changes to the unamortized debt issuance costs:

	Note	2013	2012
		(Amounts in millions)	
Balance at beginning of year		₱82	₱97
Additions		186	22
Amortization charged to interest and other financial charges	26	(61)	(37)
Balance at end of year		₱207	₱82

Redeemable Preferred Stock

The movements in the number of shares of the redeemable preferred stock, which have all been called, are as follows:

	2013	2012
Balance at beginning of year	159,356,939	165,129,647
Redemptions	(3,167,771)	(5,772,708)
Balance at end of year	156,189,168	159,356,939

The original "Terms and Conditions" of MERALCO's Special Stock Subscription Agreement, which required an applicant to subscribe to preferred stock with 10% dividend to cover the cost of extension of, or new distribution facilities, have been amended by the *Magna Carta* and the Distribution Services and Open Access Rule, or *DSOAR*, effective June 17, 2004 and January 18, 2006, respectively. The amendment sets forth the guidelines for the issuance of preferred stock, only if such instrument is available.



19. Customers' Deposits

This account consists of:

	2013			2012		
	Current Portion (see Note 23)	Noncurrent Portion	Total	Current Portion (see Note 23)	Noncurrent Portion	Total
(Amounts in millions)						
Bill deposits	₱6,130	₱21,600	₱27,730	₱4,064	₱23,313	₱27,377
Meter deposits	2,119	–	2,119	2,188	–	2,188
	₱8,249	₱21,600	₱29,849	₱6,252	₱23,313	₱29,565

Bill Deposits

Bill deposits serve to guarantee payment of bills by a customer in accordance with existing regulations.

As provided for under the *Magna Carta* and *DSOAR*, all captive customers are required to pay a deposit to the *DU* an amount equivalent to the estimated monthly bill calculated based on applied load, which shall be recognized as bill deposit of the captive customer. Such deposit shall be adjusted after one year based on the historical 12-month average bill. A captive customer who has paid his electric bills on or before due date for three consecutive years may now apply for the full refund of the bill deposit, together with the accrued interests, prior to the termination of his service; otherwise bill deposits and accrued interests shall be refunded within one month from the termination of service, provided all bills have been paid.

On February 22, 2010, the amended *DSOAR*, which became effective on April 1, 2010, was promulgated by the *ERC*. Under the amended *DSOAR*, interest on bill deposits for both residential and non-residential customers shall be computed using the equivalent peso savings account interest rate of the Land Bank of the Philippines or *Land Bank*, or other government banks, on the first working day of the year, subject to the confirmation of the *ERC*. Interest rate for bill deposits is 0.5% per annum from January 1, 2011 until December 31, 2012 and 0.375% per annum starting January 1, 2013.

As provided for under *ERC* Resolution No. 1, *A Resolution Adopting the Revised Rules for the Issuance of Licenses to Retail Electricity Suppliers*, a local *RES* may require security deposits from its contestable customers, which shall earn interest equivalent to the actual interest earnings of the total amount of deposits received from the customers.

The following are the movements of the bill deposits account:

	2013	2012
(Amounts in millions)		
Balance at beginning of year	₱27,377	₱26,429
Additions	5,068	3,211
Refunds	(4,715)	(2,263)
Balance at end of year	27,730	27,377
Less portion maturing within one year	6,130	4,064
Noncurrent portion of bill deposits and related interests	₱21,600	₱23,313



Meter Deposits

Meter deposits were intended to guarantee the cost of meters installed.

The *Magna Carta* for residential customers (effective June 17, 2004) and *DSOAR* (effective January 18, 2006) for non-residential customers exempt all customer groups from payment of meter deposits beginning July 2004 for residential customers and April 2006 for non-residential customers.

The *ERC* released Resolution No. 8, Series of 2008, otherwise known as “Rules to Govern the Refund of Meter Deposits to Residential and Non-Residential Customers,” or *Rules*, which required the refund of meter deposits from the effectivity of the said *Rules* on July 5, 2008. Under the *Rules*, a customer has the option of receiving his refund in cash, credit to future monthly billings, or as an offset to other due and demandable claims of the *DU* against him.

The total amount of refund shall be equivalent to the meter deposit paid by the customer plus the total accrued interest earned from the time the customer paid the meter deposit until the day prior to the start of refund.

On August 8, 2008, in compliance with the *Rules*, *MERALCO* submitted to the *ERC* an accounting of the total meter deposit principal amount for refund. The actual refund of meter deposits commenced on November 3, 2008.

As at December 31, 2013 and 2012, total meter deposits refunded by *MERALCO* amounted to ₱977 million (inclusive of ₱503 million interest) and ₱908 million (inclusive of ₱466 million interest), respectively.

20. Provisions

Provisions consist of amounts recognized for probable costs, charges and expenses relating to claims against the *MERALCO Group*, among others. The movements follow:

	2013	2012
	<i>(Amounts in millions)</i>	
Balance at beginning of year	₱19,411	₱16,919
Provisions	5,331	2,770
Settlements	(13)	(278)
Balance at end of year	₱24,729	₱19,411

The balance of provisions substantially represents the amounts of claims related to a commercial contract which remains unresolved and local taxes being contested as discussed in Note 30, consistent with the limited disclosure as allowed in *PFRS*.

See Note 30 – *Contingencies and Legal Proceedings*.



21. Customers' Refund

This account represents the balance of the refund related to the *SC* decision promulgated on April 30, 2003, which has not yet been claimed by the customers.

In June 2003, the *ERC*, in the implementation of the *SC* decision, ordered *MERALCO* to refund to its customers an equivalent ₱0.167 per *kWh* for billings made from February 1994 to April 2003.

On February 7, 2011, the *ERC* approved *MERALCO*'s proposal for the extension of the *SC* refund process for five (5) years up to December 31, 2015, in view of difficulties encountered by the customers in meeting the necessary documentation requirements to claim a refund and by *MERALCO* in contacting or locating terminated customers entitled to the refund.

22. Notes Payable

Notes payable represent unsecured interest-bearing working capital loans obtained from various local banks. Annual interest rates ranged from 1.5% to 3.9% in 2013 and 3.9% to 6.5% in 2012 on peso-denominated loans.

Interest expense on notes payable amounted to ₱73 million, ₱5 million and ₱6 million in 2013, 2012 and 2011, respectively.

See Note 26 – *Expenses and Income*.

23. Trade Payables and Other Current Liabilities

This account consists of the following:

	Note	2013	2012
		<i>(Amounts in millions)</i>	
Trade accounts payable	24 and 26	₱43,893	₱23,991
Output <i>VAT</i> - net		5,508	4,580
Accrued expenses:			
Employee benefits		3,659	2,629
Taxes		1,795	2,590
Interest		269	308
Others		876	741
Current portions of:			
Bill deposits and related interests	19	6,130	4,064
Meter deposits and related interests	19	2,119	2,188
Deferred lease income		726	761
Refundable service extension costs		1,615	1,512
Dividends payable on:			
Redeemable preferred stock	18	250	256
Common stock	16	91	1,023
Universal charges payable		1,547	320
Refundable transmission charges		779	180
Reinsurance liability		215	213
Regulatory fees payable		205	204
Other current liabilities		4,215	2,016
		₱73,892	₱47,576



Trade Accounts Payable

Trade accounts payable mainly represent obligations to *NPC/Power Sector Assets and Liabilities Management Corporation* or *PSALM*, power generating companies, *National Grid Corporation of the Philippines* or *NGCP*, and *Philippine Electricity Market Corporation* or *PEMC*, for cost of power purchased and for cost of transmission. In addition, this account includes liabilities due to local and foreign suppliers for purchases of goods and services, which consist of transformers, poles, materials and supplies and, contracted services.

Trade payables are noninterest-bearing and are generally settled within the 15- to 60-day trade term. Other payables are noninterest-bearing and are due within six (6) months from incurrence.

See *Note 24 – Related Party Transactions* and *Note 31 - Significant Contracts and Commitments*.

Refundable Service Extension Costs

Article 14 of the *Magna Carta*, specifically, “Right to Extension of Lines and Facilities,” requires a customer requesting for an extension of lines and facilities beyond 30-meter service distance from the nearest voltage facilities of the *DU* to advance the cost of the project. The amended *DSOAR*, which became effective April 1, 2010 requires such advances from customers to be refunded at the rate of 75% of the distribution revenue generated from the extension lines and facilities until such amounts are fully refunded. The related asset forms part of the rate base only at the time a refund has been paid out. Customer advances are noninterest-bearing.

As at December 31, 2013 and 2012, the noncurrent portion of refundable service extension costs of ₱5,782 million and ₱4,357 million, respectively, is presented as “Refundable Service Extension Costs - net of current portion” account in the consolidated statements of financial position.

24. Related Party Transactions

The following summarizes the total amount of transactions, which have been provided and/or contracted by the *MERALCO Group* to/with related parties for the relevant financial year. The outstanding balances are unsecured, non-interest bearing and settled in cash.

Pole Attachment Contracts with Philippine Long Distance Telephone Company or PLDT

MERALCO has a Pole Attachment Contract with *PLDT* similar to third party pole attachment contracts of *MERALCO* with other telecommunication companies. Under the Pole Attachment Contract, *PLDT* shall use the contacted cable position exclusively for its telecommunication cable network facilities.

Sale of Electricity under Various Service Contracts

MERALCO sells electricity to related party shareholder groups such as *PLDT*, *Metro Pacific*, *JG Summit* and *SMC* and their respective subsidiaries, and affiliates for their facilities within *MERALCO*’s franchise area. The rates charged to related parties are the same *ERC*-mandated rates applicable to customers within the franchise area.



Purchase of Telecommunication Services from PLDT and Subsidiaries

The *MERALCO Group*'s primary telecommunications carriers are *PLDT* for its wireline and *SMART* and *Digitel Mobile Philippines, Inc.*, for its wireless services. Such services are covered by standard service contracts between the telecommunications carriers and each legal entity within the *MERALCO Group*.

Purchase of Goods and Services

In the ordinary course of business, the *MERALCO Group* purchases goods and services from its affiliates and sells power to such affiliates.

Following is the summary of related party transactions for the years ended December 31, 2013, 2012 and 2011 and the outstanding balances as at December 31, 2013 and 2012:

Category	Amount of Transactions			Outstanding Receivable (Liability) as at December 31		Terms	Conditions
	2013	2012	2011	2013	2012		
	<i>(Amounts in millions)</i>						
Sale of electricity:							
<i>PLDT Group</i>	₱2,599	₱2,936	₱2,669	₱160	₱268	10-day; noninterest-bearing	Unsecured, no impairment
<i>SMC Group</i>	851	1,040	945	59	83	10-day; noninterest-bearing	Unsecured, no impairment
<i>Metro Pacific Group</i>	352	1,172	594	15	54	10-day; noninterest-bearing	Unsecured, no impairment
<i>JG Summit Group*</i>	348	—	—	293	—	10-day; noninterest-bearing	Unsecured, no impairment
Purchases of IT services - <i>Indra Philippines</i>	658	423	451	(2)	—	30-day; noninterest-bearing	Unsecured
Purchases of meters and devices - <i>GEPMICI</i>	251	248	314	—	—	30-day; noninterest-bearing	Unsecured
Revenue from pole attachment - <i>PLDT</i>	212	206	197	—	—	Advance payment	Unsecured, no impairment
Purchases of wireline and wireless services - <i>PLDT Group</i>	50	47	43	—	—	30-day; noninterest-bearing	Unsecured
Purchases of power:							
South Premiere Power Corporation or <i>SPPC</i>	34,885	—	—	(2,893)	—	30-day; noninterest-bearing	Unsecured
San Miguel Energy Corporation or <i>SMEC</i>	13,648	—	—	(951)	—	30-day; noninterest-bearing	Unsecured

*Represents sale of electricity for the month of December 2013.

Advances to FPM Power

On March 22, 2013, *FPM Power* availed a loan from *MPG Asia Limited* amounting to US\$110 million which is payable on demand. The loan is outstanding as at December 31, 2013.

Transaction with MERALCO Pension Fund

MERALCO Pension Fund holds 6,000 common shares of *RP Energy* at ₱100 par value per share, with total carrying amount of ₱600,000 or an equivalent 3% equity interest in *RP Energy*. The fair value of *RP Energy*'s common shares cannot be reliably measured as these are not traded in the financial market. As at December 31, 2013, the fair value of the total assets being managed by *MERALCO Pension Fund* amounted to ₱34.0 billion.



See Note 27 – Long-Term Employee Benefits.

Compensation of Key Management Personnel

The compensation of key management personnel of the *MERALCO Group* by benefit type is as follows:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Short-term employee benefits	₱517	₱432	₱413
Long-term employee and retirement benefits	283	256	299
Share-based payments	–	31	16
Total compensation to key management personnel	₱800	₱719	₱728

Each of the directors is entitled to a per diem of ₱120,000 for every *BOD* meeting attended. Each member of the Audit and Risk Management, Remuneration and Leadership Development (formerly Compensation and Benefits), Finance, Governance and Nomination Committees is entitled to a fee of ₱20,000 for every committee meeting attended.

On March 22, 2013, the *BOD* approved the amendment of *MERALCO's* By-Laws which entitles all directors to a reasonable per diem for their attendance in meetings of the *BOD* and Board Committees plus an additional compensation provided, the total value of such additional compensation, in whatever form so given, shall not exceed one percent of the net income before tax of *MERALCO* during the preceding year.

Consistent with the foregoing, the *BOD* approved the increase in the compensation of all members of the *BOD* up to a maximum of pre-agreed amount per annum. The increase in compensation shall be through a stock grant based on a pre-approved number of shares for each director. The implementation of such plan was approved by the stockholders in the annual general meeting of stockholders on May 28, 2013.

There are no agreements between the *MERALCO Group* and any of its key management personnel providing for benefits upon termination of employment or retirement, except with respect to benefits provided under the pension and provident plans. The Pension Plan covers employees hired up to December 31, 2003 only. The Provident Plan, which is implemented on a voluntary basis, covers employees hired beginning January 1, 2004.

25. Revenues and Purchased Power

Sale of Electricity

Electricity revenues account for 99% of the total revenues in 2013, 2012 and 2011. Following is the breakdown of electricity revenues:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Generation charge	₱192,558	₱183,708	₱157,850
Transmission charge	29,191	31,971	32,340
System loss charge	17,138	16,411	15,500

(Forward)



	2013	2012	2011
	<i>(Amounts in millions)</i>		
Power Act Reduction adjustment	(P9)	(P25)	(P106)
Interclass, lifeline subsidies and others	(134)	34	(201)
Distribution service charges	56,105	50,892	48,606
	P294,849	P282,991	P253,989

Distribution service revenue accounted for 19%, 18% and 19% of total electricity revenues in 2013, 2012 and 2011 respectively. *VAT*, *LFT* and universal charges, which are also pass-through charges are billed and collected on behalf of the national and local governments and do not form part of total electricity revenues.

See Note 7 – Segment Information.

Purchased Power

The details of purchased power are as follows:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
Generation charge	P206,507	P198,648	P170,445
Transmission charge	31,691	33,420	35,229
	P238,198	P232,068	P205,674

Purchased power costs are pass-through costs and are revenue-neutral to *MERALCO* and *CEDC*, as *DUs*.

Generation charge is inclusive of line rentals, market fees and must-run unit charges billed by *PEMC*.

Purchased power includes capacity fees, fixed operating fees and transmission line fees that are accounted for similar to a lease under Philippine Interpretation *IFRIC 4*, “*Determining whether an arrangement contains a lease*”. The total amounts billed by the suppliers presented as part of “Purchased power” account in the consolidated statements of income are P46,170 million, P18,946 million and P20,135 million in 2013, 2012 and 2011, respectively. This also includes the actual *SL* incurred but no more than 8.5%. *MERALCO*’s actual *SL* rates are 6.92%, 7.04% and 7.30% in 2013, 2012 and 2011, respectively.

The details of purchased power follow:

	2013	2012	2011
	<i>(Amounts in millions)</i>		
First Gas Power Corporation or <i>FGPC</i> and <i>FGP</i> Corp. or <i>FGP</i>	P55,360	P58,592	P58,537
<i>PEMC/ WESM</i>	40,600	28,401	20,265
<i>SPPC</i>	34,885	—	—
<i>TransCo/NGCP</i>	31,691	33,420	35,229
<i>QPPL</i>	14,251	15,147	15,687
<i>SMEC</i>	13,648	—	—

(Forward)



	2013	2012	2011
	<i>(Amounts in millions)</i>		
Masinloc Power Partners Co. Ltd. or <i>MPPCL</i>	₱12,905	₱—	₱—
<i>NPC/PSALM (including NPC Successor Generating Companies or SGCs/Independent Power Plant Administrators)</i>	11,531	96,375	75,775
Sem-Calaca Power Corporation or <i>Sem-Calaca</i>	10,673	—	—
Therma Luzon, Inc. or <i>TLI</i>	9,538	—	—
Others	3,116	133	181
	₱238,198	₱232,068	₱205,674

Generation and transmission cost over/under-recoveries occur as a result of the lag in the billing and recovery of generation and transmission costs from consumers. As at December 31, 2013 and 2012, the total transmission cost over-recoveries included in “Other noncurrent liabilities” account in the consolidated statements of financial position amounted to ₱6,358 million and ₱5,288 million, respectively.

26. Expenses and Income

Salaries, Wages and Employee Benefits

		2012	2011
		(As restated - see Note 4)	(As restated - see Note 4)
	<i>Note</i>	2013	
		<i>(Amounts in millions)</i>	
Salaries, wages and related employee benefits		₱9,824	₱9,843
Pension	27	1,176	1,367
Other long-term post-employment benefits	27	258	261
<i>ESPP</i>	17	—	134
		₱11,258	₱11,605
			₱10,864

Other Expenses

		2013	2012	2011
	<i>Note</i>			
		<i>(Amounts in millions)</i>		
Inventories	14	₱696	₱527	₱735
Rent and utilities		688	574	412
Transportation and travel		360	386	475
Corporate expenses		291	249	258
Advertising		245	179	197
Insurance		214	208	259
Communication	24	82	68	62
Others		872	1,559	489
		₱3,448	₱3,750	₱2,887



Interest and Other Financial Charges

	Note	2013	2012	2011
<i>(Amounts in millions)</i>				
Interest expense on interest-bearing long-term financial liabilities, net of interest capitalized	8 and 18	₱1,038	₱1,202	₱1,163
Interest expense on bill deposits	19	82	91	83
Interest expense on notes payable	22	73	5	6
Amortization of debt issuance costs	18	61	37	23
Interest expense on meter deposits	19	2	1	3
Others		223	192	167
		₱1,479	₱1,528	₱1,445

Interest and Other Financial Income

	2013	2012	2011
<i>(Amounts in millions)</i>			
Interest income on cash and cash equivalents	₱1,088	₱1,762	₱1,379
Carrying costs on ERC-approved under-recoveries	32	755	791
Gain on return of investment	—	—	24
Others	52	52	70
	₱1,172	₱2,569	₱2,264

27. Long-term Employee Benefits

Liabilities for long-term employee benefits consist of the following:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Long-term incentives	₱1,205	₱2,592	₱1,641
Pension liability	1,186	3,279	5,951
Other long-term post-employment benefits	1,792	2,962	2,966
	₱4,183	₱8,833	₱10,558

Retirement Plan

The features of the *MERALCO Group's* defined benefit plans are discussed in *Note 4 – Significant Accounting Policies*.

Actuarial valuations are prepared annually by the respective independent actuaries engaged by *MERALCO* and its subsidiaries.



Expense recognized for defined benefit plans (included in "Salaries, wages and employee benefits" account)

	2013	2012 (As restated - see Note 4)	2011 (As restated - see Note 4)
	<i>(Amounts in millions)</i>		
Current service costs	₱1,041	₱1,045	₱1,097
Net interest costs	130	319	364
Net pension expense	₱1,171	₱1,364	₱1,461
Actual return on plan assets	₱2,214	₱3,385	₱1,987

Pension Liability

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - See Note 4)
	<i>(Amounts in millions)</i>		
Defined benefit obligation	₱35,225	₱33,811	₱33,234
Fair value of plan assets	(34,039)	(30,532)	(27,283)
Pension liability	₱1,186	₱3,279	₱5,951

Changes in the net pension liability are as follows:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - See Note 4)
	<i>(Amounts in millions)</i>		
Pension liability at beginning of year	₱3,279	₱5,951	₱9,743
Net pension costs	1,171	1,364	1,461
Amounts recognized in <i>OCI</i>	(278)	(2,599)	(1,054)
Contributions by employer	(2,986)	(1,437)	(4,199)
Pension liability	₱1,186	₱3,279	₱5,951

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

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - See Note 4)
	<i>(Amounts in millions)</i>		
Defined benefit obligation at beginning of year	₱33,811	₱33,234	₱32,729
Interest costs	1,999	1,952	1,958
Current service costs	1,041	1,045	1,097
Benefits paid	(1,693)	(1,573)	(1,695)

(Forward)



	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - See Note 4)
Actuarial losses (gains) due to:			
Changes in financial assumptions	₱671	(₱850)	₱453
Experience adjustments	(604)	3	(1,140)
Defined benefit obligation of discontinued operations	—	—	(168)
Defined benefit obligation at end of year	₱35,225	₱33,811	₱33,234

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

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Fair value of plan assets at beginning of year	₱30,532	₱27,283	₱22,986
Benefits paid	(1,693)	(1,573)	(1,695)
Interest income	1,869	1,633	1,594
Return on plan assets, excluding amount included in net interest on the net defined benefit obligation	345	1,752	393
Contributions by employer	2,986	1,437	4,199
Fair value of plan assets of discontinued operations	—	—	(194)
Fair value of plan assets at end of year	₱34,039	₱30,532	₱27,283

The Board of Trustees or *BOT*, which manages the retirement benefit fund, is chaired by the chairman of *MERALCO*, who is neither an executive nor a beneficiary. The other members of the *BOT* are (i) an independent member of the *BOD*; (ii) a member of the *BOD* who represents the largest shareholder group; (iii) an executive member of the *BOD*; (iv) two (2) senior executives; and (v) a non-executive, non-*BOD* member who represents another shareholder group, all of whom are non-beneficiaries of the Plan.

The Fund follows a generally conservative investment approach where investments are diversified to minimize risks but ensures an increase in value of the Fund assets. Substantially all of the funds of the Plan are managed by four (4) trustee banks whose common objective is to maximize the long-term expected return of plan assets. As approved by the *BOT*, the funds are invested in a guided proportion of fixed income instruments, cash investments and equities.



Net carrying amount and fair value of the assets of the fund as at December 31, 2013 and 2012 amounted to ₱34,039 million and ₱30,532 million, respectively. The major categories of plan assets are as follows:

	2013	2012
	<i>(Amount in millions)</i>	
Cash and cash equivalents	₱5,637	₱3,100
Investments quoted in active markets:		
Quoted equity investments		
Holding firms	1,950	2,247
Electricity, energy, power and water	1,155	1,480
Food, beverages and tobacco	908	884
Banks	713	839
Property	608	660
Telecommunication	607	295
Transportation services	283	230
Construction, infrastructure and allied services	82	158
Financial institution	81	102
Gaming	75	130
Mining	66	245
Retail	44	92
Media	31	43
Hotel and leisure	15	—
Others	325	385
Quoted debt investments		
Government securities	11,385	10,587
“AAA” rated securities	7,399	6,256
Unquoted investments		
Receivables	1,721	1,967
Property	954	832
Fair value of plan assets	₱34,039	₱30,532

Marketable equity securities, government securities, bonds and commercial notes are investments held by the trustee banks. The Fund does not have any direct equity interests in *MERALCO*.

Other Long-term Post-employment Benefits (included as part of “Salaries, wages and employee benefits” account)

	2013	2012	2011
		(As restated - see Note 4)	(As restated - See Note 4)
	<i>(Amounts in millions)</i>		
Interest costs	₱178	₱176	₱156
Current service costs	80	85	54
	₱258	₱261	₱210



Other Long-term Post-employment Benefits Liability

Changes in the present value of other long-term post-employment benefits liability are as follows:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - See Note 4)
<i>(Amounts in millions)</i>			
Balance at beginning of year	₱2,962	₱2,966	₱2,471
Interest costs	178	176	156
Current service costs	80	85	54
Benefits paid	(53)	(73)	(75)
Actuarial losses (gains) due to change in assumptions	(1,375)	(192)	360
Balance at end of year	₱1,792	₱2,962	₱2,966

Actuarial Assumptions

The principal assumptions used as at January 1, 2013, 2012 and 2011 in determining pension and other long-term post-employment benefits obligations are shown below:

	2013	2012	2011
Annual discount rate	4.5%	6.0%	6.0%
Future range of annual salary increases	6.0%–10.0%	6.0%–8.0%	6.0%–8.0%

Sensitivity Analysis

The calculation of the defined benefit obligation is sensitive to the assumptions set above. The following table summarizes how the impact on the defined benefit obligation at the end of the reporting period would have increased (decreased) as a result of a change in the respective assumptions by:

		Effect on Present Value of Defined Benefit Obligation	
	% Change	2013	2012
<i>(Amounts in millions)</i>			
Annual discount rate	+1.0%	(₱2,144)	(₱1,107)
	-1.0%	4,445	1,107
Future range of annual salary increases	+1.0%	1,072	1,161

Funding

MERALCO contributes to the Fund from time to time such amounts of money required under accepted actuarial principles to maintain the Fund in a sound condition, subject to the provisions of the Plan.



The amount of the annual contributions to the Fund is determined through an annual valuation report performed by the actuary.

MERALCO expects to contribute ₱1,690 million to its defined benefit pension plan in 2014.

The following is the maturity profile of the undiscounted benefit obligation:

	(Amounts in millions)
Less than one year	₱1,400
More than one year to five years	6,838
More than five years to 10 years	7,091
More than 10 years to 15 years	7,714
More than 15 years to 20 years	7,632
More than 20 years	19,312

Risk

The Fund is exposed to the following risks:

Credit Risk

The Fund's exposure to credit risk arises from its financial assets which comprise cash and cash equivalents, investments and rental receivable. The credit risk results from the possible default of the issuer of the financial instrument, with a maximum exposure equivalent to the carrying amount of the instruments.

The credit risk is minimized by ensuring that the exposure to the various chosen financial investment structures is limited primarily to government securities and bonds or notes duly recommended by the Trust Committees of the Fund of the appointed fund managers.

Share Price Risk

The Pension Fund's exposure to share price risk arises from the shares of stock it holds and being traded at the *PSE*. The price risk emanates from the volatility of the stock market.

The policy is to limit investment in shares of stock to blue chip issues or issues with good fair values or those trading at a discount to its net asset value so that in the event that market falls drastically, the Pension Fund may still consider to hold on to such investments until the market recovers.

By having a balanced composition of holdings in the equities portfolio, exposure to industry or sector-related risks is reduced. The mix of various equities in the portfolio reduces volatility and contributes to a more stable return over time. Equity investments are made within the parameters of the investment guidelines approved by the *BOT*. The *BOT* also meets periodically to review the investment portfolio based on financial market conditions. Share prices are also monitored regularly.

Liquidity Risk

Liquidity risk is the risk that the Pension Fund is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. Liquidity risk is being managed to ensure that adequate fixed income and cash deposits are available to service the financial obligations of the Fund. The schedule of the maturities of fixed income investment assets are staggered by tenure or term. Policies are established to ensure that all financial obligations are met, wherein the timing of the maturities of fixed income investments are planned and matched to the due date of various obligations. Thus, for this investment class, maturities are



classified into short-, medium- and long-term. A certain percentage of the portfolio is left in cash to manage liquidity and settle all currently maturing financial obligations.

MERALCO Defined Contribution Provident Plan

MERALCO has a contributory Provident Plan effective January 1, 2009, intended to be a Supplemental Retirement Benefit for employees hired after 2004, on a voluntary basis. Each qualified employee-member who opts to participate in the plan shall have the option to contribute up to a maximum of 25% of his base salary. MERALCO shall match the member's contribution up to the first 10% of the member's base salary. Upon resignation, the member shall be entitled to the total amount credited to his personal retirement account immediately preceding his actual retirement date, subject to provisions of the Provident Plan. MERALCO's contribution to the Provident Plan amounted to ₱5 million, ₱3 million and ₱4 million for the years ended December 31, 2013, 2012 and 2011, respectively.

Consolidated Pension Benefit Cost (included in "Salaries, wages and employee benefits" account)

	2013	2012 (As restated - see Note 4)	2011 (As restated - See Note 4)
	(Amounts in millions)		
Expense recognized for defined benefit plans	₱1,171	₱1,364	₱1,461
Expense recognized for defined contribution plan	5	3	4
Pension expense	₱1,176	₱1,367	₱1,465

Long-term Incentive Plan or LTIP

MERALCO's LTIP covers qualified executives and is based on MERALCO Group's achievement of specified level of consolidated core net income approved by the BOD and determined on an aggregate basis for a three year period as well as executives' attainment of a minimum level of performance rating. Executives invited to the plan must serve a minimum uninterrupted period to be entitled to any pay-out.

28. Financial Assets and Financial Liabilities

Financial assets consist of cash and cash equivalents and trade and nontrade receivables, which are generated directly from operations. The principal financial liabilities, other than derivatives, consist of bank loans, redeemable preferred shares, trade and nontrade payables, which are incurred to finance operations in the normal course of business. Accounting policies related to financial assets and financial liabilities are set out in Note 4 – *Significant Accounting Policies, Changes and Improvements*.



The following table sets forth the financial assets and financial liabilities as at December 31, 2013 and 2012:

	Loans and Receivables	Held-to- maturity Investments	Fair Value through Profit or Loss	Held-for- trading	Available- for-sale Financial Assets	Liabilities Carried at Amortized Cost	Total Financial Assets and Liabilities
<i>(Amounts in millions)</i>							
Assets as at December 31, 2013							
Noncurrent							
Other noncurrent assets	P474	P129	P—	P—	P161	P—	P764
Current							
Cash and cash equivalents	59,851	—	—	—	—	—	59,851
Trade and other receivables - net	28,543	—	—	—	—	—	28,543
Short-term investments	4,841	—	—	—	—	—	4,841
Advances to an associate	4,884	—	—	—	—	—	4,884
Total assets	98,593	129	—	—	161	—	98,883
Liabilities as at December 31, 2013							
Noncurrent							
Interest-bearing long-term financial liabilities - net of current portion	—	—	—	—	—	20,756	20,756
Customers' deposits - net of current portion	—	—	—	—	—	21,600	21,600
Refundable service extension costs - net of current portion	—	—	—	—	—	5,782	5,782
Current							
Notes payable	—	—	—	—	—	1,814	1,814
Trade payables and other current liabilities	—	—	—	—	—	57,113	57,113
Customers' refund	—	—	—	—	—	6,013	6,013
Current portion of interest-bearing long-term financial liabilities	—	—	—	—	—	11,021	11,021
Total liabilities	—	—	—	—	—	124,099	124,099
Net Assets (Liabilities)	P98,593	P129	P—	P—	P161	(P124,099)	(P25,216)
<i>(Amounts in millions)</i>							
	Loans and Receivables	Held-to- maturity Investments	Fair Value through Profit or Loss	Held-for- trading	Available- for-sale Financial Assets	Liabilities Carried at Amortized Cost	Total Financial Assets and Liabilities
Assets as at December 31, 2012							
Noncurrent							
Other noncurrent assets	P325	P123	P—	P—	P331	P—	P779
Current							
Cash and cash equivalents	60,500	—	—	—	—	—	60,500
Trade and other receivables - net	23,447	—	—	—	—	—	23,447
Other current assets - derivative assets	—	—	24	—	—	—	24
Total assets	84,272	123	24	—	331	—	84,750
Liabilities as at December 31, 2012							
Noncurrent							
Interest-bearing long-term financial liabilities - net of current portion	—	—	—	—	—	20,466	20,466
Customers' deposits - net of current portion	—	—	—	—	—	23,313	23,313
Refundable service extension costs - net of current portion	—	—	—	—	—	4,357	4,357
Current							
Notes payable	—	—	—	—	—	1,787	1,787
Trade payables and other current liabilities	—	—	—	—	—	34,966	34,966
Customers' refund	—	—	—	—	—	6,127	6,127
Current portion of interest-bearing long-term financial liabilities	—	—	—	—	—	2,360	2,360
Total liabilities	—	—	—	—	—	93,376	93,376
Net Assets (Liabilities)	P84,272	P123	P24	P—	P331	(P93,376)	(P8,626)



Fair Values

The fair values of the financial assets and financial liabilities are prices that would be received to sell the financial assets or paid to transfer the financial liabilities in orderly transactions between market participants at the measurement date. Set out below is a comparison of carrying amounts and fair values of *MERALCO Group's* financial instruments as at December 31, 2013 and 2012.

	2013		2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	<i>(Amounts in millions)</i>			
Financial assets				
Loans and receivables -				
Advances to a supplier	₱474	₱522	₱325	₱409
Fair value through profit or loss -				
Derivative asset	—	—	24	24
Available-for-sale financial assets	161	161	331	331
	₱635	₱683	₱680	₱764
Financial liabilities				
Financial liabilities carried at amortized cost -				
Interest-bearing long-term financial liabilities	₱31,777	₱32,176	₱22,826	₱24,787

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate such value:

Cash and Cash Equivalents, Short-term Investments, Trade and Other Receivables, Advances to an Associate, Trade Payables and Other Current Liabilities and Notes Payable

Due to the short-term nature of transactions, the fair values of these instruments approximate their carrying amounts as at reporting date.

Advances to a Supplier

The fair values of advances to a supplier were computed by discounting the instruments' expected future cash flows using the rates of 3.76% as at December 31, 2013 and 4.16% as of December 31, 2012.

Bifurcated Foreign Currency Forward and Foreign Currency Forward

The fair values of embedded currency forwards and freestanding currency forwards were calculated by reference to forward exchange market rates.

AFS Investments

The fair values were determined by reference to market bid quotes as at reporting date. The unquoted equity securities were carried at cost.



Meter Deposits and Customers' Refund

Meter deposits and customers' refund are due and demandable. Thus, the fair values of these instruments approximate their carrying amounts.

Bill Deposits

The carrying amount of bill deposits approximates their fair values as bill deposits are interest-bearing.

Interest-bearing Long-term Financial Liabilities

The fair values of interest-bearing long-term debt (except for redeemable preferred stock) were computed by discounting the instruments' expected future cash flows using the rates ranging from 0.52% to 4.29% as at December 31, 2013 and 1.65% to 4.49% as of December 31, 2012.

Redeemable Preferred Stock

The carrying amount of the preferred stock represents the fair value. Such preferred shares have been called and are payable anytime upon presentation by the shareholder of their certification. This is included under "Interest-bearing long-term financial liabilities" account.

Refundable Service Extension Costs

The fair values of refundable service extension costs cannot be reliably measured since the timing of related cash flows cannot be reasonably estimated and are accordingly measured at cost.

Fair Value Hierarchy

MERALCO uses the following hierarchy in determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities
- Level 2: other techniques where all inputs have a significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques where inputs have a significant effect on the recorded fair value that are not based on observable market data

Below is the list of financial assets and financial liabilities that are classified using the fair value hierarchy:

	December 31, 2013				December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
	<i>(Amounts in millions)</i>							
Financial assets								
Advances to a supplier	P-	P-	P522	P522	P-	P-	P409	P409
AFS investments	124	-	37	161	128	-	203	331
Derivative assets	-	-	-	-	-	24	-	24
	P124	P-	P559	P683	P128	P24	P612	P764
Financial liabilities								
Interest-bearing long-term financial liabilities	P-	P-	P32,176	P32,176	P-	P-	P24,787	P24,787



For the years ended December 31, 2013 and 2012, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

Financial Risk Management Objectives and Policies

The main risks arising from the financial instruments are interest rate risk, foreign currency risk, commodity price risk, credit risk and liquidity risk. The importance of managing these risks has significantly increased in light of the considerable change and volatility in the Philippine and international financial markets. The *BOD* reviews and approves policies for managing each of these risks. Management monitors the market price risk arising from all financial instruments. The policies for managing these risks are as follows:

Interest Rate Risk

The *MERALCO Group*'s exposure to the changes in market interest rates relate primarily to the long-term interest-bearing financial liabilities.

The *MERALCO Group*'s policy is to manage its interest rate risk exposure using a mix of fixed and variable rate debts. The strategy, which yields a reasonably lower effective cost based on market conditions, is adopted. Refinancing of fixed rate loans may also be undertaken to manage interest cost. Approximately 90% and 83% of the borrowings bear fixed rate of interest as at December 31, 2013 and 2012, respectively.

The following table sets out the maturity profile of the financial instruments that are exposed to interest rate risk (exclusive of debt issuance costs):

	Within 1 Year	Over 1-2 Years	Over 2-3 Years	Over 3-4 Years	Over 4-5 Years	More than 5 Years	Total
<i>(Amounts in millions)</i>							
December 31, 2013	₱612	₱13	₱13	₱12	₱2,425	₱-	₱3,075
December 31, 2012	613	612	13	13	12	2,425	3,688

Floating interest rate of bank loans is repriced at intervals of less than one year. The other financial liabilities of *MERALCO Group* that are not included in the foregoing have fixed interest rate and are therefore not subject to interest rate risk.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of *MERALCO*'s profit before tax as at December 31, 2013 and 2012 through the impact on floating rate borrowings. There is no other impact on *MERALCO*'s equity other than those already affecting the consolidated statement of income.

	2013		2012	
	Increase (Decrease) in Basis Points	Effect on Profit before Tax	Increase (Decrease) in Basis Points	Effect on Profit before Tax
<i>(Amounts in millions)</i>				
Floating rate loans from various banks	+100 (100)	(₱31) 31	+100 (100)	(₱37) 37



Interest expense of floating rate loans for the year is computed by taking into account actual principal movements, based on management's best estimate of a +/-100 basis points change in interest rates. There has been no change in the methods and assumptions used by the management in the above analysis.

Foreign Currency Risk

The revaluation of any of foreign currency-denominated financial assets and financial liabilities as a result of the appreciation or depreciation of the Philippine peso is recognized as foreign exchange gains or losses as at the end of each reporting year. The extent of foreign exchange gains or losses is largely dependent on the amount of foreign currency-denominated financial instruments. While an insignificant percentage of the *MERALCO Group's* revenues and liabilities is denominated in *U.S.* dollars, a substantial portion of the *MERALCO Group's* capital expenditures for electricity capital projects and a portion of the operating expenses are denominated in foreign currencies, mostly in *U.S.* dollars. As such, a strengthening or weakening of the Philippine peso against the *U.S.* dollar will decrease or increase in Philippine peso terms, the principal amount of the *MERALCO Group's* foreign currency-denominated liabilities and the related interest expense, foreign currency-denominated capital expenditures and operating expenses as well as *U.S.* dollar-denominated revenues.

The following table shows the consolidated foreign currency-denominated financial assets and financial liabilities as at December 31, 2013 and 2012, translated to Philippine peso at ₱44.395 and ₱41.050 to \$1, respectively.

	2013		2012	
	U.S.Dollar	Peso Equivalent	U.S.Dollar	Peso Equivalent
<i>(Amounts in millions)</i>				
Financial assets:				
Cash and cash equivalents	\$65	₱2,864	\$47	₱1,913
Trade and other receivables	3	148	1	53
Advances to an associate	110	4,884	—	—
Advance payments to a supplier	11	474	8	325
	189	8,370	56	2,291
Financial liabilities -				
Trade payables and other liabilities	(46)	(2,043)	(139)	(5,724)
	\$143	₱6,327	(\$83)	(₱3,433)

All of *MERALCO's* long-term financial liabilities are denominated in Philippine peso. However, an insignificant portion of its trade payables are denominated in *U.S.* dollar. Thus, the impact of ₱1 movement of the Philippine Peso against the *U.S.* dollar will not have a significant impact on *MERALCO's* obligations. Further, *PBR* assumes a forecast level of foreign currency movements in its calculation of the regulatory asset base and expenditures. *PBR* also allows for adjustment of the rates *MERALCO* charges should there be significant deviations in the foreign exchange forecast from what is actually realized.



The following table demonstrates the sensitivity to a reasonably possible change in the *U.S.* dollar exchange rate vis-a-vis the peso, with all other variables held constant, of the *MERALCO Group's* income before income tax for the years ended December 31, 2013 and 2012 (due to changes in the fair value of financial assets and financial liabilities). There is no other impact on *MERALCO's* equity other than those already affecting the profit and loss.

	2013		2012	
	Appreciation (Depreciation) of U.S. Dollar	Effect on Income before Income Tax	Appreciation (Depreciation) of U.S. Dollar	Effect on Income before Income Tax
	(In %)	(In millions)	(In %)	(In millions)
U.S. dollar-denominated financial assets	+5	₱317	+5	(₱170)
and financial liabilities	-5	(317)	-5	170

Foreign exchange gain or loss for the year is computed based on management's best estimate of a +/-5 percent change in the closing Philippine peso to *U.S.* dollar conversion rate using the year-end balances of *U.S.* dollar-denominated cash and cash equivalents, receivables and liabilities. There has been no change in the methods and assumptions used by management in the foregoing analysis.

Commodity Price Risk

Commodity price risk is the risk that the fair value or cash flows of a financial instrument will fluctuate because of changes in commodity prices. The exposure of *MERALCO* and *CEDC* to price risk is minimal. The cost of fuel is part of *MERALCO's* and *CEDC's* generation costs that are recoverable through the generation charge in the billings to customers.

Credit Risk

Credit risk is the risk that the *MERALCO Group* is exposed to as a result of its customers, clients or counterparties failing to discharge their contracted obligations. The *MERALCO Group* manages and controls credit risk by setting limits on the amount of risk that it is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

MERALCO as a franchise holder serving public interest cannot refuse customer connection. To mitigate risk, the *DSOAR* allows *MERALCO* to collect bill deposit equivalent to one month's consumption to secure credit. Also, as a policy, disconnection notices are sent three days after the bill due date and disconnections are carried out beginning on the third day after receipt of disconnection notice.

The *MERALCO* subsidiaries trade only with recognized, creditworthy third parties. It is the *MERALCO Group's* policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivables are monitored on an ongoing basis to reduce exposure to bad debt.

With respect to placements of cash with financial institutions, these institutions are subject to the *MERALCO Group's* accreditation evaluation based on liquidity and solvency ratios and on the bank's credit rating. The *MERALCO Group* transacts derivatives only with similarly accredited financial institutions. In addition, the *MERALCO Group's* deposit accounts in banks are insured by the Philippine Deposit Insurance Corporation up to ₱500,000 per bank account.

Credit risk on other financial assets, which include cash and cash equivalents, trade and other receivables, short-term investments and certain derivative instruments, arises from the potential default of the counterparty.



Finally, credit quality review procedures are in place to provide regular identification of changes in the creditworthiness of counterparties. Counterparty limits are established and reviewed periodically based on latest available financial information of counterparties, credit ratings and liquidity. The *MERALCO Group*'s credit quality review process allows it to assess any potential loss as a result of the risks to which it may be exposed and to take corrective actions.

There are no significant concentrations of credit risk within the *MERALCO Group*.

The table below shows the maximum exposure to credit risk for the components of the consolidated statements of financial position as at December 31, 2013 and 2012. The maximum exposure is equivalent to the nominal amount of the accounts.

	Gross Maximum Exposure	
	2013	2012
	<i>(Amounts in millions)</i>	
Cash and cash equivalents:		
Cash in banks	₱4,994	₱3,250
Cash equivalents	54,722	57,244
Trade and other receivables:		
Billed electricity	24,312	20,779
Service contracts	1,310	671
Insurance receivable	453	383
Cost of estimated earnings in excess of billings on uncompleted contracts	455	258
Nontrade receivables	2,013	1,356
Other current assets:		
Short-term investments	4,841	—
Advances to an associate	4,884	—
Derivatives	—	24
Other noncurrent assets:		
Advance payments to suppliers	474	325
HTM investments	129	123
	₱98,587	₱84,413

The credit quality of financial assets is managed by *MERALCO* using “High Grade,” “Standard Grade” and “Sub-standard Grade” for accounts, which are neither impaired nor past due as internal credit ratings. The following tables show the credit quality by asset class:

	2013					Total
	Neither Past Due nor Impaired			Past Due but not Impaired	Impaired Financial Assets	
	High Grade	Standard Grade	Sub-standard Grade			
	<i>(Amounts in millions)</i>					
Cash in banks and cash equivalents	₱59,716	₱—	₱—	₱—	₱—	₱59,716
Trade and other receivables:						
Billed electricity	6,048	3,583	9,064	5,616	2,970	27,281
Service contracts	1,118	—	—	192	180	1,490
Insurance receivable	33	—	304	116	—	453
Cost of estimated earnings in excess of billings on uncompleted contracts	455	—	—	—	—	455
Nontrade receivables	1,883	8	20	103	2	2,016

(Forward)



2013						
	Neither Past Due nor Impaired			Past Due but not Impaired	Impaired Financial Assets	Total
	High Grade	Standard Grade	Sub-standard Grade			
(Amounts in millions)						
Other current assets:						
Short-term investments	₱4,841	₱—	₱—	₱—	₱—	₱4,841
Advances to an associate	—	4,884	—	—	—	4,884
Other noncurrent assets	—	—	603	—	—	603
	₱74,094	₱8,475	₱9,991	₱6,027	₱3,152	₱101,739
2012						
	Neither Past Due nor Impaired			Past Due but not Impaired	Impaired Financial Assets	Total
	High Grade	Standard Grade	Sub-standard Grade			
(Amounts in millions)						
Cash in banks and cash equivalents	₱60,494	₱—	₱—	₱—	₱—	₱60,494
Trade and other receivables:						
Billed electricity	5,946	3,313	8,513	3,007	2,559	23,338
Service contracts	671	—	—	—	145	816
Insurance receivable	313	—	—	70	—	383
Cost of estimated earnings in excess of billings on uncompleted contracts	258	—	—	—	—	258
Nontrade receivables	954	151	3	248	2	1,358
Derivative assets	24	—	—	—	—	24
Other noncurrent assets	—	—	448	—	—	448
	₱68,660	₱3,464	₱8,964	₱3,325	₱2,706	₱87,119

Credit ratings are determined as follows:

- “High Grade”

‘High’ grade financial assets include “cash in banks and cash equivalents and derivative assets to counterparties with good credit rating or bank standing. Consequently, credit risk is minimal. These counterparties include large prime financial institutions, large industrial companies and commercial establishments, and government agencies. For trade receivables, these consist of current month’s billings (less than 30 days) that are expected to be collected within 10 days from the time bills are delivered.
- “Standard Grade”

‘Standard’ grade financial assets include trade receivables that consist of current month’s billings (less than 30 days) that are expected to be collected before due date (10 to 14 days after bill date).
- “Sub-standard Grade”

‘Sub-standard’ grade financial assets include trade receivables that consist of current month’s billings, which are not expected to be collected within 60 days.



The following table shows the aging analysis of financial assets as at December 31, 2013 and 2012:

2013						
	Neither Past Due nor Impaired	Past Due But Not Impaired			Impaired Financial Assets	Total
		31-60 Days	61-90 Days	Over 90 Days		
<i>(Amounts in millions)</i>						
Cash and cash equivalents:						
Cash equivalents	₱54,722	₱-	₱-	₱-	₱-	₱54,722
Cash in banks	4,994	-	-	-	-	4,994
Trade and other receivables:						
Trade:						
Billed electricity	18,695	2,068	504	3,044	2,970	27,281
Service contracts	1,118	-	-	192	180	1,490
Insurance receivable	337	5	9	102	-	453
Cost and estimated earnings in excess of billings on uncompleted contracts	455	-	-	-	-	455
Nontrade receivables	1,911	22	5	76	2	2,016
Other current assets:						
Short-term investments	4,841	-	-	-	-	4,841
Advances to associate	4,884	-	-	-	-	4,884
Other noncurrent assets:						
Advance payments to a supplier	474	-	-	-	-	474
HTM investments	129	-	-	-	-	129
	₱92,560	₱2,095	₱518	₱3,414	₱3,152	₱101,739

2012						
	Neither Past Due nor Impaired	Past Due But Not Impaired			Impaired Financial Assets	Total
		31-60 Days	61-90 Days	Over 90 Days		
<i>(Amounts in millions)</i>						
Cash and cash equivalents:						
Cash in banks	₱3,250	₱-	₱-	₱-	₱-	₱3,250
Cash equivalents	57,244	-	-	-	-	57,244
Trade and other receivables:						
Trade:						
Billed electricity	17,772	1,896	628	483	2,559	23,338
Service contracts	671	-	-	-	145	816
Insurance receivable	313	11	12	47	-	383
Cost and estimated earnings in excess of billings on uncompleted contracts	258	-	-	-	-	258
Nontrade receivables	1,108	9	6	233	2	1,358
Other current assets - Derivative assets	24	-	-	-	-	24
Other noncurrent assets:						
Advance payments to a supplier	325	-	-	-	-	325
HTM investments	123	-	-	-	-	123
	₱81,088	₱1,916	₱646	₱763	₱2,706	₱87,119

Liquidity Risk

Liquidity risk is the risk that the *MERALCO Group* will be unable to meet its payment obligations when these fall due. The *MERALCO Group* manages this risk through monitoring of cash flows in consideration of future payment of obligations and the collection of its trade receivables. The *MERALCO Group* also ensures that there are sufficient, available and approved working capital lines that it can draw from at any time.

The *MERALCO Group* maintains an adequate amount of cash and cash equivalents and government securities, which may be readily converted to cash in any unforeseen interruption of its cash collections. The *MERALCO Group* also maintains accounts with several relationship banks to avoid significant concentration of funds with one institution.



The following table sets out the maturity profile of the financial liabilities based on contractual undiscounted payments plus future interest:

2013					
	Less than 3 Months	Over 3–12 Months	Over 1–5 Years	More than 5 Years	Total
<i>(Amounts in millions)</i>					
Notes payable	₱1,816	₱–	₱–	₱–	₱1,816
Trade payables and other current liabilities	47,018	231	–	–	47,249
Customers' refund	6,013	–	–	–	6,013
Interest-bearing long-term financial liabilities:					
Floating rate borrowings	14	601	2,592	–	3,207
Fixed rate borrowings	3,975	5,057	–	–	9,032
Bonds payable	211	645	3,427	21,716	25,999
Redeemable preferred stock	1,562	–	–	–	1,562
Customers' deposits	3,179	5,070	4,151	17,449	29,849
Refundable service extension costs	–	1,615	2,772	3,010	7,397
Total undiscounted financial liabilities	₱63,788	₱13,219	₱12,942	₱42,175	₱132,124

2012					
	Less than 3 Months	Over 3–12 Months	Over 1–5 Years	More than 5 Years	Total
<i>(Amounts in millions)</i>					
Notes payable	₱283	₱2,224	₱–	₱–	₱2,507
Trade payables and other current liabilities	26,076	1,126	–	–	27,202
Customers' refund	6,127	–	–	–	6,127
Interest-bearing long-term financial liabilities:					
Floating rate borrowings	35	684	847	2,447	4,013
Fixed rate borrowings	388	847	11,206	12,361	24,802
Redeemable preferred stock	1,594	–	–	–	1,594
Customers' deposits	640	5,612	169	23,144	29,565
Refundable service extension costs	1,512	–	4,357	–	5,869
Total undiscounted financial liabilities	₱36,655	₱10,493	₱16,579	₱37,952	₱101,679

The maturity profile of bill deposits is not determinable since the timing of each refund is linked to the cessation of service, which is not reasonably predictable. However, *MERALCO* estimates that the amount of bill deposits (including related interest) of ₱6,130 million will be refunded within the year. This is shown as part of "Trade payables and other current liabilities" account in the consolidated statement of financial position as at December 31, 2013.

Capital Management

The primary objective of the *MERALCO Group's* capital management is to enhance shareholder value. The capital structure is reviewed with the end view of achieving a competitive cost of capital and at the same time ensuring that returns on, and of, capital are consistent with the levels approved by its regulators for its core distribution business.

The capital structure optimization plan is complemented by efforts to improve capital efficiency to increase yields on invested capital. This entails efforts to improve the efficiency of capital assets, working capital and non-core assets.



The *MERALCO Group* monitors capital using debt to equity ratio, which is gross debt divided by equity attributable to the holders of the parent. The *MERALCO Group* considers long-term debt, redeemable preferred stock and notes payable as debt.

	2013	2012 (As restated - see Note 4)
	<i>(Amounts in millions, except debt to equity ratio)</i>	
Long-term debt	₱30,215	₱21,232
Redeemable preferred stock	1,562	1,594
Notes payable	1,814	1,787
Debt (a)	33,591	24,613
Equity attributable to the holders of the parent (b)	75,162	67,902
Debt to equity ratio (a)/(b)	0.45	0.36

29. Income Taxes and Local Franchise Taxes

Income Taxes

The components of net deferred tax assets (liabilities) as at December 31, 2013 and 2012 are as follows:

	Note	2013	2012 (As restated - see Note 4)
		<i>(Amounts in millions)</i>	
Deferred tax assets:			
Provisions for various claims	20	₱12,682	₱9,503
Accrued employee benefits		899	1,007
Unfunded pension cost and unamortized past service cost		480	1,577
Allowance for doubtful accounts	13	945	777
Allowance for excess of cost over net realizable value of inventories	14	61	62
Others		324	412
		15,391	13,338
Deferred tax liabilities:			
Revaluation increment in utility plant and others	16	7,389	7,645
Depreciation method differential		1,082	1,124
Capitalized interest		744	751
Capitalized duties and taxes deducted in advance		651	655
Net book value of capitalized/realized foreign exchange losses		22	37
Others		123	76
		10,011	10,288
		₱5,380	₱3,050



Provision for income tax consists of:

	2013	2012 (As restated - see Note 4)	2011 (As restated - see Note 4)
	<i>(Amounts in millions)</i>		
Current	₱9,889	₱9,490	₱8,454
Deferred	(2,835)	(3,749)	(2,501)
	₱7,054	₱5,741	₱5,953

A reconciliation between the provision for (benefit from) income tax computed at statutory income tax rate of 30% in 2013, 2012 and 2011, and provision for (benefit from) income tax as shown in the consolidated statements of income is as follows:

	2013	2012 (As restated - see Note 4)	2011 (As restated - see Note 4)
	<i>(Amounts in millions)</i>		
Income tax computed at statutory tax rate of:			
Continuing operations	₱7,298	₱6,607	₱5,624
Discontinued operations	–	318	386
	7,298	6,925	6,010
Income tax effects of:			
Interest income subjected to lower final tax rate	(314)	(521)	(590)
Nondeductible interest expense	130	213	236
Nontaxable income	(113)	(262)	(10)
Equity in net losses (earnings) of associates and joint ventures	78	45	(20)
Nondeductible expenses	–	40	593
Others	(25)	(616)	56
	7,054	5,824	6,275
Less provision for income tax of discontinued operations	–	83	322
	₱7,054	₱5,741	₱5,953

On December 18, 2009, the *BIR* issued Revenue Regulation, or *RR* No. 16-2008, which implemented the provisions of *RA* No. 9504 on Optional Standard Deductions or *OSD*. Such regulation allows both individual and corporate taxpayers to use *OSD* in computing their taxable income. For corporations, they may elect to adopt standard deduction in an amount not exceeding 40% of gross income in lieu of the allowed itemized deductions. For the years ended December 31, 2013, 2012 and 2011, none of the entities in the *MERALCO Group* availed of the *OSD* in computing taxable income, except for *RSIC* and *CFS*.

The temporary difference for which deferred tax assets have not been recognized pertains to the tax effect of net operating loss carryover amounting ₱717 million and ₱513 million as at December 31, 2013 and 2012, respectively.



NOLCO totaling to ₱717 million may be claimed as deduction against taxable income as follows:

Date Incurred	Expiry Date	Amount
		(In millions)
December 31, 2011	December 31, 2014	₱106
December 31, 2012	December 31, 2015	194
December 31, 2013	December 31, 2016	417
		₱717

LFT

Consistent with the decisions of the *ERC*, *LFT* is a recoverable charge of the *DU* in the particular province or city imposing and collecting the *LFT*. It is presented as a separate line item in the customer's bill and computed as a percentage of the sum of generation, transmission, distribution services and related system loss charges.

The Implementing Rules and Regulations issued by the *ERC* provide that local franchise taxes shall be paid only on its distribution wheeling and captive market supply revenues. Pending the promulgation of guidelines from the relevant government agencies, *MERALCO* is paying *LFT* based on the sum of the foregoing charges in the customers' bill.

30. Contingencies and Legal Proceedings

Overpayment of Income Tax related to SC Refund

With the decision of the *SC* for *MERALCO* to refund ₱0.167 per *kWh* to cover customers during the billing period February 1994 to May 2003, *MERALCO* overpaid income tax in the amount of ₱7,107 million for taxable years 1994 to 1998 and 2000 to 2001. Accordingly, *MERALCO* filed a claim on November 27, 2003 for the recovery of such excess income taxes paid. After examination of the books of *MERALCO* for the covered periods, the *BIR* determined that *MERALCO* had in fact overpaid income taxes in the amount of ₱6,690 million. However, the *BIR* also maintained that *MERALCO* is entitled to a refund amount of only ₱894 million, which pertains to taxable year 2001, claiming that the period for filing a claim had prescribed in respect of the difference between *MERALCO*'s overpayment and the refund amount *MERALCO* is entitled to.

The *BIR* then approved the refund of ₱894 million for issuance of tax credit certificates or *TCCs*, proportionate to the actual refund of claims to utility customers. The *BIR* initially issued *TCCs* amounting to ₱317 million corresponding to actual refund to customers as at August 31, 2005.

As at December 31, 2013 and 2012, the amount of unissued *TCCs* amounting to ₱577 million refund entitlement is presented as part of "Other noncurrent assets" account in the consolidated statements of financial position.

See Note 11 – Other Noncurrent Assets.

MERALCO filed a Petition with the Court of Tax Appeals or *CTA*, assailing the denial by the *BIR* of its income tax refund claim of ₱5,796 million for the years 1994 - 1998 and 2000, arising from the *SC* decision (net of ₱894 million as approved by the *BIR* for taxable year 2001). In a decision dated December 6, 2010, the *CTA*'s Second Division granted *MERALCO*'s claim and ordered the *BIR* to refund or to issue tax credit certificate in favor of *MERALCO* in the amount of



₱5,796 million in proportion to the tax withheld on the total amount that has been actually given or credited to its customers.

On appeal by the *BIR* to the *CTA En Banc*, *MERALCO*'s petition was dismissed on the ground of prescription in the Decision of the *CTA En Banc* dated May 8, 2012. On Motion for Reconsideration by *MERALCO* of the said dismissal, the *CTA En Banc* partly granted *MERALCO*'s motion and issued an Amended Decision dated November 13, 2012, ruling that *MERALCO*'s claim was not yet barred by prescription and remanding the case back to the *CTA Second Division* for further reception of evidence.

The *BIR* filed a Motion for Reconsideration of the above Amended Decision, while *MERALCO* filed its Motion for Partial Reconsideration or Clarification of Amended Decision. Both parties filed their respective Comments to the said motions, and these were submitted for resolution at the *CTA En Banc*.

In a Resolution promulgated on May 22, 2013, the *CTA* denied the said motions of the *BIR* and *MERALCO*, and the *CTA Second Division* was ordered to receive evidence and rebuttal evidence relating to *MERALCO*'s level of refund to customers, pertaining to the excess charges it made in taxable years 1994-1998 and 2000, but corresponding to the amount of ₱5,796 million, as already determined by the said court.

On July 12, 2013, the *BIR* appealed the *CTA En Banc*'s Amended Decision dated November 13, 2012 and Resolution dated May 22, 2013 via Petition for Review with the *SC*.

Overpayment of Income Tax Related to Change in Tax Basis

On February 4, 2008, the *SC* denied with finality a motion for reconsideration filed by the Commissioner of Internal Revenue or *CIR*, against *MERALCO*, with respect to the issue on excess income tax paid by the latter. The *SC* affirmed a *CA* decision and ordered the *CIR* to refund or issue a *TCC* in favor of *MERALCO* for ₱107 million representing overpaid income taxes for taxable years 1987 and 1988. The overpayment is in accordance with the effectivity of Executive Order No. 72, which subjected *MERALCO* to regular corporate income tax instead of 2% franchise tax based on gross receipts it was previously liable for. On February 5, 2013, *MERALCO* filed a Motion for Issuance of a Writ of Execution with the *CTA* to enforce the judgment of the *SC*. On February 14, 2013, the *CTA* promulgated a Resolution ordering the *CIR* and the *OSG* to comment on the Motion filed by *MERALCO*. On March 14, 2013, the *CTA* promulgated a Resolution granting the Motion of *MERALCO* and directed the issuance of corresponding Writ of Execution.

LFT Assessments of Municipalities

Certain municipalities have served assessment notices on *MERALCO* for *LFT*. As provided in the Local Government Code or *LGC*, only cities and provincial governments may impose taxes on establishments doing business in their localities. On the basis of the foregoing, *MERALCO* and its legal counsel believe that *MERALCO* is not subject or liable for such assessments.

Real Property Tax or RPT Assessments

Several Local Government Units or *LGUs*, assessed *MERALCO* for deficiency *RPTs* on certain assets of *MERALCO*. The assets include electric poles, wires, insulators, and transformers, collectively referred to as *TWIP*. Of these *LGUs*, one has secured a favorable decision from the *CA*. Such decision was appealed by *MERALCO* to the *SC* for the benefit of *MERALCO* customers, where



it is now submitted for resolution. The cases of the other *LGUs* are pending with their respective administrative bodies or government offices.

MERALCO also filed a case against the City of Manila before Regional Trial Court – Pasig branch or *RTC-Pasig*, to enjoin the collection of *RPT* on *MERALCO*'s *TWIP* and nullify *RPT* assessments made thereon based on the argument that these are not within the ambit of the definition of real property under the *LGC*. The case is set for mediation after the City of Manila filed its comments on *MERALCO*'s petition.

In the event that the assessment is sustained by the *SC* and payment is warranted or appropriate, *MERALCO* will file for the recovery of any resulting *RPT* payments from customers in the relevant *LGU* through a separate application with the *ERC*.

Mediation with NPC

The *NPC* embarked on a Power Development Program or *PDP*, which consisted of contracting generating capacities and the construction of its own, as well as private sector, generating plants, following a crippling power supply crisis. To address the concerns of the creditors of *NPC*, namely, Asian Development Bank and the World Bank, the Department of Energy or *DOE* required that *MERALCO* enter into a long-term supply contract with the *NPC*.

Accordingly, on November 21, 1994, *MERALCO* entered into a 10-year Contract for Sale of Electricity or *CSE*, with *NPC* to commence on January 1, 1995. The *CSE* and the rates and amounts charged to *MERALCO* therein, were approved by the *BOD* of *NPC* and the then Energy Regulatory Board, respectively.

Separately, the *DOE* further asked *MERALCO* to provide a market for half of the output of the Camago–Malampaya gas field to enable its development and production of natural gas, which was to generate significant revenues for the Philippine Government and equally significant foreign exchange savings for the country to the extent of the fuel imports, which the domestic volume of natural gas will displace.

MERALCO's actual purchases from *NPC* exceeded the contract level in the first seven years of the *CSE*. However, the 1997 Asian crisis resulted in a significant curtailment of energy demand.

While the events were beyond the control of *MERALCO*, *NPC* did not honor *MERALCO*'s good faith notification of its off-take volumes. A dispute ensued and both parties agreed to enter into mediation.

The mediation resulted in the signing of a Settlement Agreement or *SA*, between the parties on July 15, 2003. The *SA* was approved by the respective *BODs* of *NPC* and *MERALCO*. The net settlement amount of ₱14,320 million was agreed upon by *NPC* and *MERALCO* and manifested before the *ERC* through a Joint Compliance dated January 19, 2006. The implementation of the *SA* is subject to the approval of *ERC*.

Subsequently, the Office of the Solicitor General or *OSG* filed a "Motion for Leave to Intervene with Motion to Admit Attached Opposition to the Joint Application and Settlement Agreement between *NPC* and *MERALCO*." As a result, *MERALCO* sought judicial clarification with the *RTC-Pasig*. Pre-trials were set which *MERALCO* complied with and attended. However, the *OSG* refused to participate in the pre-trial and opted to seek a *TRO* from the *CA*.



In a Resolution dated December 1, 2010, the *CA* issued a *TRO* against *RTC-Pasig*, *MERALCO* and *NPC* restraining the respondents from further proceeding with the case. Subsequently, in a Resolution dated February 3, 2011, the *CA* issued a writ of preliminary injunction enjoining the *RTC-Pasig* from conducting further proceedings pending resolution of the Petition. In a Decision dated October 14, 2011, the *CA* resolved to deny the Petition filed by the *OSG* and lifted the injunction previously issued. The said Decision likewise held that the *RTC-Pasig* committed no error in finding the *OSG* in default due to its failure to participate in the proceedings. The *RTC-Pasig* was thus ordered to proceed to hear the case *ex-parte*, as against the *OSG*, and with dispatch. The *OSG* filed a motion for reconsideration which was denied by the *CA* in its Resolution dated April 25, 2012. The *OSG* filed a Petition for Review on Certiorari with the *SC*. In a Resolution dated July 25, 2012, the *SC* required *MERALCO* to file a Comment. *MERALCO*'s Comment was filed on October 29, 2012. The *SC* then issued a Resolution dated November 26, 2012 requiring the *OSG* to file a Reply. On February 19, 2013, the *OSG* filed a motion for extension to file a consolidated reply.

With the dismissal of the petition filed by the *OSG* with the *CA*, *MERALCO* filed a motion for the reception of its evidence *ex-parte* with the *RTC-Pasig* pursuant to the ruling of the *CA*. In a Decision dated May 29, 2012, the *RTC-Pasig* declared the *SA*, independent of the pass-through for the settlement amount which is reserved for the *ERC*, valid and binding. The *OSG* has filed a Notice of Appeal with the *RTC-Pasig* on June 19, 2012. Both parties have filed their respective appeal briefs. The case is deemed submitted for resolution by the *CA*.

On January 22, 2014, *MERALCO* received a Notice of Judgment from the *SC* stating that a Decision dated December 11, 2013 was rendered by the First Division of the *SC* denying the Petition for Review on Certiorari by the *OSG* and affirming the decision promulgated by the *CA* on October 14, 2011.

Sucat-Araneta-Balintawak Transmission Line

The Sucat-Araneta-Balintawak transmission line is a two-part transmission line, which completed the 230kV-line loop within Metro Manila. The two main parts are the Araneta to Balintawak leg and the Sucat to Araneta leg, which cuts through Dasmariñas Village, Makati City.

On March 10, 2000, certain residents along Tamarind Road, Dasmariñas Village, Makati City or plaintiffs, filed a case against *NPC* with the *RTC-Makati*, enjoining *NPC* from further installing high voltage cables near the plaintiffs' homes and from energizing and transmitting high voltage electric current through said cables because of the alleged health risks and danger posed by the same. Following its initial status quo Order issued on March 13, 2000, *RTC-Makati* granted on April 3, 2000 the preliminary injunction sought for by the plaintiffs. The decision was affirmed by the *SC* on March 23, 2006, which effectively reversing a decision of the *CA* to the contrary. The *RTC-Makati* subsequently issued a writ of execution based on the order of the *SC*. *MERALCO*, in its capacity as an intervenor, was constrained to file an Omnibus Motion to maintain status quo because of the significant effect of a de-energization of the Sucat-Araneta line to the public and economy. Shutdown of the 230-kV line will result in widespread and rotating brownouts within *MERALCO*'s franchise area with certain power plants unable to run at their full capacities.

On September 8, 2009, the *RTC-Makati* granted the motions for intervention filed by intervenors *MERALCO* and *NGCP* and dissolved the Writ of Preliminary Injunction issued, upon the posting of the respective counter bonds by defendant *NPC*, intervenors *MERALCO* and *NGCP*, subject to the condition that *NPC* and intervenors pay all damages, which the plaintiffs may incur as a result of the Writ of Preliminary Injunction.



Thereafter, the plaintiffs questioned the *RTC-Makati* order before the *CA*. As at March 17, 2014, this case remains pending for resolution in the *CA*.

Moreover, in its Order dated February 5, 2013, the *RTC-Makati* granted plaintiffs' motion and directed the re-raffle of the case to another court after the judicial dispute resolution failed.

Petition for Dispute Resolution against PEMC, TransCo, NPC and PSALM

On September 9, 2008, *MERALCO* filed a Petition for Dispute Resolution, against *PEMC*, *TransCo*, *NPC* and *PSALM* with the *ERC* as a result of the congestion in the transmission system of *TransCo* arising from the outages of the San Jose-Tayabas 500kV Line 2 on June 22, 2008, and the 500kV 600 Mega volt-ampere Transformer Bank No. 2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The Petition seeks to, among others, direct *PEMC* to adopt the *NPC-TOU* rate or the new price determined through the price substitution methodology of *PEMC* as approved by the *ERC*, as basis for its billing during the period of the congestion and direct *NPC* and *PSALM* to refund the transmission line loss components of the line rentals associated with *NPC/PSALM* bilateral transactions from the start of *WESM* operation on June 26, 2006.

In a Decision dated March 10, 2010, the *ERC* granted *MERALCO*'s petition and ruled that there is double charging of the Transmission Line Costs billed to *MERALCO* by *NPC* for the *TSC* quantities to the extent of 2.98% loss factor, since the start of the *TSC* in November 2006. Thus, *NPC* was directed to refund/collect line rental adjustment to/from *MERALCO*. In the meantime, the *ERC* issued an Order on May 4, 2011 directing *PEMC* to submit an alternative methodology for the segregation of line rental into congestion cost and line losses from the start of the *WESM*. *PEMC* has filed its compliance submitting its alternative methodology.

On September 8, 2011, *MERALCO* received a copy of *PEMC*'s compliance to *ERC*'s directive and on November 11, 2011, *MERALCO* filed a counter-proposal which effectively simplifies *PEMC*'s proposal.

On November 11, 2011, *MERALCO* filed its Motion to Implement the Decision dated March 10, 2010 by immediately effecting the refund/collection of line rental adjustments to consumers. On December 21, 2011, *PSALM* filed its comment on *MERALCO*'s said Motion. Then, in an Order dated January 24, 2012, the *ERC* directed *PEMC*, *Transco* and *NPC* to submit their respective comments on *MERALCO*'s motion within five days from receipt.

In an Order of the *ERC* dated June 21, 2012, *MERALCO* was directed to submit its computation of the amount of the double charging of line loss on a per month basis from June 26, 2006 up to June 2012. On July 4, 2012, *MERALCO* filed its Compliance to the said Order. Thereafter, the *ERC* issued an Order directing the parties to comment on *MERALCO*'s submissions.

In an Order dated March 4, 2013, the *ERC* approved the methodology proposed by *MERALCO* and *PEMC* in computing the double charged amount on line losses by deducting 2.98% from the *NPC-TOU* amount. Accordingly, the *ERC* determined that the computed double charge amount to be collected from *NPC* is ₱5.2 billion, covering the period November 2006 to August 2012 until actual cessation of the collection of the 2.98% line loss charge in the *NPC-TOU* rates imposed on *MERALCO*, while the amount to be collected from the *SGCs* is ₱4.7 billion. Additionally, *MERALCO* was directed to file a petition against the following *SGCs*: *MPPCL*, Aboitiz Power Renewables, Inc. or *APRI*, *TLI*, *SMEC* and *SCPC*, within thirty (30) days from receipt thereof, to recover the line loss collected by them. *MERALCO* filed a motion for clarification with the *ERC* regarding the directives contained in the March 4, 2013 Order. On April 30, 2013 and May 8, 2013, *PSALM* and *NPC*, respectively, filed motions seeking reconsideration of the March 4, 2013 Order.



In an Order dated July 1, 2013, the *ERC* issued the following clarifications/resolutions: 1) *SPPC* should be included as one of the *SGCs* against whom a petition for dispute resolution should be filed by *MERALCO*; 2) Amount to be refunded by *NPC* is not only ₱5.2 billion but also the subsequent payments it received from *MERALCO* beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates and Petition to be filed by *MERALCO* against the *SGCs* should not only be for the recovery of the amount of ₱4.7 billion but also the subsequent payments beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates. ; 3) “*SCPC Ilijan*” pertains to *SPPC* instead. Thus, the refundable amount of ₱706 million pertaining to “*SCPC Ilijan*” should be added to *SPPC*’s refundable amount of ₱1.1 billion; 4) Grant the “*Motion for Extension*” filed by *MERALCO* which was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC*, *Sem-Calaca* and *SPPC*, otherwise, it shall be the one liable to refund the subject amount to its customers; and 5) deny the respective “*Motions for Reconsideration*” filed by *NPC* and *PSALM*.

On September 12, 2013, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking approval of its proposal to offset the amount of ₱74 million against some of its monthly remittances to *PSALM*. *PSALM* and *NPC* filed their comments *ad cautelam* on *MERALCO*’s Manifestation and Motion. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion. On November 4, 2013, *MERALCO* filed its Reply. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion.

On October 24, 2013, *MERALCO* received *PSALM*’s Petition for Review on Certiorari with the *CA* (With Urgent *TRO* and/or Writ of Preliminary Mandatory Injunction Applications) questioning the March 4, 2013 and July 1, 2013 Orders of the *ERC*. In a Resolution dated December 29, 2013, the *CA* gave *MERALCO* until December 26, 2013, within which to submit its Comment on the Petition for Review on Certiorari and to show cause why the prayer for the Application for *TRO* and/or Preliminary Injunction should not be granted (“*Comment and Opposition*”). On December 23, 2013, January 5, 2014 and January 15, 2014, *MERALCO* requested for an additional period of ten (10) days each, within which to submit its *Comment and Opposition*.

On February 2, 2014, *MERALCO* filed its Comment to said Petition. As at March 17, 2014, the *CA* has yet to rule on the Petition.

Petition for Dispute Resolution Against SPPC, MPPCL, APRI, TLI, SMEC and Sem-Calaca

On August 29, 2013, *MERALCO* filed a Petition for Dispute Resolution against *SPPC*, *MPPCL*, *APRI*, *TLI*, *SMEC* and *Sem-Calaca*. Said Petition seeks the following: a) Refund of the 2.98% transmission line losses in the amount of ₱5.4 billion from said *SGCs*; and 2) approval of *MERALCO*’s proposal to correspondingly refund to its customers the aforementioned line loss amounts, as and when the same are received from the *SGCs*, until such time that the said over-recoveries are fully refunded, by way of automatic deduction of the amount of refund from the computed monthly generation rate. On September 20, 2013, *MERALCO* received the *SGCs*’ Joint Motion to Dismiss. On October 7, 2013, *MERALCO* filed its Comment on the said Joint Motion. On October 8, 2013, *MERALCO* received the *SGCs* Manifestation and Motion. On October 14, 2013, *MERALCO* filed its Opposition thereto. On October 24, 2013, *MERALCO* received the *SGC*’s Reply to its Comment. On October 29, 2013, *MERALCO* filed its Rejoinder.



PSALM versus PEMC and MERALCO

Due to the unusually large increases in *WESM* prices during the 3rd and 4th months of the *WESM* operations, *MERALCO* raised concerns with the *PEMC* to investigate whether *WESM* rules were breached or if anti-competitive behavior had occurred.

While resolutions were initially issued by the *PEMC* directing adjustments of *WESM* settlement amounts, a series of exchanges and appeals with the *ERC* ensued. *ERC*'s decision directing the *WESM* settlement price for the 3rd and 4th billing months to be *NPC-TOU* rates prompted *PSALM* to file a Motion for Reconsideration with the *CA*, which was denied on November 6, 2009. In December 2009, *PSALM* filed a Petition for Review on Certiorari with the *SC*.

As at March 17, 2014, *PSALM*'s Petition for Review is pending resolution by the *SC*.

Petition for Dispute Resolution with NPC on Premium Charges

On June 2, 2009, *MERALCO* filed a Petition for Dispute Resolution against *NPC* and *PSALM* with respect to *NPC*'s imposition of premium charges for the alleged excess energy it supplied to *MERALCO* covering the billing periods May 2005 to June 2006. The premium charges amounting to ₱315 million during the May-June 2005 billing periods have been paid but are the subject of a protest by *MERALCO*, and premium charges of ₱318 million during the November 2005, February 2006 and April to June 2006 billing periods are being disputed and withheld by *MERALCO*. *MERALCO* believes that there is no basis for the imposition of the premium charges. The hearings on this case have been completed and *MERALCO* is now awaiting the resolution of the *ERC* on the petition.

SC Temporary Restraining Order on MERALCO's December 2013 Billing Rate Increase

On December 9, 2013, the *ERC* gave clearance to the request of *MERALCO* to implement a staggered collection over three (3) months covering the December 2013 billing month for the increase in generation charge and other bill components such as *VAT*, *LFT*, transmission charge, and *SL* charge, which reflected a total increase of ₱4.15 per *kWh* for a 200-*kWh* residential consumer. The generation costs for the November 2013 supply month increased significantly because of the use of the more expensive liquid fuel by the natural gas-fired power plants that were affected by the Malampaya Gas Field or *Malampaya*, shutdown from November 11 to December 10, 2013. This was compounded by the aberrant spike in the *WESM*, charges on account of the scheduled and extended shutdowns, and the forced outages, of several base load power plants, as well as the non-compliance with *WESM* Rules by certain plants resulting in significant power generation capacities not being offered and dispatched.

The Department of Justice commenced an investigation while the House of Representatives and the Senate conducted separate hearings to determine the underlying reasons for the price increase, including any possible collusion among the power firms. In the meantime, *MERALCO* proceeded with billing its captive customers with the *ERC* approval.

On December 19, 2013, several interest groups filed a Petition against *MERALCO*, *ERC* and the *DOE* before the *SC*, questioning the *ERC* clearance granted to *MERALCO* to charge the ₱4.15 per *kWh* price increase, alleging the lack of hearing and due process. It also sought for the declaration of the unconstitutionality of the *EPIRA*, which essentially declared the generation and supply sectors competitive and open, and not considered public utilities. A similar petition was filed by a consumer group and several private homeowners associations challenging also the legality of the *AGRA* that



the *ERC* had promulgated. Both petitions prayed for the issuance of *TRO*, and a Writ of Preliminary Injunction.

On December 23, 2013, the *SC* consolidated the two (2) Petitions and granted the application for *TRO* effective immediately and for a period of sixty (60) days, which effectively enjoined the *ERC* and *MERALCO* from implementing the ₱4.15 per *kWh* price increase. The *SC* also ordered *MERALCO*, *ERC* and *DOE* to file their respective comments to the Petitions and set the hearing for Oral Arguments on January 21, 2014. The *SC* further set two more Oral Arguments on February 4, 2014 and February 11, 2014. After the conclusion of the Oral Arguments, the *SC* ordered all the Parties to the consolidated Petitions to file their respective Memorandum on or before February 26, 2014 after which the Petitions will be deemed submitted for resolution of the *SC*. *MERALCO* complied with said directive and filed its Memorandum on said date.

On February 18, 2014, acting on the motion filed by the Petitioners, the *SC* extended for another period of 60 days or until April 22, 2014, the *TRO* that it originally issued against *MERALCO* and *ERC* last December 23, 2013. The *TRO* was also similarly applied to the generating companies, specifically *MPPCL*, *SMEC*, *SPPC*, *FGPC*, and the *NGCP*, and the *PEMC* (the administrator of *WESM* and market operator) who were all enjoined from collecting from *MERALCO* the deferred amounts representing the ₱4.15 per *kWh* price increase for the November 2013 supply month.

In the meantime, on January 30, 2014, *MERALCO* filed an Omnibus Motion with Manifestation with the *ERC* for the latter to direct *PEMC* to conduct a re-run or re-calculation of the *WESM* prices for the supply months of November to December 2013. Subsequently, on February 17, 2014, *MERALCO* filed with the *ERC* an Application for the recovery of deferred generation costs for the December 2013 supply month praying that it be allowed to recover the same over a six (6)-month period.

On March 3, 2014, the *ERC* issued an Order voiding the Luzon *WESM* prices given that the prices in *WESM* during the November and December 2013 supply months could not qualify as reasonable, rational and competitive. *PEMC* was given seven (7) days upon receipt of the Order to calculate these regulated prices and implement the same in the revised *WESM* bills of the concerned.

As at March 17, 2014, *MERALCO* is still awaiting decisions of the *SC* on the *TRO*.

Others

Management and its internal and external counsels believe that the probable resolution of these issues will not materially affect the *MERALCO Group*'s financial position and results of operations.

31. Significant Contracts and Commitments

NPC

MERALCO and *NPC* entered into a Transition Supply Contract or *TSC*, effective the earlier of five years from November 16, 2006 up to December 25, 2011 or one year after the introduction of Open Access, should *RCOA* be in place within the five-year contract period. Two addenda for additional contracted volumes were signed, the most recent being in 2010. The adjusted contracted volume was for a total of more than 40,000 *GWh* up to 2011.



On December 26, 2011, the *TSC* with *NPC* was extended until December 25, 2012 or three months after the implementation of the *RCOA*, whichever comes first.

As a result of the extension of the *TSC*, the Customer Choice Program or *CCP*, which is a joint program of *NPC* and *MERALCO* aimed at providing *NPC* time-of-use or *TOU*, benefits to qualified customers, has also been extended to be co-terminus with the *TSC*. The *CCP* expired on December 25, 2012.

With respect to the *TSC*, *MERALCO*, *NPC* and *PSALM* then executed a Memorandum of Agreement or *MOA* which further extended the *TSC* until June 25, 2013.

On June 26, 2013, *MERALCO*'s *TSC* with *NPC* was terminated.

Assignment of TSC Volume to SGCS

From 2008 to 2009, *NPC* privatized a number of its generating assets and Independent Power Plants or *IPP* contracts in favor of the successful bidders. As a result, the contracted energy volume under the original *TSC* between *MERALCO* and *NPC* was assigned by *NPC* to the respective new owners and *IPPs*. Following are the privatized plants and *IPP* contracts:

Year	Power Plant	Successor Owner/ <i>IPPs</i>	% of Total Volume
2008	Masinloc coal-fired power plant – 600 <i>MW</i>	<i>MPPCL</i>	21.3
2009	Tiwi-Makban geothermal power plants – 289 <i>MW</i>	<i>APRI</i>	8.1
	Pagbilao power plant – 735 <i>MW</i>	<i>TLI</i>	25.0
	Sual coal-fired power plant – 1,000 <i>MW</i>	<i>SMEC</i>	8.6
	Coal-fired Calaca power plant – 600 <i>MW</i>	<i>Sem-Calaca</i>	10.4
2010	Combined cycle gas turbine, natural gas-fired Ilijan power plant – 1,200 <i>MW</i>	<i>SPPC</i>	15.2

NPC/PSALM remained the contracting party of record for the supply of power to *MERALCO*. Payments of the contracted volume are made based on the billing instructions from *NPC/PSALM* received by *MERALCO*.

PSAs with Privatized Plants and IPPs

MERALCO entered into separate *PSAs* with *SPPC*, *Sem-Calaca* and *MPPCL* on December 12, 20 and 21, 2011, respectively. Also, a *PSA* with *TLI* was executed on February 29, 2012. These *PSAs* are for a period of seven years, extendable for three years upon agreement of the parties.

In March 2012, the application for approval of the *PSAs* was filed with the *ERC*. On June 26, 2012, *MERALCO BOD* approved the grant of authority to *MERALCO* to enter into a *PSA* with *SMEC* for a period of seven years, extendable for three years upon agreement of the parties.

On March 16, 2012, *MPower* signed a separate *PSA* with *MPPCL* for 30*MW* of contracted capacity from the Masinloc coal-fired power plant in Zambales for seven years, extendable for three years upon agreement of the parties.

On April 26, 2012, the *BOD* approved the *PSA* with Pangea Green Energy Philippines, Inc., or *PGEP*, a biogas power plant located in Payatas, Quezon City using methane gas extracted from the Payatas Landfill as its fuel. Its plant has a total nominal generating capacity of 1,236 *kW*.



In separate Decisions dated December 17, 2012, the *ERC* approved with modifications the *PSAs* of *MERALCO* with *MPPCL*, *SPPC*, *Sem-Calaca*, *TLI* and *SMEC*.

Motions for Reconsideration were filed regarding the *ERC* decisions on the *PSAs* with *SPPC*, *Sem-Calaca* and *SMEC*. *MERALCO* is awaiting the decision of the *ERC*.

On December 27, 2012, *MERALCO* executed the *PSAs* with *TLI* and *APRI* to cover the volume needed by *MERALCO* during the six-month transition period before the start of the commercial operations of *RCOA*. Under the *PSAs* with *TLI* and *APRI*, *MERALCO* will procure power from *TLI* and *APRI* from the expiration of the *TSC* until June 25, 2013 conditioned upon *ERC* approval. The said *PSAs* had been submitted to the *ERC* for approval on January 2, 2013. However, on September 26, 2013, *MERALCO* filed Motions to Withdraw the said *PSAs*, considering that the *TSC* was extended up to June 25, 2013. The *ERC* granted said Motions in separate Orders dated September 27, 2013.

Under the *PSAs*, fixed capacity fees and fixed operating maintenance fees are recognized monthly based on their contracted capacities. The annual projection of these payments is shown in the table below:

Year	Contracted Capacity	Fixed Payment Amount
	<i>(In Megawatt)</i>	<i>(In million)</i>
2014	3,000	₱35,419
2015	3,084	37,775
2016	3,114	39,865
2017	3,114	39,574
2018	2,880	39,198
2019	2,460	33,864

FGPC and FGP

In compliance with the *DOE*'s program to create a market for Camago-Malampaya gas field and enable its development, *MERALCO* was committed to contract 1,500-MW of the 2,700 MW output of the Malampaya gas field.

Accordingly, *MERALCO* entered into separate 25-year *PPAs* with *FGPC* (March 14, 1995) and *FGP* (July 22, 1999) for a minimum number of *kWh* of the net electrical output of the Sta. Rita and San Lorenzo power plants, respectively, from the start of their commercial operations. The *PPA* with *FGPC* terminates on August 17, 2025, while that of *FGP* ends on October 1, 2027.

On January 7, 2004, *MERALCO*, *FGP* and *FGPC* signed an Amendment to their respective *PPAs*. The negotiations resulted in certain new conditions including the assumption of *FGP* and *FGPC* of community taxes at current tax rate, and subject to certain conditions increasing the discounts on excess generation, payment of higher penalties for non-performance up to a capped amount, recovery of accumulated deemed delivered energy until 2011 resulting in the non-charging of *MERALCO* of excess generation charge for such energy delivered beyond the contracted amount but within a 90% capacity quota. The amended terms under the respective *PPAs* of *FGP* and *FGPC* were approved by the *ERC* on May 31, 2006.



Under the respective *PPAs* of *FGP* and *FGPC*, the fixed capacity fees and fixed operating and maintenance fees are recognized monthly based on the actual Net Dependable Capacity tested and proven, which is usually conducted on a semi-annual basis.

QPPL

MERALCO entered into a *PPA* with *QPPL* on August 12, 1994, which was subsequently amended on December 1, 1996. Under the terms of the amended *PPA*, *MERALCO* is committed to purchase a specified volume of electric power and energy from *QPPL*, subject to certain terms and conditions. The *PPA* is for a period of 25 years from the start of commercial operations up to July 12, 2025.

In a Letter Agreement signed on February 21, 2008, the amount billable by *QPPL* included a transmission line charge reduction in lieu of a previous rebate program. The Letter Agreement also provides that *MERALCO* make advances to *QPPL* of US\$2.85 million per annum for 10 years beginning 2008 to assist *QPPL* in consideration of the difference between the transmission line charge specified in the *TLA* and the *ERC*-approved transmission line charge in March 2003. *QPPL* shall repay *MERALCO* the same amount at the end of the 10-year period in equal annual payments without adjustment. However, if *MERALCO* is able to dispatch *QPPL* at a plant capacity factor of no less than 86% in any particular year, *MERALCO* shall not be required to pay US\$2.85 million in that year. This arrangement did not have any impact on the rates to be charged to consumers and hence, did not require any amendment in the *PPA*, as approved by *ERC*.

See Note 11 – Other Noncurrent Assets.

Committed Energy Volume to be Purchased

The following are forecasted purchases/payments to *FGPC*, *FGP* and *QPPL* corresponding to the Minimum Energy Quantity or *MEQ*, provisions of the contracts. The forecasted fixed payments include capacity charge and fixed operation and maintenance cost escalated using the US and Philippine Consumer Price Index or *CPI*.

Year	Minimum Energy Quantity (MEQ) <i>(In Million Kilowatt-Hours)</i>	Equivalent Amount <i>(In millions)</i>
2014	14,955	₱21,476
2015	14,955	21,577
2016	14,855	21,592
2017	14,855	21,817
2018	14,855	22,011
2019-2025	103,984	159,967

Montalban Methane Power Corporation or MMPC

MMPC operates an 8 *MW* (designed capacity of 11 *MW*) renewable energy generating facility, which utilizes landfill gas.

On May 13, 2009, *MERALCO* filed an application for the approval of the *CSE* with *MMPC* with the *ERC*. On June 9, 2009, *ERC* issued an order dated June 1, 2009 provisionally approving the *CSE* subject to the following conditions: (i) any amendments to the *CSE* shall be filed with the *ERC* for approval and the implementation shall be prospective; and (ii) in the event the rates approved are higher than the final rates, the amount corresponding to the excess shall be refunded by *MERALCO* to its customers by crediting the same in their electric bills.



On June 11, 2009, *MMPC* began delivering energy to *MERALCO* under a two year *CSE*. The *CSE* is a “take and pay” arrangement, without a minimum energy volume. Energy is billed to *MERALCO* on an hourly basis at the *ERC*- approved *NPC TOU* rate plus certain pre-agreed cost components. Being an embedded renewable energy generator, purchases from *MMPC* are *VAT* zero-rated and energy deliveries from *MMPC* are exempt from power delivery service charge.

After a series of negotiations, on May 23, 2011, *MERALCO* and *MMPC* signed a Letter Agreement extending the *CSE*. Said Agreement likewise contained minor amendments to the *CSE* that were intended to benefit the consumers. On June 3, 2011, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking the approval of the Letter Agreement, pursuant to the condition contained in the *ERC* Order dated June 1, 2009. On February 19, 2013, the *ERC* issued its Decision approving the application.

BEI

MERALCO signed a *CSE* with *BEI* on November 12, 2010. *BEI* owns and operates a 4*MW* renewable energy generation facility powered by landfill gas in San Pedro, Laguna.

The terms of the *CSE* with *BEI* are similar to that signed with *MMPC*. Purchases from *BEI*, an embedded renewable energy generator, are *VAT* zero-rated and exempt from power delivery service charge. *MERALCO* filed an application for the approval of the *CSE* with the *ERC*, for the provisional implementation of the contract on December 15, 2010. In an order dated January 31, 2011, the *ERC* provisionally approved the said application which extended the implementation indefinitely. The said case is pending decision by the *ERC*.

Therma Mobile, Inc. or TMO

On March 4, 2013, *MERALCO* signed an Interconnection Agreement with *Therma Mobile Inc. or TMO* for their 243 *MW* generating facility at the Navotas Fish Port Complex, Navotas City, which is an interconnection at *MERALCO*’s Grace Park - Malabon 115kV line. *TMO* is thus an embedded generator. *TMO* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*’s system.

On September 27, 2013, *MERALCO* signed a *PSA* with *TMO* for the output of the barge-mounted, bunker oil-fired diesel engines moored at the Fishport Complex in Navotas, Manila. On November 4, 2013, the application for approval of the *MERALCO-TMO PSA* was provisionally approved by the *ERC*.

Interconnection Agreement with Alternergy Philippine Holdings Corporation or Alternergy

On March 1, 2012, *MERALCO* signed an Interconnection Agreement with *Alternergy* for their 90*MW* Wind Farm Renewable Energy plant in Pililla, Rizal, which is an interconnection at *MERALCO*’s Malaya-Teresa 115kV line, *Alternergy* is thus an embedded generator. *Alternergy* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*’s system.



Interconnection Agreement with Maibarara Geothermal, Inc. or MGI

On December 6, 2012, *MERALCO* signed an Interconnection Agreement with *MGI* for their 20MW (with max capacity of 40 MW) Geothermal Facility plant in Sto. Tomas, Batangas, which is an interconnection at *MERALCO*'s FPIP - Los Banos 115kV line. *MGI* is thus an embedded generator. *MGI* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*'s system.

32. Earnings Per Share Attributable to Equity Holders of the Parent

Basic and diluted earnings per share are calculated as follows:

	2013	2012 (As restated - see Note 4)	2011 (As restated - see Note 4)
<i>(In millions, except per share data)</i>			
Net income attributable to equity holders of the Parent (a)	₱17,211	₱17,117	₱13,260
Weighted average common shares outstanding (b)	1,127	1,127	1,127
Per Share Amounts:			
Basic and diluted earnings per share (a/b)	₱15.27	₱15.19	₱11.76
Net income attributable to equity holders of the Parent of continuing operations (a)	₱17,211	₱16,236	₱12,748
Weighted average common shares outstanding (b)	1,127	1,127	1,127
Per Share Amounts:			
Basic and diluted earnings per share of continuing operations (a/b)	₱15.27	₱14.40	₱11.31
Basic and diluted earnings per share of discontinued operations	₱—	₱0.86	₱0.86

Basic and diluted earnings per share amounts are calculated by dividing net income for the year attributable to common shareholders of the parent by the weighted average number of common shares outstanding during the year. There are no potential dilutive common shares in 2013, 2012 and 2011.

There are no other transactions involving common shares or potential common shares between the reporting date and the date of completion of these consolidated financial statements.

To calculate earnings per share amounts for the discontinued operations, the weighted average number of common shares for both basic and diluted amounts is as per the table above.



33. Other Matters

Revised SL Caps

On December 8, 2008, the *ERC* promulgated a resolution providing for a lower maximum rate of *SL* (technical and non-technical) that a utility can pass on to its customers. The revised *SL* cap is 8.5% for private utilities, effective January 2010 billing. This is one percentage point lower than the *SL* cap of 9.5% provided under *RA* No. 7832. The actual volume of electricity used by *MERALCO* (administrative loss) is treated as part of the operation and maintenance expense beginning July 2011. The manner by which the utility is rewarded for its efforts in *SL* reduction is addressed by the *ERC* in the *PIS* under *PBR*.

On December 8, 2009, *MERALCO* filed a Petition to amend the said Resolution with an urgent prayer for the immediate suspension of the implementation of the new *SL* cap of 8.5% starting January 2010. The proposed amendment is aimed at making the Resolution consistent with the provisions of *RA* No. 9136 and *RA* No. 7832, by increasing the *SL* cap to not less than 9%. The hearing on the Petition was conducted on November 18, 2010. Thereafter, *MERALCO* was directed to submit its *FOE*. *MERALCO* has submitted its *FOE* and is awaiting *ERC* decision on this Petition.

Benefit Sharing Scheme to Lower System Loss

On January 26, 2011, *MERALCO*, together with Private Electric Power Operators Association, Inc. or *PEPOA* and Philippine Rural Electric Cooperative Association or *PHILRECA*, filed a joint petition to the *ERC* to initiate rule-making to adopt the *Proposed Guidelines for the Implementation of an Incentive Scheme to Lower the System Losses of Private Distribution Utilities and Electric Cooperatives to Level Below the System Loss Cap, for the Benefit of End-Users*. This was aimed to encourage the *DUs* to reduce system loss levels below the cap set by the *ERC* and benefit the end-users through lower system loss charges. Public hearings were conducted and completed on June 15, 2011.

On December 11, 2012, the *ERC* posted on its website the second draft of the *Rules to Govern the Implementation of a Benefit Sharing to Lower the System Losses of Electric Distribution Utilities*. The salient points of the second draft rules include calculation of System Loss Charge using the prevailing system loss cap or the lowest consecutive five year average system loss, whichever is lower, and an equitable sharing (50-50) of incentives between the customer and the *DU* on the savings which is the difference between the lower of this system loss level and the *DU*'s actual system loss. Any system loss reward from the *PIS* under the *RDWR* for private *DUs* shall be offset from the rewards the *DU* will receive from this Benefit-Sharing scheme, except when the net benefit from this scheme is less than the *PIS* rewards of the *DU*, in which case the *DU* will retain the rewards under the *PIS* and forego its share under this Benefit-Sharing Scheme. The foregone share of the *DU* shall be added to the End-user share correspondingly. As at March 17, 2014, *MERALCO* and *PEPOA* are awaiting the action of the *ERC* on this matter.

Retail Competition

On February 24, 2012, the *DOE* issued a circular designating the *PEMC* as the Central Registration Body, or *CRB* under the *RCOA*. The *CRB* is tasked to develop market infrastructure, systems and processes capable of supporting *RCOA* registration, customer switching and information exchange among industry participants.



On May 9, 2012, the *DOE* issued another circular prescribing the general policies for the implementation of *RCOA*. The circular provides the overall direction *DOE* intends to take in developing the policy framework for *RCOA* implementation.

On September 27, 2012, the *DOE* and the *ERC* issued a joint statement setting the initial *RCOA* implementation on December 26, 2012. The joint statement clarified that the *RCOA* commencement is on a phase-in and partial implementation of the program, with the first six (6) months of *RCOA* implementation (December 26, 2012 – June 25, 2013) allotted as the Transition Period to allow all concerned parties to undertake their respective preparations to operationalize the mechanism for *RCOA*. An initial *RCOA* Commercial Operation using an interim IT system was set to start on June 26, 2013.

On December 17, 2012, the *ERC* issued Resolution No. 16 series of 2012 adopting the Transitory Rules for the implementation of *RCOA*. The resolution provides the detailed responsibilities of industry participants during the *RCOA* transition period.

On January 9, 2013, the *DOE* issued Department Circular, "Promulgating the Retail Rules for the Integration of Retail Competition and Open Access in the Wholesale Electricity Spot Market", to provide rules for the integration of retail competition in the operations and governance processes of the WESM, the management of the transactions of Suppliers and Contestable Customers, and the operations of the Central Registration Body.

On March 26, 2013, *PEMC* began the *RCOA* Trial Operations Program, a nine-week test period participated in by the various entities and service providers of *RCOA*.

On May 6, 2013, the *DOE* issued Department Circular, "Enjoining all Generation Companies, Distribution Utilities, Suppliers and Local Suppliers to Ensure an Effective and Successful Transition towards the Implementation of Retail Competition and Open Access", which required generation companies, suppliers and *DUs* to disclose their supply portfolio and capacity allocation to determine the available energy supply for Contestable Customer in the market. *MERALCO* submitted its first compliance to said Circular last June 7, 2013.

On June 19, 2013, the *ERC* issued a resolution adopting the Supplemental Rules to the Transitory Rules for the implementation of *RCOA*. The resolution seeks to prevent contestable customers who have yet to execute a Retail Supply Contract or *RSC*, with a *RES* from being disconnected or transferred to *SOLR* service upon the commencement of initial commercial operations of *RCOA*. Qualified contestable customers who fail to enter into a *RSC* with a *RES* shall be deemed to stay with their current *DU* until December 26, 2013 or until such time that it is able to find a *RES* provided that they inform the *DU*.

In accordance with the *ERC*'s "Transitory Rules for the Initial Implementation of Open Access and Retail Competition", commercial operations of *RCOA* began on June 26, 2013.

Nineteen *RESs* were licensed by the *ERC* to provide competitive retail supply service to eligible contestable customers. As at December 31, 2013, 287 customers have opted for contestability and are now being supplied by competitive retail electricity suppliers.

On September 4, 2013, the *ERC* conducted a public consultation on its proposed amendments to the *RES Licensing Rules*, for which *MERALCO* submitted comments and participated in the public consultation.



As at December 31, 2013, there are about 782 contestable customers in *MERALCO*'s franchise area and 287 have already switched to their respective *RESs*.

Philippine Export Zone Authority or PEZA – ERC Jurisdiction

On September 13, 2007, *PEZA* issued “Guidelines in the Registration of Electric Power Generation Facilities/Utilities/Entities Operating Inside the Ecozones” and “Guidelines for the Supply of Electric Power in Ecozones.” Under these Guidelines, *PEZA* effectively bestowed upon itself franchising and regulatory powers in Ecozones operating within the legislative franchise areas of *DUs* which are under the legislatively-authorized regulatory jurisdiction of the *ERC*. The Guidelines are the subject of an injunction case filed by the *DUs* at the *RTC-Pasig*.

In support of the government’s objective of providing lower cost to Ecozone locators, *MERALCO* entered into a *MOA* with *NPC* on September 17, 2007 for the provision of special Ecozone rates to high load factor *PEZA*-accredited industries. The *ERC* authorized the immediate implementation of the Ecozone Rate Program or *ERP*. The program expired in December 2012.

The *ERP* was initially scheduled to expire by December 25, 2011 but was extended twice and was terminated on December 25, 2012.

In January 2013, *MERALCO* entered into a tripartite agreement with *PEZA* and Trans-Asia Oil and Energy Development Corporation for the sale of power to *CEZ* and its locators beginning January 26, 2013.

As an alternative to the *ERP*, *MERALCO* filed an application for the implementation of Peak/Off-Peak (POP) Program. On December 17, 2012, the *ERC* provisionally approved the application and *MERALCO* started implementing the program on February 1, 2013.

Purchase of Subtransmission Assets or STAs

On November 25, 2009, *MERALCO* signed a Contract to Sell with *TransCo* for the sale and purchase of certain subtransmission assets for ₱86 million. On February 25, 2010, the *ERC* approved this Contract to Sell. On June 1, 2012, the *ERC* rendered a decision dated March 6, 2012, approving the sale of the said *STAs* in favor of *MERALCO* for ₱85 million.

On April 17, 2012, *MERALCO* and *TransCo* filed a joint application for the approval of the Batch 4 contract to sell with the *ERC*. On April 22, 2013, the *ERC* issued a Decision on *MERALCO*'s joint application for the acquisition of the Batch 4 contract to sell. On June 21, 2013, *MERALCO* filed a motion for partial reconsideration regarding the exclusion of certain facilities for acquisition, which has yet to be resolved by the *ERC*.

On December 12, 2011, *MERALCO* signed various agreements for the acquisition of certain sub-transmission assets of *TransCo* within the *MERALCO* franchise area for its sole account, as well as with a consortium with Batangas II Electric Cooperative, Inc., or *BATELEC II* and First Bay Power Corporation. On September 18, 2012, an amended consortium agreement was executed between *MERALCO* and *FBPC*. On October 17, 2012, *MERALCO* signed two separate amended consortium agreements with *BATELEC II*, and with *FBPC* and *BATELEC II*. These amended consortium agreements superseded the ones signed on December 12, 2011. On December 27 and 28, 2012, the Contract to Sell and Consortium Agreements, respectively, covering these sub-transmission assets were filed with the *ERC* for approval.



MERALCO's POP Program

On November 15, 2012, *MERALCO* filed an application with the *ERC* for the approval of its revised Time of Use or *TOU* rates program, also known as the *POP* Program. The *POP* is a rate program being offered by *MERALCO* to customers whose load characteristics can benefit from *TOU* rates as well as to those that can shift their loads from peak to off-peak hours. The proposed revised *POP* Rate aims to provide better savings to avalees by providing them with a *TOU* program that has a wider pricing difference between peak and off-peak rates.

In an Order dated December 17, 2012, the *ERC* provisionally approved the *POP* Program.

Feed-in-Tariff (FIT)

Pursuant to Republic Act No. 9513, or the Renewable Energy Act of 2008 or *RE* Act, the *ERC* issued Resolution No. 16, Series of 2010, Adopting the Feed-in-Tariff or *FIT* Rules, on July 23, 2010. As defined under the *FIT* Rules, the *FIT* system is as a renewable energy policy that offers a guaranteed payment on a fixed rate per kilowatt-hour for electricity from wind, solar, ocean, hydropower and biomass energy sources.

On May 16, 2011, the National Renewable Energy Board or *NREB* filed its Petition to Initiate Rule Making for the Adoption of *FIT*. The Petition proposed a specific *FIT* Rate for each emerging renewable resource. On July 27, 2012, after undergoing several public consultations and public hearings, the *ERC* approved *FIT* Rates that are significantly lower than the rates applied by the *NREB*.

To fund the *FIT* payments to eligible *RE* developers, a *FIT*-Allowance charge will be imposed on all end-users. The *FIT*-Allowance will be established by the *ERC* upon petition by the *TransCo*, which had been designated as the *FIT* Fund Administrator. The *FIT*-Allowance Petition will go through the process of public hearings and consultations.

To supplement the *FIT* Rules, the *ERC* is currently drafting *FIT*-Allowance Payment and Collection Guidelines. This set of guidelines will govern how the *FIT*-Allowance will be calculated using the formulae provided. It will also outline the process of billing and collecting the *FIT*-Allowance from the electricity consumers, the remittance to a specified fund, the disbursement from the *FIT*-Allowance fund and the payment to eligible *RE* developers. The draft is currently undergoing public consultations.

Net Metering Program

The *RE* Act mandates the *DUs* to provide the mechanism for the “physical connection and commercial arrangements necessary to ensure the success of the *RE* programs”, specifically the Net Metering Program. The *RE* Act defines Net Metering as “a system, appropriate for distributed generation, in which a distribution grid user has a two-way connection to the grid and is only charged for his net electricity consumption and is credited for any overall contribution to the electricity grid”. By their nature, net metering installations will be small (less than 100 *kW*) and will likely be adopted by the households and small business end-users of *DUs*.



On September 4, 2012, the *ERC* released the first draft of the Proposed Net Metering Rules. The proposed rules will govern the implementation of the Net Metering program for *RE* sources. It also seeks to establish the standards for interconnecting these *RE* sources to the *DUs*' systems. The pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. Meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. On September 21, 2012, the *ERC* conducted the first public consultation on the proposed rules.

After consultations with stakeholders, the *ERC* issued on July 3, 2013 its Resolution No. 09, Series of 2013, entitled, "A Resolution Adopting the Rules enabling the Net Metering Program for Renewable Energy". The rules will govern the *DUs*' implementation of the Net Metering program. Included in Rules are the Interconnection Standards that shall provide technical guidance to address engineering, electric system reliability, and safety concerns for net metering interconnections. The final pricing methodology, however, will be addressed in another set of rules and will be endorsed to the *ERC* in due course. In the meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. The rules took effect on July 24, 2013. *MERALCO* started accepting net metering applications on the same day. As at March 17, 2014, *MERALCO* has already energized five Net Metering customers, the country's first participants to the net metering program.

34. Subsequent Event

On March 17, 2014, the *BOD* declared a final cash dividend of ₱6.45 per share to all shareholders of record as at April 15, 2014, payable on May 8, 2014.

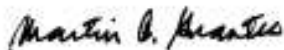


INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTARY SCHEDULES

The Stockholders and the Board of Directors
Manila Electric Company
Lopez Building
Ortigas Avenue, Pasig City

We have audited in accordance with Philippine Standards on Auditing, the consolidated financial statements of Manila Electric Company and Subsidiaries as at December 31, 2013 and 2012 and for each of the three years in the period ended December 31, 2013, included in this Form 17-A, and have issued our report thereon dated March 17, 2014. Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedules listed in the Index to the Consolidated Financial Statements and Supplementary Schedules are the responsibility of the Company's management. These schedules are presented for purposes of complying with Securities Regulation Code Rule 68, As Amended (2011) and are not part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly state in all material respects, the information required to be set forth therein in relation to the basic financial statements taken as a whole.

SYCIP GORRES VELAYO & CO.



Martin C. Guantes
Partner
CPA Certificate No. 88494
SEC Accreditation No. 0325-AR-2 (Group A),
March 15, 2012, valid until March 14, 2015
Tax Identification No. 152-884-272
BIR Accreditation No. 08-001998-52-2012,
April 11, 2012, valid until April 10, 2015
PTR No. 4225178, January 2, 2014, Makati City

March 17, 2014



MANILA ELECTRIC COMPANY
Schedule C: Accounts Receivable from Related Parties which are Eliminated during the Consolidation of Financial Statements
As at December 31, 2013
(Amounts in Millions Pesos)

Name of Related Party	January 1, 2013	Additions	Collections	Amount written off	Current	Noncurrent	December 31, 2013
Meralco Financial Services Corporation	31	-	(1)	-	30	-	30
Miescor Builders, Inc.	-	61	(38)	-	23	-	23
Miescorrail, Inc.	-	7	-	-	7	-	7
Meralco Energy Inc.	45	6	(46)	-	5	-	5
Miescor Logistics, Inc.	-	21	(18)	-	3	-	3
Corporate Information Solutions, Inc.	5	12	(15)	-	2	-	2
CIS Bayad Center, Inc.	103	-	(103)	-	-	-	-
eMERALCO Ventures, Inc.	4	3	(7)	-	-	-	-
Meralco Industrial Engineering Services Corporation	1	-	(1)	-	-	-	-
	189	110	(229)	-	70	-	70

MANILA ELECTRIC COMPANY

Schedule D: The Movement of Intangible Assets (Included under Other Noncurrent Assets)

As at December 31, 2013

(Amounts In Millions Pesos)

Description	January 1, 2013	Additions at cost	Charged to cost and expenses	Charged to other accounts	Other changes additions (deductions)	December 31, 2013
Software	972	876	(169)	-	-	1,679
Franchise	49	-	-	-	-	49
TOTALS	1,021	876	(169)	-	-	1,728

MANILA ELECTRIC COMPANY AND SUBSIDIARIES
Schedule E: Interest Bearing Long-term Financial Liabilities
As at December 31, 2013
(Amounts In Millions)

Title of issue and type of obligation	Amount authorized by indenture	Amount shown under caption "Current Portion of Interest Bearing Long-term Financial Liabilities" in the Consolidated Statement of Financial Position	Amount shown under caption "Interest Bearing Long-term Financial Liabilities" in the Consolidated Statement of Financial Position
BONDS:			
7-YEAR, P11,500 MILLION	11,500	-	11,500
12-YEAR, P7,000 MILLION	7,000	-	7,000
FIXED RATE LOANS:			
P3.0 BILLION NOTE FACILITY	3,000		
7-YEAR FIXED RATE, P1,000 MILLION		277	-
10-YEAR FIXED RATE , P2,000 MILLION		253	-
P5.0 BILLION NOTE FACILITY	5,000		
7-YR FIXED RATE, P500 MILLION		490	-
10-YR FIXED RATE, P4,500 MILLION		4,410	-
P4.8 BILLION NOTE FACILITY	4,800		
7-YEAR FIXED RATE, P1,997 MILLION		917	-
10-YEAR FIXED RATE, P2,803 MILLION		2,500	-
FLOATING RATE LOANS:			
P2,500 MILLION, 7-YEAR TERM LOAN FACILITY	2,500	12	2,463
P3,000 MILLION, 5-YEAR TERM LOAN FACILITY	3,000	600	-
REDEEMABLE PREFERRED STOCK:		1,562	-
TOTAL		11,021	20,963
LESS UNAMORTIZED DEBT ISSUE COST		-	207
BALANCE AT END OF THE YEAR		11,021	20,756

Manila Electric Company
Schedule H. Capital Stock
As at December 31, 2013
(Amounts in millions)

Title of Issue	Number of shares authorized	Number of shares issued and outstanding as shown under related balance sheet caption	Number of shares reserved for options, warrants, conversion and other rights	Number of shares held by related parties	Directors, officers and employees	Others
Common Stock	1,250	1,127	-	913	8	206

MANILA ELECTRIC COMPANY
Schedule I. List of Effective Standards and Interpretations
As at December 31, 2013

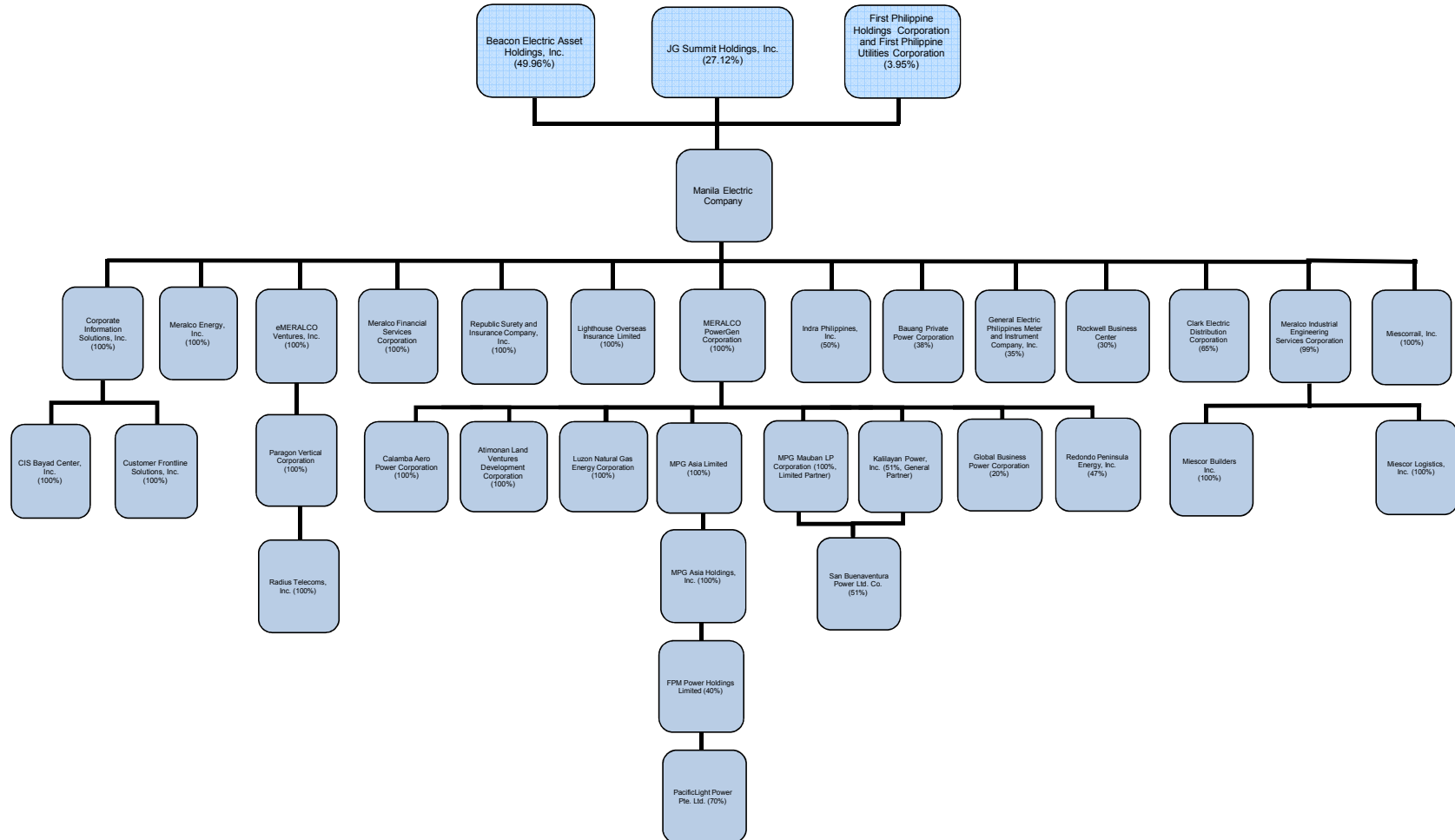
PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS (issued as of December 31, 2013)		ADOPTED	NOT ADOPTED	NOT APPLICABLE
PFRS 1	First-time Adoption of Philippine Financial Reporting Standards	X		
(Revised)	Amendments to PFRS 1 and PAS 27: Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate			X
	Amendments to PFRS 1: Additional Exemptions for First-time Adopters			X
	Amendment to PFRS 1: Limited Exemption from Comparative PFRS 7 Disclosures for First-time Adopters			X
	Amendments to PFRS 1: Severe Hyperinflation and Removal of Fixed Date for First-time Adopters			X
	Amendments to PFRS 1: Government Loans		Not Early Adopted	
PFRS 2	Share-based Payment	X		
	Amendments to PFRS 2: Vesting Conditions and Cancellations	X		
	Amendments to PFRS 2: Group Cash-settled Share-based Payment Transactions			X
PFRS 3	Business Combinations			
(Revised)		X		
PFRS 4	Insurance Contracts	X		
	Amendments to PAS 39 and PFRS 4: Financial Guarantee Contracts	X		
PFRS 5	Non-current Assets Held for Sale and Discontinued Operations	X		
PFRS 6	Exploration for and Evaluation of Mineral Resources			X
PFRS 7	Financial Instruments: Disclosures	X		
	Amendments to PFRS 7: Transition	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets - Effective Date and Transition			
		X		
	Amendments to PFRS 7: Improving Disclosures about Financial Instruments	X		
	Amendments to PFRS 7: Disclosures - Transfers of Financial Assets	X		
	Amendments to PFRS 7: Disclosures - Offsetting Financial Assets and Financial Liabilities	X		
	Amendments to PFRS 7: Mandatory Effective Date of PFRS 9 and Transition Disclosures		Not Early Adopted	
PFRS 8	Operating Segments	X		
PFRS 9	Financial Instruments		Not Early Adopted	
	Amendments to PFRS 9: Mandatory Effective Date of PFRS 9 and Transition Disclosures		Not Early Adopted	
PFRS 10	Consolidated Financial Statements	X		
PFRS 11	Joint Arrangements	X		
PFRS 12	Disclosure of Interests in Other Entities	X		
PFRS 13	Fair Value Measurement	X		
Philippine Accounting Standards				
PAS 1	Presentation of Financial Statements	X		
(Revised)	Amendment to PAS 1: Capital Disclosures	X		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			X
	Amendments to PAS 1: Presentation of Items of Other Comprehensive Income	X		
PAS 2	Inventories	X		
PAS 7	Statement of Cash Flows	X		
PAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	X		
PAS 10	Events after the Balance Sheet Date	X		
PAS 11	Construction Contracts	X		
PAS 12	Income Taxes	X		
	Amendment to PAS 12 - Deferred Tax: Recovery of Underlying Assets	X		
PAS 16	Property, Plant and Equipment	X		
PAS 17	Leases	X		
PAS 18	Revenue	X		
PAS 19	Employee Benefits	X		
	Amendments to PAS 19: Actuarial Gains and Losses, Group Plans and Disclosures	X		
PAS 19	Employee Benefits			
(Amended)		X		
	Amendments to PAS 19: Defined Benefit Plans : Employee Contributions		Not Early Adopted	
PAS 20	Accounting for Government Grants and Disclosure of Government Assistance			X
PAS 21	The Effects of Changes in Foreign Exchange Rates	X		
	Amendment: Net Investment in a Foreign Operation	X		
PAS 23	Borrowing Costs			
(Revised)		X		
PAS 24	Related Party Disclosures			
(Revised)		X		
PAS 26	Accounting and Reporting by Retirement Benefit Plans			X
PAS 27	Consolidated and Separate Financial Statements	X		
PAS 28	Investments in Associates	X		
PAS 27	Separate Financial Statements			
(Amended)		X		
PAS 28	Investments in Associates and Joint Ventures			
(Amended)		X		
PAS 29	Financial Reporting in Hyperinflationary Economies			X
PAS 31	Interests in Joint Ventures	X		
PAS 32	Financial Instruments: Disclosure and Presentation	X		
	Amendments to PAS 32 and PAS 1: Puttable Financial Instruments and Obligations Arising on Liquidation			X
	Amendment to PAS 32: Classification of Rights Issues			X

PHILIPPINE FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS (issued as of December 31, 2013)		ADOPTED	NOT ADOPTED	NOT APPLICABLE
	Amendments to PAS 32: Offsetting Financial Assets and Financial Liabilities		Not Early Adopted	
PAS 33	Earnings per Share	X		
PAS 34	Interim Financial Reporting	X		
PAS 36	Impairment of Assets	X		
	Amendments to PAS 36: Recoverable Amount Disclosures for Non-Financial Assets		Not Early Adopted	
PAS 37	Provisions, Contingent Liabilities and Contingent Assets	X		
PAS 38	Intangible Assets	X		
PAS 39	Financial Instruments: Recognition and Measurement	X		
	Amendments to PAS 39: Transition and Initial Recognition of Financial Assets and Financial Liabilities	X		
	Amendments to PAS 39: Cash Flow Hedge Accounting of Forecast Intragroup Transactions			X
	Amendments to PAS 39: The Fair Value Option	X		
	Amendments to PAS 39 and PFRS 4: Financial Guarantee Contracts	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets	X		
	Amendments to PAS 39 and PFRS 7: Reclassification of Financial Assets – Effective Date and Transition	X		
	Amendments to Philippine Interpretation IFRIC–9 and PAS 39: Embedded Derivatives	X		
	Amendment to PAS 39: Eligible Hedged Items			X
	Amendment to PAS 39: Recognition and Measurements - Novation of Derivatives and Continuation of Hedge Accounting		Not Early Adopted	
PAS 40	Investment Property	X		
PAS 41	Agriculture			X
Philippine Interpretations				
IFRIC 1	Changes in Existing Decommissioning, Restoration and Similar Liabilities	X		
IFRIC 2	Members' Share in Co-operative Entities and Similar Instruments			X
IFRIC 4	Determining Whether an Arrangement Contains a Lease	X		
IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds			X
IFRIC 6	Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment			X
IFRIC 7	Applying the Restatement Approach under PAS 29 Financial Reporting in Hyperinflationary Economies			X
IFRIC 8	Scope of PFRS 2	X		
IFRIC 9	Reassessment of Embedded Derivatives	X		
	Amendments to Philippine Interpretation IFRIC–9 and PAS 39: Embedded Derivatives	X		
IFRIC 10	Interim Financial Reporting and Impairment	X		
IFRIC 11	PFRS 2- Group and Treasury Share Transactions			X
IFRIC 12	Service Concession Arrangements			X
IFRIC 13	Customer Loyalty Programmes			X
IFRIC 14	The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	X		
	Amendments to Philippine Interpretations IFRIC- 14, Prepayments of a Minimum Funding Requirement	X		
IFRIC 15	Agreements for the Construction of Real Estate		Not Early Adopted	
IFRIC 16	Hedges of a Net Investment in a Foreign Operation			X
IFRIC 17	Distributions of Non-cash Assets to Owners	X		
IFRIC 18	Transfers of Assets from Customers			X
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments			X
IFRIC 20	Stripping Costs in the Production Phase of a Surface Mine			X
IFRIC 21	Levies		Not Early Adopted	
SIC-7	Introduction of the Euro			X
SIC-10	Government Assistance - No Specific Relation to Operating Activities			X
SIC-12	Consolidation - Special Purpose Entities			X
	Amendment to SIC - 12: Scope of SIC 12			X
SIC-13	Jointly Controlled Entities - Non-Monetary Contributions by Venturers			X
SIC-15	Operating Leases - Incentives	X		
SIC-21	Income Taxes - Recovery of Revalued Non-Depreciable Assets	X		
SIC-25	Income Taxes - Changes in the Tax Status of an Entity or its Shareholders			X
SIC-27	Evaluating the Substance of Transactions Involving the Legal Form of a Lease	X		
SIC-29	Service Concession Arrangements: Disclosures			X
SIC-31	Revenue - Barter Transactions Involving Advertising Services			X
SIC-32	Intangible Assets - Web Site Costs			X

MANILA ELECTRIC COMPANY
Schedule J: Reconciliation of Retained Earnings Available for Dividend Declaration
As at December 31, 2013
(Amounts in millions)

Unappropriated retained earnings as at December 31, 2012, as restated	P 43,873
Adjustments in previous years' reconciliation:	
Deferred tax assets, as restated	(13,430)
Revaluation increment on utility plant and others	(17,839)
Derivative assets	(17)
Retained earnings available for dividends declaration as at December 31, 2012, as restated	<u>12,587</u>
Net income based on the face of annual parent company financial statements	17,487
Reconciling items:	
Dividends declared during the year	(11,621)
Appropriation during the year	(5,000)
Movement of deferred tax assets	(2,554)
Depreciation of revaluation increment on utility plant and others - net of tax	597
Movement of derivative assets - net of tax	17
	<u>(1,074)</u>
Retained earnings available for dividend declaration as at December 31, 2013	<u>P 11,513</u>

MANILA ELECTRIC COMPANY
Schedule K: Map Showing the Relationships among the Companies within the Group
As at December 31, 2013



MANILA ELECTRIC COMPANY AND SUBSIDIARIES

Financial Soundness Indicators
December 31, 2013 and 2012

	2013	2012
Current Ratio ⁽¹⁾	1.14 : 1.00	1.55 : 1.00
Debt to Equity Ratio ⁽²⁾	0.45 : 1.00	0.36 : 1.00
Asset to Equity Ratio ⁽³⁾	3.51x	3.19x
Interest Coverage Ratio ⁽⁴⁾	16.66x	13.73x
Profit margin Ratio ⁽⁵⁾	0.06x	0.06x
Return on Assets ⁽⁶⁾	.07x	.08x
EBITDA Margin ⁽⁷⁾	10.27%	9.71%

⁽¹⁾ Current ratio is measured as current assets divided by current liabilities.

⁽²⁾ Debt to equity ratio is measured as total debts divided to total equity attributable to equity holders of the parent.

⁽³⁾ Asset to equity ratio is measured as total assets divided by total equity attributable to equity holders of the parent.

⁽⁴⁾ Interest coverage ratio is measured as earnings before interest and taxes, divided by total interest and other financial charges.

⁽⁵⁾ Profit margin ratio is computed by dividing net income attributable to parent with total revenues.

⁽⁶⁾ Return on assets is measured as net income attributable to parent with total assets.

⁽⁷⁾ EBITDA margin is measured as EBITDA divided by total revenues.

EBITDA is measured as net income excluding depreciation and amortization, impairment of noncurrent assets, interest and other financial charges, interest and other financial income, equity share in net earnings of associates and a joint venture, foreign exchange gains or losses, mark-to-market gain or loss, provision for income tax and other non-recurring gain or loss, if any.

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Manila Electric Company
Lopez Building
Ortigas Avenue, Pasig City

Report on the Parent Company Financial Statements

We have audited the accompanying parent company financial statements of Manila Electric Company, which comprise the parent company statements of financial position as at December 31, 2013 and 2012, and the parent company statements of income, statements of comprehensive income, statements of changes in equity and statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Parent Company Financial Statements

Management is responsible for the preparation and fair presentation of these parent company financial statements in accordance with Philippine Financial Reporting Standards, and for such internal control as management determines necessary to enable the preparation of parent company financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the parent company financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the parent company financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the parent company financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the parent company financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



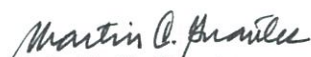
Opinion

In our opinion, the parent company financial statements present fairly, in all material respects, the financial position of Manila Electric Company as at December 31, 2013 and 2012, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards.

Report on the Supplementary Information Required Under Revenue Regulations Nos. 15-2010 and 19-2011

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information required under Revenue Regulations Nos. 15-2010 and 19-2011 in Notes 32 and 33 to the parent company financial statements, respectively, is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such information is the responsibility of the management of Manila Electric Company. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

SYCIP GORRES VELAYO & CO.


Martin C. Guantes

Partner

CPA Certificate No. 88494

SEC Accreditation No. 0325-AR-2 (Group A),
March 15, 2012, valid until March 14, 2015

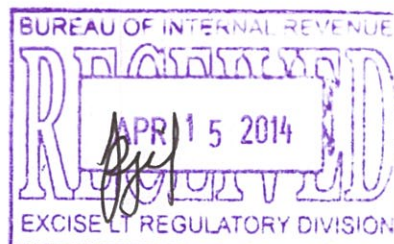
Tax Identification No. 152-884-272

BIR Accreditation No. 08-001998-52-2012,

April 11, 2012, valid until April 10, 2015

PTR No. 4225178, January 2, 2014, Makati City

March 17, 2014



MANILA ELECTRIC COMPANY
PARENT COMPANY STATEMENTS OF FINANCIAL POSITION

		December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
	Note			
(Amounts in millions)				
ASSETS				
Noncurrent Assets				
Utility plant and others	6, 9 and 14	₱111,012	₱107,880	₱104,295
Investments in subsidiaries and associates and interests in joint ventures	7	20,514	3,514	3,071
Investment properties	8 and 14	1,503	1,608	1,612
Deferred tax assets - net	27	5,353	3,019	108
Other noncurrent assets	9, 11 and 26	22,937	8,326	6,136
Total Noncurrent Assets		161,319	124,347	115,222
Current Assets				
Cash and cash equivalents	10 and 26	57,607	58,592	42,223
Trade and other receivables	2, 9, 11, 17, 22 and 26	29,547	26,046	27,026
Inventories	12	2,651	1,280	1,635
Other current assets	13 and 26	7,067	2,013	2,219
		96,872	87,931	73,103
Asset held for distribution to owners		—	—	525
Total Current Assets		96,872	87,931	73,628
		₱258,191	₱212,278	₱188,850
EQUITY AND LIABILITIES				
Equity				
Common stock	14	₱11,273	₱11,273	₱11,273
Subscriptions receivable		(69)	(211)	(521)
Additional paid-in capital		4,111	4,111	4,111
Employee stock purchase plan	15	1,049	1,049	915
Unrealized fair value gains on available-for-sale investments	9	88	107	74
Cumulative actuarial gains (losses)		1,446	286	(1,662)
Cost of treasury shares held	14	(11)	(11)	(9)
Retained earnings	14			
Appropriated		11,000	6,000	6,000
Unappropriated		44,739	43,873	37,460
Total Equity		73,626	66,477	57,641
Noncurrent Liabilities				
Interest-bearing long-term financial liabilities - net of current portion	16, 24 and 26	20,756	20,466	19,816
Customers' deposits - net of current portion	17, 21, 24 and 26	21,330	23,144	23,921
Refundable service extension costs - net of current portion	21 and 26	5,782	4,357	3,794
Long-term employee benefits	25	4,110	8,788	10,516
Provisions	18	24,729	19,411	16,919
Other noncurrent liabilities	23 and 26	16,426	12,183	5,659
Total Noncurrent Liabilities		93,133	88,349	80,625
Current Liabilities				
Notes payable	20 and 26	1,700	1,700	—
Trade payables and other current liabilities	14, 15, 17, 21, 22 and 26	71,071	45,638	38,055
Customers' refund	2, 19 and 26	6,013	6,127	6,250
Income tax payable		1,627	1,627	1,719
Current portion of interest-bearing long-term financial liabilities	16, 24 and 26	11,021	2,360	4,560
Total Current Liabilities		91,432	57,452	50,584
Total Liabilities		184,565	145,801	131,209
		₱258,191	₱212,278	₱188,850

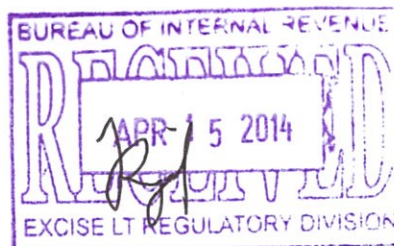
See accompanying Notes to Parent Company Financial Statements.



MANILA ELECTRIC COMPANY
PARENT COMPANY STATEMENTS OF INCOME

Years Ended December 31			
			2012
	Note	2013	(As restated - see Note 4)
(Amounts in millions, except per share data)			
REVENUES			
Sale of electricity	22, 23 and 29	₱292,251	₱280,977
Lease income	22	548	530
		292,799	281,507
COSTS AND EXPENSES			
Purchased power	22, 23 and 29	235,920	230,322
Salaries, wages and employee benefits	15, 24 and 25	9,249	10,215
Provisions for probable charges and expenses from claims	18	10,749	9,225
Depreciation and amortization	6, 8 and 9	5,858	5,349
Contracted services		3,966	3,543
Provision for doubtful accounts - net		481	819
Taxes, fees and permits		386	364
Other expenses	24	2,294	2,906
		268,903	262,743
OTHER EXPENSES (INCOME)			
Interest and other financial income	2 and 24	(1,573)	(2,547)
	16, 17,		
Interest and other financial charges	20 and 24	1,474	1,518
Derivative mark-to-market loss (gain)	26	24	(40)
Foreign exchange loss - net		37	2
Others	2	(415)	(5,961)
		(453)	(7,028)
INCOME BEFORE INCOME TAX		24,349	25,792
PROVISION FOR (BENEFIT FROM) INCOME TAX	27		
Current		9,690	9,346
Deferred		(2,828)	(3,747)
		6,862	5,599
NET INCOME		₱17,487	₱20,193
Earnings Per Share - Basic and Diluted	30	₱15.52	₱17.92

See accompanying Notes to Parent Company Financial Statements.



MANILA ELECTRIC COMPANY
PARENT COMPANY STATEMENTS OF COMPREHENSIVE INCOME

		Years Ended December 31	
		2013	2012
		(As restated – see Note 4)	
	Note	(Amounts in millions)	
NET INCOME FOR THE YEAR		₱17,487	₱20,193
OTHER COMPREHENSIVE INCOME			
Items that will be reclassified to profit or loss in subsequent years:			
Unrealized fair value gain (loss) on available-for-sale financial assets	9	(21)	47
Income tax effect		2	(14)
		(19)	33
Items that will not be reclassified to profit or loss in subsequent years:			
Actuarial gain		1,657	2,783
Income tax effect		(497)	(835)
		1,160	1,948
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX		1,141	1,981
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX		₱18,628	₱22,174

See accompanying Notes to Parent Company Financial Statements.



MANILA ELECTRIC COMPANY

PARENT COMPANY STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 2013 AND 2012

	Common Stock (Note 14)	Subscriptions Receivable	Additional Paid-in Capital	Employee Stock Purchase Plan (Note 15)	Unrealized Fair Value Gains on Available-for- sale Investments (Note 9)	Cumulative Actuarial Gains (Losses)	Cost of Treasury Shares Held (Note 14)	Appropriated Retained Earnings (Note 14)	Unappropriated Retained Earnings (Note 14)	Total Equity
						(Amounts in millions)				
At January 1, 2013, as previously presented	₱11,273	(₱211)	₱4,111	₱1,049	₱107	₱ -	(₱11)	₱6,000	₱43,739	₱66,057
Effect of adoption of PAS 19R	-	-	-	-	-	286	-	-	134	420
At January 1, 2013, as restated	11,273	(211)	4,111	1,049	107	286	(11)	6,000	43,873	66,477
Net income	-	-	-	-	-	-	-	-	17,487	17,487
Other comprehensive income (loss)	-	-	-	-	(19)	1,160	-	-	-	1,141
Total comprehensive income (loss)	-	-	-	-	(19)	1,160	-	-	17,487	18,628
Collection of subscriptions receivable	-	142	-	-	-	-	-	5,000	(5,000)	-
Appropriation	-	-	-	-	-	-	-	-	(11,621)	(11,621)
Dividends	-	142	-	-	-	-	-	5,000	(16,621)	(11,479)
At December 31, 2013	₱11,273	(₱69)	₱4,111	₱1,049	₱88	₱1,446	(₱11)	₱11,000	₱44,739	₱73,626
At January 1, 2012, as previously presented	₱11,273	(₱521)	₱4,111	₱915	₱74	₱ -	(₱9)	₱6,000	₱37,431	₱59,274
Effect of adoption of PAS 19R	-	-	-	-	-	(1,662)	-	-	29	(1,633)
At January 1, 2012, as restated	11,273	(521)	4,111	915	74	(1,662)	(9)	6,000	37,460	57,641
Net income	-	-	-	-	33	1,948	-	-	20,193	20,193
Other comprehensive income	-	-	-	-	33	1,948	-	-	-	1,981
Total comprehensive income	-	-	-	-	33	1,948	-	-	20,193	22,174
Share-based payments	-	-	-	134	-	-	-	-	-	134
Collection of subscriptions receivable	-	310	-	-	-	-	-	-	-	310
Treasury shares	-	-	-	-	-	-	(2)	-	-	(2)
Dividends	-	-	-	-	-	-	-	-	(13,780)	(13,780)
At December 31, 2012	₱11,273	(₱211)	₱4,111	₱1,049	₱107	₱286	(₱11)	₱6,000	₱43,873	₱66,477

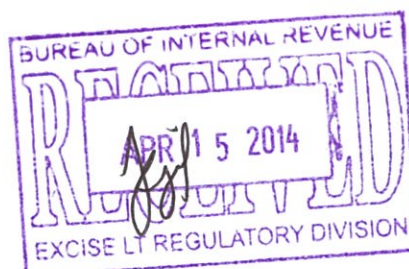
See accompanying Notes to Parent Company Financial Statements.



MANILA ELECTRIC COMPANY
PARENT COMPANY STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

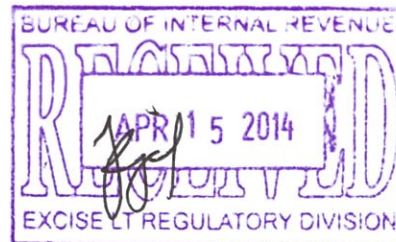
	Note	2013	2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
CASH FLOWS FROM OPERATING ACTIVITIES			
Income before income tax		₱24,349	₱25,792
Adjustments for:			
Provisions for probable charges and expenses from claims, net of settlement		10,736	8,948
Depreciation and amortization	6, 8 and 9	5,858	5,349
Interest and other financial charges	24	1,474	1,518
Interest and other financial income	24	(1,423)	(2,547)
Provision for doubtful accounts - net	11	481	819
Dividend income		(491)	(58)
Gain on the distribution of investment in Rockwell Land		—	(4,117)
Others		(48)	206
Operating income before working capital changes		40,936	35,910
Decrease (increase) in:			
Trade and other receivables		(19,166)	(1,061)
Inventories		(1,371)	408
Other current assets		(214)	201
Increase (decrease) in:			
Trade payables and other current liabilities		24,403	4,854
Customers' deposits		1,632	2,472
Long-term employee benefits		(3,024)	1,056
Customers' refund		(114)	(123)
Cash generated from operations		43,082	43,717
Income tax paid		(7,102)	(7,125)
Net cash from operating activities		35,980	36,592
CASH FLOWS FROM INVESTING ACTIVITIES			
Additions to:			
Investments in a subsidiary and associates	7	(17,000)	(473)
Utility plant and others	6	(8,886)	(9,090)
Intangible assets	9	(875)	(307)
Short-term investments		(4,841)	—
Proceeds from:			
Disposal of utility plant and others		127	155
Return of investment	7	—	30
Disposal of investment properties		91	—
Interest, other financial income and dividends received		1,069	1,741
Increase in other noncurrent assets		(484)	(2,031)
Net cash used in investing activities		(30,799)	(9,975)

(Forward)



	Note	2013	2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
CASH FLOWS FROM FINANCING ACTIVITIES			
Payments of:			
Dividends		(12,567)	(8,767)
Interest-bearing long-term financial liabilities		(9,424)	(4,565)
Notes payable		(4,685)	—
Interest and other financial charges		(1,727)	(2,883)
Proceeds from:			
Issuances of bonds, net of issue costs		18,314	—
Availment of notes payable		4,685	1,700
Collection of subscriptions receivable		142	310
Availment of interest-bearing long-term financial liabilities, net of issue costs		—	3,000
Acquisition of treasury shares		—	(2)
Increase (decrease) in other noncurrent liabilities		(904)	959
Net cash used in financing activities		(6,166)	(10,248)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(985)	16,369
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		58,592	42,223
CASH AND CASH EQUIVALENTS AT END OF YEAR	10	₱57,607	₱58,592

See accompanying Notes to Parent Company Financial Statements.



MANILA ELECTRIC COMPANY

NOTES TO PARENT COMPANY FINANCIAL STATEMENTS

1. Corporate Information

Manila Electric Company or *MERALCO*, holds a congressional franchise under Republic Act or *RA* No. 9209 effective June 28, 2003. *RA* No. 9209 grants *MERALCO* a 25-year franchise valid through June 28, 2028 to construct, operate, and maintain the electric distribution system in the cities and municipalities of Bulacan, Cavite, Metro Manila, and Rizal and certain cities, municipalities, and barangays in the provinces of Batangas, Laguna, Pampanga, and Quezon. On October 20, 2008, the Energy Regulatory Commission or *ERC*, granted *MERALCO* a consolidated Certificate of Public Convenience and Necessity for the operation of electric service within its franchise coverage, effective until the expiration of *MERALCO*'s congressional franchise. *MERALCO* has a unit for its participation in retail electricity supply or *RES*. *MERALCO*'s local *RES*, otherwise known as *MPower*, is a business unit within *MERALCO*.

Under its latest amended Articles of Incorporation, *MERALCO*'s corporate life was extended for another 50 years through 2019. *MERALCO* distributes and supplies electricity in its franchise areas and is subject to the rate-making regulations and regulatory policies of the *ERC*.

The single largest shareholder of *MERALCO* as at December 31, 2013 is Beacon Electric Asset Holdings, Inc. or *Beacon Electric*, which owns 49.96% of the common shares. *Beacon Electric* is jointly owned by Metro Pacific Investments Corporation or *Metro Pacific* and PLDT Communications and Energy Ventures, Inc., or *PCEV*, both of which are domestic corporations and are affiliates of First Pacific Company Limited or *First Pacific*, a Hong Kong-based investment and management company. In December 2013, JG Summit Holdings, Inc. or *JG Summit*, completed the purchase of the remaining 27.12% equity interest of San Miguel Corporation or *SMC*, San Miguel Pure Foods Company, Inc. and San Miguel Global Power Holdings Corp. in *MERALCO*. In July 2013, *SMC* sold its 5.71%-interest in *MERALCO* through the market. First Philippine Holdings Corporation or *First Holdings*, and First Philippine Utilities Corporation, collectively own 3.95%. The balance of *MERALCO*'s common shares is held by the public.

The common shares of *MERALCO* are listed on and traded in the Philippine Stock Exchange or *PSE*, with security symbol *MER*.

The registered office address of *MERALCO* is Lopez Building, Ortigas Avenue, Pasig City, Philippines.

The accompanying parent company financial statements as at December 31, 2013 and 2012 and January 1, 2012 and for years ended December 31, 2013 and 2012, were reviewed and recommended by the Audit and Risk Management Committee for approval to the Board of Directors or *BOD* on March 17, 2014. On the same date, these parent company financial statements were approved and authorized for issue by the *BOD*.

2. Rate Regulations

As a distribution utility or *DU*, *MERALCO* is subject to the rate-making regulations and regulatory policies of the *ERC*. Billings to customers are itemized or "unbundled" into a number of bill components that reflect the various activities and costs incurred in providing electric service. The adjustment to each bill component is governed by mechanisms promulgated and enforced by the *ERC*, mainly: [i] the "Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities," which govern the recovery of



pass-through costs, including over- or under-recoveries of the bill components, namely, (a) generation charge, (b) transmission charge, (c) system loss or *SL*, charge, (d) lifeline subsidy, (e) local franchise tax or *LFT*, and (f) business tax; and [ii] the “Rules for the Setting of Distribution Wheeling Rates” or *RDWR*, as modified by *ERC* Resolution No. 20, Series of 2008, which govern the determination of *MERALCO*’s distribution, supply, and metering charges.

Rate Application

Performance Based Regulation or PBR

MERALCO was among the Group A entrants to the *PBR*, together with two other private *DUs*.

Rate-setting under *PBR* is governed by the *RDWR*. The *PBR* scheme sets tariffs based on the regulated asset base of the *DU*, and the required operating and capital expenditures once every regulatory period or *RP*, to meet operational performance and service level requirements responsive to the needs for adequate, reliable, quality power, efficient service and growth of all customer classes in the franchise area as approved by the *ERC*. The *PBR* also employs a mechanism that penalizes or rewards a *DU* depending on its network and service performance.

Rate filings and settings are done on a *RP* basis. One (1) *RP* consists of four (4) Regulatory Years or *RYs*. An *RY* for *MERALCO* begins on July 1 and ends on June 30 of the following year. As at December 31, 2013, *MERALCO* is operating in the first half of the third *RY* of the third *RP*. The third *RP* is from July 1, 2011 to June 30, 2015.

Maximum Average Price or MAP for RY 2008 and RY 2009

On January 11 and April 1, 2008, *MERALCO* filed separate applications for the approval of its proposed translation of the *MAP* for *RY 2008* and *RY 2009*, respectively, into different rate schedules for its various customer segments. A portion of the distribution charge under-recoveries as a result of the delayed implementation of the *PBR* was incorporated in the proposed *MAP* for *RY 2009*.

In April 2009, the *ERC* approved the implementation of *MERALCO*’s average distribution rate of ₱1.2227 per kilowatt hour or *kWh* effective billing period of May 2009. This rate is inclusive of the under-recoveries for calendar year 2007 of ₱0.1285 per *kWh*.

On May 28, 2009, certain electricity consumer groups filed a Petition with the Court of Appeals, or *CA*, questioning the decision and Order of the *ERC* on *MERALCO*’s rate translation application for *RY 2008* and *RY 2009*. In a decision dated January 27, 2010, the *CA* denied the Petition. Consequently, the consumer groups brought the case to the Supreme Court of the Philippines or *SC*. Comments and responses were filed by both parties with a Manifestation filed by *MERALCO* on January 26, 2011. As at March 17, 2014, the *SC* has yet to render its decision on this case.

MAP for RY 2012

On June 21, 2011, *MERALCO* filed an application for the approval of its *MAP* for *RY 2012* and its translation into rate tariffs by customer category. On October 6, 2011, the *ERC* provisionally approved the *MAP* for *RY 2012* of ₱1.6012 per *kWh* and the rate translation per customer class was reflected commencing with the October 2011 customer bills. Hearings for the final approval of the application have been completed and all parties have submitted their respective memoranda. As at March 17, 2014, the application is pending final approval by the *ERC*.



MAP for RY 2013

On June 11, 2012, the *ERC* provisionally approved the *MAP* for *RY* 2013 of ₱1.6303 per *kWh* which was reflected starting with the July 2012 customer bills. Hearings on this case have been completed and *MERALCO* is awaiting the final decision of the *ERC*.

MAP for RY 2014

On April 1, 2013, *MERALCO* filed its application for the approval of its *MAP* for *RY* 2014 of ₱1.6510 per *kWh* and the translation thereof into rate tariffs by customer category. Hearing was completed on May 9, 2013. *MERALCO* filed its Formal Offer of Evidence or *FOE* on May 10, 2013. On June 10, 2013, the *ERC* provisionally approved the *MAP* for *RY* 2014 of ₱1.6474 per *kWh* and the rate translation per customer class. As at March 17, 2014, the application is pending final approval by the *ERC*.

SC Decision on Unbundling Rate Case

On May 30, 2003, the *ERC* issued an Order approving *MERALCO*'s unbundled tariffs that resulted in a total increase of ₱0.17 per *kWh* over the May 2003 tariff levels. However, on August 4, 2003, certain consumer and civil society groups filed a Petition for Review of the *ERC*'s ruling with the *CA*. On July 22, 2004, the *CA* set aside the *ERC*'s ruling on *MERALCO*'s rate unbundling and remanded the case to the *ERC*. Further, the *CA* opined that the *ERC* should have asked the Commission on Audit or *COA*, to audit the books of *MERALCO*. The *ERC* and *MERALCO* subsequently filed separate motions asking the *CA* to reconsider its decision. On January 24, 2005, as a result of the denial by the *CA* of the motions, the *ERC* and *MERALCO* elevated the case to the *SC*.

In an En Banc Decision promulgated on December 6, 2006, the *SC* set aside and reversed the *CA* ruling saying that a *COA* audit was not a prerequisite in the determination of a utility's rates. However, while the *SC* affirmed the *ERC*'s authority in rate-fixing, the *SC* directed *ERC* to request *COA* to undertake a complete audit of the books, records and accounts of *MERALCO*. On January 15, 2007, in compliance with the directive of the *SC*, the *ERC* requested *COA* to conduct an audit of the books, records and accounts of *MERALCO* using calendar years 2004 and 2007 as test years.

The *COA* audit, which began in September 2008, was completed in August 2009.

On February 17, 2010, the *ERC* issued its Order directing *MERALCO* and all intervenors in the case to submit within 15 days from receipt of the Order, their respective comments on the *COA*'s "Report No. 2009-01 Rate Audit Unbundled Charges."

On July 1, 2011, the *ERC* maintained and affirmed its findings and conclusions in its Order dated March 20, 2003. The *ERC* stated that the *COA* recommendation to apply disallowances under *PBR* to rate unbundling violates the principle against retroactive rate-making. An intervenor group filed a motion for reconsideration of the said Order. On September 5, 2011, *MERALCO* filed its comment to the intervenor's motion for reconsideration. On February 4, 2013, the *ERC* denied the intervenor's motion for reconsideration. The intervenor filed a petition for review before the *CA*. *MERALCO* is awaiting further action of the *CA* on this matter.



Applications for the Recovery of Generation Costs and SL Charges

MERALCO filed separate applications for the full recovery of generation costs, including value-added tax or *VAT*, incurred for the supply months of August 2006 to May 2007 or total under-recoveries of ₱12,679 million for generation charges and ₱1,295 million for *SL* charges.

The separate applications for the full recovery of generation charges have been approved by the *ERC* in its decisions released on January 18, 2008, September 3, 2008 and August 16, 2010.

As at December 31, 2013, the remaining balance of ₱137 million of such unrecovered generation costs will be billed subsequent to December 2013 at the rate of ₱0.0314 per *kWh* until fully recovered. The amount is recoverable within 12 months and included in the “Trade and other receivables” account.

With respect to the ₱1,295 million *SL* charge under-recoveries, the *ERC* ordered *MERALCO* to file a separate application for the recovery of *SL* adjustments after the *ERC* confirms the transmission rate to be used in the calculation of the *SL* rate in accordance with the *SL* rate formula of the Automatic Generation Rate Adjustments Guidelines or *AGRA*. *MERALCO* has filed the application for recovery of the ₱1,295 million *SL* charge under-recoveries with the *ERC*. This was included in the Consolidated Application of over- or under-recoveries in generation, transmission, *SL* charges and lifeline subsidies charges filed on March 31, 2011 with the *ERC*. Hearings were completed on October 25, 2011. On December 12, 2011, *MERALCO* filed for the admission of its Supplemental Application. An expository hearing was conducted on February 1, 2012. As at March 17, 2014, *MERALCO* has already filed its *FOE* and is awaiting the final resolution by the *ERC*.

Inter-Class Cross Subsidies and Lifeline Subsidies

MERALCO filed separate applications to recover inter-class cross subsidies (on November 14, 2007) and lifeline subsidies (on February 19, 2008).

In a decision dated November 16, 2009, the *ERC* authorized *MERALCO* to recover the inter-class cross subsidy under-recoveries covering the period June 2003 to October 2006 amounting to ₱1,049 million and total lifeline subsidy under-recoveries covering the period June 2003 to December 2007 amounting to ₱856 million.

In December 2009, *MERALCO* implemented the decisions of the *ERC* on the inter-class cross and lifeline subsidies. The balances of inter-class cross subsidies and lifeline subsidies were fully recovered in April 2013 and December 2013, respectively.

Consolidated Applications for the Confirmation of Over/Under-recoveries of Pass-through Charges

On August 12, 2009, the *ERC* issued Resolution No. 16, Series of 2009, adopting the “Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities.” These rules govern the recovery of pass-through costs, including over- or under-recoveries with respect to the following bill components: generation charge, transmission charge, *SL* charge, lifeline and interclass rate subsidies, *LFT* and business tax. On October 18, 2010, the *ERC* promulgated *ERC* Resolution No. 21, Series of 2010, amending certain formula contained in *ERC* Resolution No. 16, Series of 2009, and setting March 31, 2011 (covering adjustments implemented until the billing month of December 2010) and March 31, 2014 (covering adjustments from January 2011 to December 2013) as the new



deadlines for *DUs* in Luzon to file their respective applications. Subsequent filings shall be made every three years thereafter.

On March 31, 2011, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries accumulated from June 2003 to December 2010 in compliance with Resolution No. 16, Series of 2009, as subsequently amended by Resolution No. 21, Series of 2010. Hearings were completed on October 25, 2011. On December 8, 2011, *MERALCO* filed an Omnibus Motion praying for, among other things, the admission of the Supplemental Application. In an Order dated December 12, 2011, the *ERC* granted *MERALCO*'s Omnibus Motion and admitted its Supplemental Application. Accordingly, hearings for the Supplemental Application were conducted where *MERALCO* presented additional evidence. *MERALCO* filed its *FOE* on September 13, 2012. The consolidated filing includes net generation charge under-recoveries of ₱1,000 million, net transmission charge over-recoveries of ₱111 million, net lifeline subsidy under-recoveries of ₱9 million and net *SL* over-recoveries of ₱425 million, excluding any applicable carrying charges.

On July 6, 2012, *MERALCO* filed a consolidated application with the *ERC* to confirm its under- or over-recoveries for the calendar year 2011. The consolidated filing includes net generation charge under-recoveries of ₱1,826 million, transmission charge under-recoveries of ₱253 million, net lifeline subsidy under-recoveries of ₱39 million and *SL* over-recoveries of ₱445 million, excluding any applicable carrying charges. Hearings on the application have been completed and *MERALCO* has submitted its *FOE* on January 25, 2013. As at March 17, 2014, the application is pending approval by the *ERC*. As at March 17, 2014, the application is pending approval by the *ERC*.

Deferred PPA

On October 14, 2009, the *ERC* released its findings on *MERALCO*'s implementation of the collection of the approved pass-through cost under-recoveries in 2004. *ERC* directed *MERALCO* to refund ₱268 million of deferred *PPA* transmission line costs related to Quezon Power (Philippines) Limited Company or *QPPL* and deferred accounting adjustments or *DAA* incurred to customers, along with ₱184 million in carrying charges, or an equivalent of ₱0.0169 per *kWh*. *MERALCO* implemented the refund beginning November 2009 until September 2010. However, the *ERC* has yet to rule on *MERALCO*'s deferred *PPA* under-recoveries of ₱106 million, which does not represent the transmission line fee. As at March 17, 2014, *MERALCO* has filed a Motion for Reconsideration, which is pending decision by the *ERC*.

Application for Recovery of LFT

On March 25, 2011, *MERALCO* filed with the *ERC* an application for recovery of *LFT* paid but not yet billed to customers for the period beginning first quarter of 1993 up to the second quarter of 2004 for five (5) provinces, namely: Bulacan, Batangas, Cavite, Laguna and Rizal; and 14 cities, namely: San Jose Del Monte, Batangas, San Pablo, Tagaytay, Lucena, Mandaluyong, Marikina, Quezon, Caloocan, Pasay, Las Piñas, Manila, Pasig and Calamba. The *LFT* is recognized as a legitimate and reasonable *DU* expense in the *ERC*'s unbundling decision.



In a Decision dated February 27, 2012, the *ERC* released its Order approving with modifications *MERALCO*'s application. The *ERC* approved recovery of *LFT* amounting to ₱1,571 million plus carrying charges of ₱730 million. As directed by the *ERC*, the recovery was reflected as a separate item in the *MERALCO* billing statement to its customers beginning April 2012. As at December 31, 2013, a total of ₱856 million *LFT* and carrying charges have been billed to affected customers. The amount recoverable within 12 months is included in the "Trade and other receivables" account while the long-term portion is included in the "Other noncurrent assets" account.

SC Decision on the ₱0.167 per kWh Refund

Following the *SC*'s final ruling that directed *MERALCO* to refund affected customers ₱0.167 per *kWh* for billings made from February 1994 to April 2003, the *ERC* approved the release of the refund in four phases. The refund is still ongoing.

See Note 19 – Customers' Refund.

3. Basis of Preparation and Statement of Compliance

The accompanying parent company financial statements have been prepared on a historical cost basis, except for utility plant and others and investment properties acquired before January 1, 2004, which are carried at deemed cost and for derivative financial instruments and available-for-sale, or *AFS*, financial assets, which are measured at fair value. Derivative financial instruments are shown as part of "Other current assets" account in the parent company statement of financial position. *AFS* financial assets are included as part of "Other noncurrent assets" account in the parent company statement of financial position.

The accompanying parent company financial statements are presented in Philippine peso, *MERALCO*'s functional and presentation currency, and all values are rounded to the nearest million peso, except when otherwise indicated.

The parent company financial statements provide comparative information in respect of the previous year. In addition, *MERALCO* presents an additional parent company statement of financial position at the beginning of the earliest year presented when there is a retrospective application of an accounting policy, a retrospective restatement, or a reclassification of items in the parent company financial statements. An additional parent company statement of financial position as at January 1, 2012 is presented in these parent company financial statements due to retrospective application of certain accounting policies.

Statement of Compliance

The parent company financial statements have been prepared in compliance with Philippine Financial Reporting Standards, or *PFRS*.

MERALCO also prepares and issues consolidated financial statements in compliance with *PFRS*. These are available publicly and may be downloaded from www.meralco.com.ph.



4. Significant Accounting Policies, Changes and Improvements

Changes in Accounting Policies and Disclosures

The accounting policies adopted in the preparation of the parent company financial statements are consistent with those of the previous financial year except for the adoption of the following Philippine Interpretations and amendments and improvements to existing standards, which were effective beginning January 1, 2013.

PAS 1, Presentation of Financial Statements – Presentation of Items of Other Comprehensive Income or OCI

The amendments to *PAS 1* change the grouping of items presented in *OCI*. Items that can be reclassified (or “recycled”) to profit or loss at a future point in time (for example, upon derecognition or settlement) will be presented separately from items that will never be recycled. The adoption did not have significant effect on the parent company financial statements. The amendments affected the presentation in the parent company statement of comprehensive income only and had no impact on *MERALCO*’s financial position or performance.

PAS 19, Employee Benefits (Amendments)

For defined benefit plans, the revised *PAS 19* requires all actuarial gains and losses to be recognized in other comprehensive income and unvested past service costs previously recognized over the average vesting period to be recognized immediately in profit or loss when incurred.

Prior to adoption of the revised *PAS 19*, *MERALCO* recognized actuarial gains and losses as income or expense when the net cumulative unrecognized gains and losses for each individual plan at the end of the previous period exceeded 10% of the higher of the defined benefit obligation and the fair value of the plan assets and recognized unvested past service costs as an expense on a straight-line basis over the average vesting period until the benefits become vested. Upon adoption of the revised *PAS 19*, *MERALCO* changed its accounting policy to recognize all actuarial gains and losses in other comprehensive income and all past service costs in profit or loss in the period they occur.

The revised *PAS 19* replaced the interest cost and expected return on plan assets with the concept of net interest on defined benefit liability or asset which is calculated by multiplying the net balance sheet defined benefit liability or asset by the discount rate used to measure the employee benefit obligation, each as at the beginning of the annual period.

The revised *PAS 19* also amended the definition of short-term employee benefits and requires employee benefits to be classified as short-term based on expected timing of settlement rather than the employee’s entitlement to the benefits. In addition, the revised *PAS 19* modifies the timing of recognition for termination benefits. The modification requires the termination benefits to be recognized at the earlier of when the offer cannot be withdrawn or when the related restructuring costs are recognized.



MERALCO reviewed its existing employee benefits and determined that the amended standard has a significant impact on its accounting for retirement benefits. MERALCO obtained the services of an external actuary to compute the impact in the parent company financial statements upon adoption of the standard. The effects are detailed below:

	As at December 31, 2013	As at December 31, 2012	As at January 1, 2012
<i>(In millions)</i>			
<u>Parent company statements of</u>			
<u>financial position</u>			
Increase (decrease) in:			
Net defined benefit liability	(₱1,989)	(₱600)	₱2,332
Deferred tax assets	(597)	(180)	699
Other comprehensive income	1,446	286	(1,662)
Retained earnings	(54)	134	29
<hr/>			
	Years Ended December 31		
	2013	2012	2011
<hr/>			
<i>(In millions)</i>			
<u>Parent company statements of</u>			
<u>income</u>			
Increase (decrease) in:			
Net benefit cost	₱269	(₱149)	(₱42)
Provision for income tax	(81)	44	13
Profit for the year	(188)	105	29
Earnings per share	(0.17)	0.09	0.03
<hr/>			
<u>Parent company statements of</u>			
<u>comprehensive income</u>			
Increase in other comprehensive income	₱1,160	₱1,948	₱1,125

The adoption of the Revised *PAS 19* had no impact on the parent company statements of cash flows.

Philippine Interpretation IFRIC 20, Stripping Costs in the Production Phase of a Surface Mine

This interpretation applies to waste removal (stripping) costs incurred in surface mining activity, during the production phase of the mine. The interpretation addresses the accounting for the benefit from the stripping activity. This new interpretation is not relevant to MERALCO.

PFRS 7, Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities

These amendments require an entity to disclose information about rights of set-off and related arrangements (such as collateral agreements). The new disclosures are required for all recognized financial instruments that are set off in accordance with *PAS 32, Financial Instruments: Presentation*. These disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or 'similar agreement', irrespective of whether they are set-off in accordance with *PAS 32*. The amendments require entities to disclose, in a tabular



format unless another format is more appropriate, the following minimum quantitative information. These are presented separately for financial assets and financial liabilities recognized at the end of the reporting period:

- a) The gross amounts of those recognized financial assets and recognized financial liabilities;
- b) The amounts that are set off in accordance with the criteria in *PAS 32* when determining the net amounts presented in the statement of financial position;
- c) The net amounts presented in the statement of financial position;
- d) The amounts subject to an enforceable master netting arrangement or similar agreement that are not otherwise included in (b) above, including:
 - i. Amounts related to recognized financial instruments that do not meet some or all of the offsetting criteria in *PAS 32*; and
 - ii. Amounts related to financial collateral (including cash collateral); and
- e) The net amount after deducting the amounts in (d) from the amounts in (c) above.

The amendments are applicable to *MERALCO* and based on the evaluation, the amendments have no impact on its financial position or performance.

PFRS 10, Consolidated Financial Statements

PFRS 10 replaces the portion of *PAS 27, Consolidated and Separate Financial Statements*, that addresses the accounting for consolidated financial statements. It also includes the issues raised in Standing Interpretations Committee or *SIC 12, Consolidation - Special Purpose Entities*. *PFRS 10* establishes a single control model that applies to all entities including special purpose entities. The changes introduced by *PFRS 10* require management to exercise significant judgment to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in *PAS 27*. A reassessment of control was performed by *MERALCO* on all its subsidiaries and associates in accordance with the provisions of *PFRS 10*. Based on the reassessment made, *MERALCO* has not determined any change in the control or significant influence in any of its subsidiaries and associates.

PFRS 11, Joint Arrangements

PFRS 11 replaces *PAS 31, Interests in Joint Ventures*, and *SIC 13, Jointly Controlled Entities - Non-Monetary Contributions by Venturers*. *PFRS 11* removes the option to account for jointly controlled entities using proportionate consolidation. Instead, jointly controlled entities that meet the definition of a joint venture must be accounted for using the equity method. The standard is applicable to *MERALCO* and based on *MERALCO*'s evaluation, the application of this new standard will have no impact on the parent company financial statements.

PFRS 12, Disclosure of Interests in Other Entities

PFRS 12 includes all of the disclosures related to consolidated financial statements that were previously in *PAS 27*, as well as all the disclosures that were previously included in *PAS 31* and *PAS 28, Investments in Associates*. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. The standard is applicable to *MERALCO* and based on the evaluation, the standard has no impact on *MERALCO*'s financial position or performance but affects disclosures only.



PFRS 13, Fair Value Measurement

PFRS 13 establishes a single source of guidance under *PFRS* for all fair value measurements. *PFRS 13* does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under *PFRS* when fair value is required or permitted. The standard is applicable to *MERALCO* and based on *MERALCO*'s evaluation, the standard has no impact on the parent company financial statements but affects disclosures only.

PAS 27, Separate Financial Statements (as revised in 2011)

As a consequence of the issuance of the new *PFRS 10* and *PFRS 12*, what remains of *PAS 27* is limited to accounting for subsidiaries, jointly controlled entities, and associates in the separate financial statements. The standard is applicable to *MERALCO* and based on its evaluation, the application of this new standard has no impact on the parent company financial statements.

PAS 28, Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the issuance of the new *PFRS 11* and *PFRS 12*, *PAS 28* has been renamed *PAS 28, Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. The standard is applicable to *MERALCO* and based on *MERALCO*'s evaluation, the application of this new standard has no impact on the parent company financial statements.

Annual Improvements to PFRS (2009-2011 cycle)

The *Annual Improvements to PFRS (2009-2011 cycle)* contain non-urgent but necessary amendments to *PFRS*. The amendments are effective for annual periods beginning on or after January 1, 2013 and to be applied retrospectively.

PFRS 1, First-time Adoption of PFRS - Borrowing Costs

The amendment clarifies that, upon adoption of *PFRS*, an entity that capitalized borrowing costs in accordance with its previous generally accepted accounting principles, may carry forward, without any adjustment, the amount previously capitalized in its opening statement of financial position at the date of transition. Subsequent to the adoption of *PFRS*, borrowing costs are recognized in accordance with *PAS 23, Borrowing Costs*. The amendment does not apply to *MERALCO* as it is not a first-time adopter of *PFRS*.

PAS 1, Presentation of Financial Statements - Clarification of the Requirements for Comparative Information

The amendment clarifies the requirements for comparative information that are disclosed voluntarily and those that are mandatory due to retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The additional comparative period does not need to contain a complete set of financial statements. On the other hand, supporting notes for the third balance sheet (mandatory when there is a retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the financial statements) are not required. The amendments affect disclosures only and have no impact on *MERALCO*'s financial position or performance.



PAS 16, Property, Plant and Equipment - Classification of Servicing Equipment

The amendment clarifies that spare parts, stand-by equipment and servicing equipment should be recognized as property, plant and equipment when they meet the definition of property, plant and equipment and should be recognized as inventory if otherwise. The amendment has no impact on *MERALCO*'s financial position or performance.

PAS 32, Financial Instruments: Presentation - Tax Effect of Distribution to Holders of Equity Instruments

The amendment clarifies that income taxes relating to distributions to equity holders and to transaction costs of an equity transaction are accounted for in accordance with *PAS 12, Income Taxes*. The amendment has no impact on *MERALCO*'s financial position or performance.

PAS 34, Interim Financial Reporting - Interim Financial Reporting and Segment Information for Total Assets and Liabilities

The amendment clarifies that the total assets and liabilities for a particular reportable segment need to be disclosed only when the amounts are regularly provided to the chief operating decision maker and there has been a material change from the amount disclosed in the entity's previous annual financial statements for that reportable segment. The amendment has no impact on *MERALCO*'s financial position or performance.

New Accounting Standards and Interpretations to Existing Standards Effective Subsequent to December 31, 2013

MERALCO will adopt the following revised standards and interpretations enumerated below, which are relevant when these become effective. Except as otherwise indicated, *MERALCO* does not expect the adoption of these revised standards and amendments to *PFRS* to have a significant impact on the parent company financial statements.

Effective 2014

PAS 36, Impairment of Assets - Recoverable Amount Disclosures for Non-Financial Assets (Amendments)

These amendments remove the unintended consequences of *PFRS 13* on the disclosures required under *PAS 36*. In addition, these amendments require disclosure of the recoverable amounts for the assets or cash-generating units for which impairment loss has been recognized or reversed during the period. These amendments are effective retrospectively for annual periods beginning on or after January 1, 2014 with earlier application permitted, provided *PFRS 13* is also applied. The amendments affect disclosures only and have no impact on *MERALCO*'s financial position or performance.

Investment Entities (Amendments to PFRS 10, PFRS 12 and PAS 27)

These amendments provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under *PFRS 10*. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. It is not expected that this amendment would be relevant to *MERALCO* since none of the entities in *MERALCO* would qualify to be an investment entity under *PFRS 10*.



Philippine Interpretation IFRIC 21, Levies (IFRIC 21)

IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. *MERALCO* does not expect that *IFRIC 21* will have material financial impact in future financial statements.

PAS 39, Financial Instruments: Recognition and Measurement - Novation of Derivatives and Continuation of Hedge Accounting (Amendments)

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. *MERALCO* has not novated its derivatives during the current period. However, these amendments would be considered for future novations.

PAS 32, Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities

The amendments clarify the meaning of “currently has a legally enforceable right to set-off” and also clarify the application of the *PAS 32* offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments affect presentation only and have no impact on *MERALCO*’s financial position or performance. The amendments to *PAS 32* are to be applied retrospectively for annual periods beginning on or after January 1, 2014.

Effective 2015

PAS 19, Employee Benefits – Defined Benefit Plans: Employee Contributions (Amendments)

The amendments apply to contributions from employees or third parties to defined benefit plans. Contributions that are set out in the formal terms of the plan shall be accounted for as reductions to current service costs if they are linked to service or as part of the remeasurements of the net defined benefit asset or liability if they are not linked to service. Contributions that are discretionary shall be accounted for as reductions of current service cost upon payment of these contributions to the plans. The amendments to *PAS 19* are to be retrospectively applied for annual periods beginning on or after July 1, 2014.

Annual Improvements to PFRS (2010-2012 cycle)

The *Annual Improvements to PFRS (2010-2012 cycle)* contain non-urgent but necessary amendments to the following standards:

PFRS 2, Share-based Payment – Definition of Vesting Condition

The amendment revised the definitions of vesting condition and market condition and added the definitions of performance condition and service condition to clarify various issues. This amendment shall be prospectively applied to share-based payment transactions for which the grant date is on or after July 1, 2014. This amendment does not apply to *MERALCO* as it has no share-based payments.



PFRS 3, Business Combinations – Accounting for Contingent Consideration in a Business Combination

The amendment clarifies that a contingent consideration that meets the definition of a financial instrument should be classified as a financial liability or as equity in accordance with *PAS 32*. Contingent consideration that is not classified as equity is subsequently measured at fair value through profit or loss whether or not it falls within the scope of *PFRS 9* (or *PAS 39*, if *PFRS 9* is not yet adopted). The amendment shall be prospectively applied to business combinations for which the acquisition date is on or after July 1, 2014. *MERALCO* shall consider this amendment for future business combinations.

PFRS 8, Operating Segments – Aggregation of Operating Segments and Reconciliation of the Total of the Reportable Segments' Assets to the Entity's Assets

The amendments require entities to disclose the judgment made by management in aggregating two or more operating segments. This disclosure should include a brief description of the operating segments that have been aggregated in this way and the economic indicators that have been assessed in determining that the aggregated operating segments share similar economic characteristics. The amendments also clarify that an entity shall provide reconciliations of the total of the reportable segments' assets to the entity's assets if such amounts are regularly provided to the chief operating decision maker. These amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments affect disclosures only and have no impact on *MERALCO*'s financial position or performance.

PFRS 13, Fair Value Measurement – Short-term Receivables and Payables

The amendment clarifies that short-term receivables and payables with no stated interest rates can be held at invoice amounts when the effect of discounting is immaterial.

PAS 16, Property, Plant and Equipment – Revaluation Method – Proportionate Restatement of Accumulated Depreciation

The amendment clarifies that, upon revaluation of an item of property, plant and equipment, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated depreciation at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated depreciation is eliminated against the gross carrying amount of the asset.

The amendment is effective for annual periods beginning on or after July 1, 2014. The amendment shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendment has no impact on *MERALCO*'s financial position or performance.



PAS 24, Related Party Disclosures – Key Management Personnel

The amendments clarify that an entity is a related party of the reporting entity if the said entity, or any member of a group for which it is a part of, provides key management personnel services to the reporting entity or to the parent company of the reporting entity. The amendments also clarify that a reporting entity that obtains management personnel services from another entity (also referred to as management entity) is not required to disclose the compensation paid or payable by the management entity to its employees or directors. The reporting entity is required to disclose the amounts incurred for the key management personnel services provided by a separate management entity. The amendments are effective for annual periods beginning on or after July 1, 2014 and are applied retrospectively. The amendments affect disclosures only and have no impact on MERALCO's financial position or performance.

PAS 38, Intangible Assets – Revaluation Method – Proportionate Restatement of Accumulated Amortization

The amendments clarify that, upon revaluation of an intangible asset, the carrying amount of the asset shall be adjusted to the revalued amount, and the asset shall be treated in one of the following ways:

- a. The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. The accumulated amortization at the date of revaluation is adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account any accumulated impairment losses.
- b. The accumulated amortization is eliminated against the gross carrying amount of the asset.

The amendments also clarify that the amount of the adjustment of the accumulated amortization should form part of the increase or decrease in the carrying amount accounted for in accordance with the standard.

The amendments are effective for annual periods beginning on or after July 1, 2014. The amendments shall apply to all revaluations recognized in annual periods beginning on or after the date of initial application of this amendment and in the immediately preceding annual period. The amendments have no impact on MERALCO's financial position or performance.

Annual Improvements to PFRS (2011-2013 cycle)

The *Annual Improvements to PFRS (2011-2013 cycle)* contain non-urgent but necessary amendments to the following standards:

PFRS 1, First-time Adoption of Philippine Financial Reporting Standards – Meaning of 'Effective PFRS'

The amendment clarifies that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but that permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first PFRS financial statements. This amendment is not applicable to MERALCO's as it is not a first-time adopter of PFRS.



PFRS 3, Business Combinations – Scope Exceptions for Joint Arrangements

The amendment clarifies that *PFRS 3* does not apply to the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively.

PFRS 13, Fair Value Measurement – Portfolio Exception

The amendment clarifies that the portfolio exception in *PFRS 13* can be applied to financial assets, financial liabilities and other contracts. The amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on *MERALCO*'s financial position or performance.

PAS 40, Investment Property

The amendment clarifies the interrelationship between *PFRS 3* and *PAS 40* when classifying property as investment property or owner-occupied property. The amendment states that judgment is needed when determining whether the acquisition of investment property is the acquisition of an asset or a group of assets or a business combination within the scope of *PFRS 3*. This judgment is based on the guidance of *PFRS 3*. This amendment is effective for annual periods beginning on or after July 1, 2014 and is applied prospectively. The amendment has no significant impact on *MERALCO*'s financial position or performance.

Deferred Effectivity

Philippine Interpretation IFRIC 15, Agreements for the Construction of Real Estate

This interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. The interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under *PAS 11* or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and reward of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The Philippine *SEC* and the *PFRSC* have deferred the effectivity of this interpretation until the final Revenue standard is issued by the International Accounting Standards Board and an evaluation of the requirements of the final Revenue standard against the practices of the Philippine real estate industry is completed. Adoption of the interpretation when it becomes effective will not have any impact on the financial statements of *MERALCO*.

PFRS 9, Financial Instruments: Classification and Measurement

PFRS 9, as issued, reflects the first and third phases of the project to replace *PAS 39* and applies to the classification and measurement of financial assets and financial liabilities and hedge accounting, respectively. Work on second phase, which relates impairment of financial instruments, and the limited amendments to the classification and measurement model is still ongoing, with a view to replace *PAS 39* in its entirety. *PFRS 9* requires all financial assets to be measured at fair value at initial recognition. A debt financial asset may, if the fair value option *or FVO*, is not invoked, be subsequently measured at amortized cost if it is held within a business model that has the objective to hold the assets to collect the contractual cash flows and its contractual terms give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal outstanding. All other debt instruments are subsequently measured at fair value through profit or loss. All equity financial assets are measured at fair value either



through *OCI* or profit or loss. All equity financial assets held for trading must be measured at fair value through profit or loss. For liabilities designated as at *FVPL* using the fair value option, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in *OCI*. The remainder of the change in fair value is presented in profit or loss, unless presentation of the fair value change relating to the entity's own credit risk in *OCI* would create or enlarge an accounting mismatch in profit or loss. All other *PAS 39* classification and measurement requirements for financial liabilities have been carried forward into *PFRS 9*, including the embedded derivative separation rules and the criteria for using the *FVO*. *MERALCO* conducted an evaluation of the early adoption of *PFRS 9* and has assessed that the first phase of *PFRS 9* will have an effect on the classification and measurement of financial assets. *MERALCO* will quantify the effect on the parent company financial statements in conjunction with the other phases, when issued, to present a comprehensive picture.

On hedge accounting, *PFRS 9* replaces the rules-based hedge accounting model of *PAS 39* with a more principles-based approach. Changes include replacing the rules-based hedge effectiveness test with an objectives-based test that focuses on the economic relationship between the hedged item and the hedging instrument, and the effect of credit risk on that economic relationship; allowing risk components to be designated as the hedged item, not only for financial items, but also for non-financial items, provided that the risk component is separately identifiable and reliably measurable; and allowing the time value of an option, the forward element of a forward contract and any foreign currency basis spread to be excluded from the designation of a financial instrument as the hedging instrument and accounted for as costs of hedging. *PFRS 9* also requires more extensive disclosures for hedge accounting.

PFRS 9 currently has no mandatory effective date. *PFRS 9* may be applied before the completion of the limited amendments to the classification and measurement model and impairment methodology. *MERALCO* will not adopt the standard before the completion of the limited amendments and the second phase of the project.

Significant Accounting Policies

The principal accounting policies adopted in the preparation of the parent company financial statements are as follows:

Utility Plant and Others

Utility plant and others, except land, are stated at cost, net of accumulated depreciation and amortization and accumulated impairment loss, if any. Costs include the cost of replacing part of such utility plant and others when such cost is incurred, if the recognition criteria are met. All other repair and maintenance costs are recognized as incurred in the parent company statement of income. The present value of the expected cost for the decommissioning of the asset after use is included in the cost of the respective asset if the recognition criteria for a provision are met.

Land is stated at cost less any impairment in value.



MERALCO's utility plant and others are stated at deemed cost. The revalued amount recorded as at January 1, 2004 was adopted as deemed cost as allowed by the transitional provisions of *PFRS 1*. The balance of revaluation increment was closed to retained earnings. Depreciation and amortization of utility plant and others are computed using the straight-line method (except for certain sub-transmission and distribution assets, which use straight-line functional group method) over the following estimated useful lives:

Asset Type	Estimated Useful Lives
Sub-transmission and distribution	10-50 years, depending on the life of the significant parts
Others:	
Buildings and improvements	15-40 years
Communication equipment	10 years
Office furniture, fixtures and other equipment	5-15 years
Transportation equipment	5-10 years
Others	5-20 years

An item of utility plant and others is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising as a result of the derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the parent company statement of income in the year the asset is derecognized.

The assets' residual values, useful lives and methods of depreciation and amortization are reviewed, and adjusted prospectively if appropriate, at each reporting date to ensure that the residual values, periods and methods of depreciation and amortization are consistent with the expected pattern of economic benefits from items of utility plant and others.

Construction in Progress

Construction in progress is stated at cost, which includes cost of construction, plant and equipment, capitalized borrowing costs and other direct costs. Construction in progress is not depreciated until such time that the relevant assets are substantially completed and available for their intended use.

Borrowing Costs

Borrowing costs are capitalized if they are directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. Capitalization of borrowing costs commences when the activities necessary to prepare the qualifying asset for its intended use or sale have been undertaken and expenditures and borrowing costs have been incurred. Borrowing costs are capitalized until the asset is substantially available for its intended use.

Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds, as well as any exchange differences arising from any foreign currency-denominated borrowings used to finance the projects, to the extent that they are regarded as an adjustment to interest costs.

All other borrowing costs are expensed as incurred.



Investment Properties

Investment properties, except land, are stated at cost, net of accumulated depreciation and accumulated impairment loss, if any. The carrying amount includes transaction costs and costs of replacing part of an existing investment property at the time such costs are incurred if the recognition criteria are met and excludes the costs of day-to-day servicing of an investment property.

Investment properties include properties that are being constructed or developed for future use as investment property.

Land classified as investment property is carried at cost less any impairment in value.

MERALCO's investment properties acquired before January 1, 2004 are stated at deemed cost.

Investment properties, except land, are being depreciated on a straight-line basis over the useful lives of five (5) to 35 years.

Investment properties are derecognized either when they have been disposed of or when these are permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss from the derecognition of the investment properties are recognized in the parent company statement of income in the year these are disposed or retired.

Transfers are made to investment property when and only when there is a change in use, evidenced by ending of owner-occupation or commencement of an operating lease to another party. If owner-occupied property becomes an investment property, *MERALCO* accounts for such property in accordance with the policy stated under utility plant and others up to the date of the change in use. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale. Transfers from investment property are recorded using the carrying amount of the investment property at the date of change in use.

Asset Retirement Obligations

Under the terms of certain lease contracts, *MERALCO* is required to dismantle the installations made in leased sites and restore such sites to their original condition at the end of the term of the lease contracts. *MERALCO* recognizes a liability measured at the present value of the estimated costs of these obligations and capitalizes such costs as part of the balance of the related item of utility plant and others and investment properties. The amount of asset retirement obligations is accreted and such accretion is recognized as interest expense.

Intangible Assets

Intangible assets acquired separately are initially measured at cost. Following initial recognition, intangible assets are carried at cost less accumulated amortization and any accumulated impairment loss. The useful lives of intangible assets are assessed at the individual asset level as having either finite or indefinite useful lives.



Intangible assets with finite lives are amortized over the useful economic lives of five years using the straight-line method and assessed for impairment whenever there is an indication that the intangible assets may be impaired. At a minimum, the amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at each reporting date. Changes in the expected useful life or the expected consumption pattern of future economic benefit embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and treated as change in accounting estimates. The amortization expense of intangible assets with finite lives is recognized in the parent company statement of income.

Intangible assets with indefinite useful lives are not amortized, but are assessed for impairment annually either individually or at the cash-generating unit level. The assessment of indefinite useful life is done annually at every reporting date to determine whether such indefinite useful life continues to exist. Otherwise, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

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

Intangible assets generated within the business are not capitalized and expenditures are charged to profit or loss in the year these are incurred.

Investments in Subsidiaries and Associates and Interest in Joint Ventures

Investments in subsidiaries (entities over which *MERALCO* has control) and associates (entities over which *MERALCO* has significant influence) and interests in joint ventures (entities over which *MERALCO* has joint control) are accounted for under the cost method of accounting in the parent company financial statements. Investments in subsidiaries and associates and interests in joint ventures are carried in the parent company statement of financial position at cost less any impairment in value. *MERALCO* recognizes income from the investments only to the extent that *MERALCO* receives distributions from accumulated profits of the subsidiaries, associates and joint venture arising after the date of acquisition. Distributions received in excess of such profits are regarded as recovery of investment and are recognized as a reduction of the cost of the investment.

Impairment of Nonfinancial Assets

MERALCO assesses at each reporting date whether there is an indication that a nonfinancial asset (utility plant and others, investment properties, investments in subsidiaries, associates and interests in joint ventures, receivable from the *BIR* and intangible assets), other than intangible assets with indefinite useful life, may be impaired. If any such indication exists, *MERALCO* makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an individual asset's or a cash-generating unit's fair value less costs to sell and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. The fair value is the amount obtainable from the sale of the asset in an arm's-length transaction. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation factors/parameters, quoted share prices for publicly traded securities or other available fair value indicators. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognized in the parent company statement of income.



An assessment is also made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, *MERALCO* estimates the individual asset's or cash generating unit's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If a reversal of impairment loss is to be recognized, the carrying amount of the asset is increased to its recoverable amount. The increased amount cannot exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the parent company statement of income. After such reversal, the depreciation and amortization expense are adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Intangible assets with indefinite useful lives are tested for impairment annually at every reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired, either individually or at the cash generating unit level, as appropriate. The amount of impairment is calculated as the difference between the recoverable amount of the intangible asset and its carrying amount. The impairment loss is recognized in the parent company statement of income. Impairment losses relating to intangible assets may be reversed in future periods.

Goodwill is reviewed for impairment annually at every reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Impairment is determined for goodwill by assessing the recoverable amount of the cash-generating unit or group of cash-generating units, to which the goodwill relates. Where the recoverable amount of the cash-generating unit or group of cash generating units is less than the carrying amount of the cash generating unit or group of cash generating units to which goodwill has been allocated, an impairment loss is recognized. Impairment losses relating to goodwill cannot be reversed in future periods.

If there is incomplete allocation of goodwill acquired in a business combination to cash-generating units or group of cash-generating units, an impairment testing of goodwill is only carried out when impairment indicators exist. Where impairment indicators exist, impairment testing of goodwill is performed at a level at which the acquirer can reliably test for impairment.

Fair Value Measurement

MERALCO measures financial instruments at fair value at each reporting date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transactions between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either (a) in the principal market for the asset or liability, or (b) in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible to *MERALCO*.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a nonfinancial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.



MERALCO uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- i. Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- ii. Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and
- iii. Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognized in the parent company financial statements on a recurring basis, *MERALCO* determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting year.

For the purpose of fair value disclosures, *MERALCO* has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy.

Inventories

Inventories are stated at the lower of cost or net realizable value. Costs of acquiring materials and supplies including costs incurred in bringing each item to their present location and condition are accounted using the moving average cost method. Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost to sell or the current replacement cost of the asset.

Financial Assets

Initial Recognition

Financial assets are classified as at fair value through profit or loss or *FVPL*, loans and receivables, held-to-maturity or *HTM* investments, *AFS* financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The classification of financial assets is determined at initial recognition and, where allowed and appropriate, re-evaluated at each reporting date.

Financial assets are recognized initially at fair value. Transaction costs are included in the initial measurement of all financial assets, except for financial instruments measured at *FVPL*.

Purchases or sales of financial assets that require delivery of assets within a timeframe established by regulation or convention in the market place (regular way purchase) are recognized on the trade date, which is the date *MERALCO* commits to purchase or sell the asset.

MERALCO's financial assets include cash and cash equivalents, trade and non-trade receivables, advance payments to a supplier, quoted and unquoted equity securities and embedded derivatives that are not accounted for as effective accounting hedges.



Subsequent Measurement

The subsequent measurement of financial assets depends on the classification as follows:

Financial Assets at FVPL

Financial assets at *FVPL* include financial assets held-for-trading and financial assets designated upon initial recognition as at *FVPL*. Financial assets are classified as held-for-trading if they are acquired for the purpose of selling in the near term. Derivative assets, including separated embedded derivatives are also classified as held-for-trading unless they are designated as effective hedging instruments.

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

Financial assets at *FVPL* are carried in the parent company statement of financial position at fair value with gains or losses on fair value changes recognized in the parent company statement of income under “Interest and other financial income” or “Interest and other financial charges” account, respectively. Interest earned and dividends received from investment at *FVPL* are also recognized in the parent company statement of income under “Interest and other financial income” account.

Derivatives embedded in host contracts are accounted for as separate derivatives when their risks and characteristics are not clearly and closely related to those of the host contracts and the host contracts are not carried at fair value. These embedded derivatives are measured at fair value with gains and losses arising from changes in fair value recognized in the parent company statement of income. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required under the contract.

Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such financial assets are carried at amortized cost using the effective interest method. This method uses an effective interest rate that discounts estimated future cash receipts through the expected life of the financial asset to the net carrying amount of the financial asset. Gains or losses are recognized in the parent company statement of income when the loans and receivables are derecognized or impaired, as well as when these are amortized. Interest earned or incurred is recorded in “Interest and other financial income” or “Interest and other financial charges” account, respectively, in the parent company statement of income. Assets in this category are included under current assets except for assets with maturities beyond 12 months from the reporting date, which are classified as noncurrent assets.

HTM Investments

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as *HTM* when *MERALCO* has the positive intention and ability to hold these assets to maturity. After initial measurement, *HTM* investments are measured at amortized cost using the effective interest method. Gains or losses are recognized in the parent company statement of



income. Assets in this category are included in the current assets except for maturities beyond 12 months from the reporting date, which are classified as noncurrent assets.

AFS Financial Assets

AFS financial assets are non-derivative financial assets that are designated as *AFS* or are not classified in any of the three foregoing categories. They are purchased and held indefinitely and may be sold in response to liquidity requirements or changes in market conditions. After initial measurement, *AFS* financial assets are measured at fair value with unrealized gains or losses recognized in other comprehensive income until the investment is derecognized, at which time the cumulative gain or loss recorded in other comprehensive income is recognized in the parent company statement of income, or determined to be impaired, at which time the cumulative loss recorded in other comprehensive income is recognized in the parent company statement of income. Interest earned on holding *AFS* debt securities are included under “Interest and other financial income” account in the parent company statement of income. Dividends earned on holding *AFS* equity are recognized in the parent company statement of income under “Interest and other financial income” account when the right of the payment has been established. These are included under noncurrent assets unless there is an intention to dispose of the investment within 12 months from the reporting date.

Financial Liabilities

Initial Recognition

Financial liabilities are classified as financial liabilities at *FVPL*, other financial liabilities, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The classification of the financial liability is determined at initial recognition.

Financial liabilities are recognized initially at fair value inclusive of directly attributable transaction costs, except for financial liabilities at *FVPL*.

MERALCO’s financial liabilities include notes payable, interest-bearing long-term financial liabilities, trade payables and other current liabilities (excluding output *VAT*, accrued taxes, reinsurance liability and deferred lease income), customers’ deposits, refundable service extension costs, customers’ refund and other noncurrent liabilities.

Subsequent Measurement

The subsequent measurement of financial liabilities depends on their classification as follows:

Financial Liabilities at FVPL

Financial liabilities at *FVPL* include financial liabilities held-for-trading and financial liabilities designated upon initial recognition as at *FVPL*. Financial liabilities are classified as held-for-trading if they are incurred for the purpose of repurchasing in the near term. Derivative liabilities, including separated embedded liabilities are also classified as held-for-trading unless they are designated as effective hedging instruments. Financial liabilities at *FVPL* are carried in the parent company statement of financial position at fair value with gains or losses recognized in the parent company statement of income under “Interest and other financial income” or “Interest and other financial charges” account, respectively. Interest incurred on financial liabilities designated as at *FVPL* is recognized in the parent company statement of income under “Interest and other financial charges” account.



Financial liabilities may be designated at initial recognition as at *FVPL*, if any of the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the liabilities or recognizing gains or losses on them on a different bases; (ii) the financial liabilities are part of a group which are managed and their performance are evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial liabilities contain one or more embedded derivatives that would need to be recorded separately. *MERALCO* does not have financial liabilities designated as at *FVPL* as at December 31, 2013 and 2012.

Other Financial Liabilities

After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method.

Gains and losses are recognized in the parent company statement of income when the liabilities are derecognized as when these are amortized. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are integral part of the effective interest rate. The effective interest amortization is included under “Interest and other financial charges” account in the parent company statement of income.

Derivative Financial Instruments

Initial Recognition and Subsequent Measurement

MERALCO has separated embedded foreign currency forwards which are derivative financial instruments used to hedge risks associated with foreign currency fluctuations.

Derivative instruments, including separated embedded derivatives, are initially recognized at fair value on the date at which a derivative transaction is entered into or separated, and are subsequently re-measured at fair value. Changes in fair value of derivative instruments, other than those accounted for as effective hedges, are recognized immediately in the parent company statement of income. Changes in fair value of derivative instruments accounted as effective hedges are recognized in other comprehensive income. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. *MERALCO* does not have derivatives accounted for under hedge accounting.

An embedded derivative is separated from the hybrid or combined contract if all the following conditions are met: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the hybrid instrument is not recognized as at *FVPL*.

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

See Note 26 – *Financial Assets and Financial Liabilities*.



Offsetting of Financial Instruments

Financial assets and financial liabilities are offset and the net amount is reported in the parent company statement of financial position if, and only if, there is currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Amortized Cost of Financial Instruments

Amortized cost is computed using the effective interest method less any allowance for impairment and principal repayment, plus or minus the cumulative amortization of premium or discount. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of effective interest.

'Day 1' Profit or Loss

Where the transaction price in a non-active market is different from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, *MERALCO* recognizes the difference between the transaction price and fair value (a 'Day 1' profit or loss) in the parent company statement of income, unless it qualifies for recognition as some other type of asset or liability. In cases where data used are not observable, the difference between the transaction price and model value is only recognized in the parent company statement of income when the inputs become observable or when the instrument is derecognized. For each transaction, *MERALCO* determines the appropriate method of recognizing the 'Day 1' profit or loss amount.

Impairment of Financial Assets

MERALCO assesses at each reporting date whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial Assets Carried at Amortized Cost

For financial assets carried at amortized cost, *MERALCO* first assesses whether objective evidence of impairment exists individually. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment based on historical loss experience. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment. *MERALCO* consider termination or disconnection of service and significant financial difficulties of debtors as objective evidence that a financial asset or group of financial assets is impaired. For both specific and collective assessments, any deposits, collateral and credit enhancement are considered in determining the amount of impairment loss.



If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). If a loan is subject to variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The carrying amount of the asset is reduced either directly or through the use of an allowance account and the amount of the loss is recognized in the parent company statement of income. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. The financial asset together with associated allowance is written off when there is no realistic prospect of future recovery and all collateral or deposits has been realized or has been transferred to *MERALCO*.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If an asset written off is recovered, the recovery is recognized in the parent company statement of income. Any reversal of an impairment loss is recognized in the parent company statement of income, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

AFS Financial Assets

In the case of equity instruments classified as *AFS*, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. When a decline in the fair value of an *AFS* financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from equity to profit or loss even though the financial asset has not been derecognized. The amount of the cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on the financial asset previously recognized in profit or loss. Impairment losses recognized in profit or loss for investment in equity instruments are not reversed in the parent company statement of income. Subsequent increases in fair value after impairment are recognized directly in other comprehensive income.

In the case of debt instruments classified as *AFS*, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued based on the rate of interest used to discount future cash flows for the purpose of measuring impairment loss. Such accrual is recorded as part of "Interest and other financial charges" in the parent company statement of income. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the parent company statement of income, the impairment loss is reversed in the parent company statement of income.

Assets Carried at Cost

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



Derecognition of Financial Instruments

Financial Assets

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

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

Where *MERALCO* has transferred its right to receive cash flows from an asset or has entered into a “pass-through” arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, a new asset is recognized to the extent of *MERALCO*’s continuing involvement in the asset.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that *MERALCO* could be required to repay.

Financial Liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or has expired.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the carrying amount of a financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed is recognized in the parent company statement of income.

Redeemable Preferred Stock

MERALCO’s peso-denominated redeemable preferred stock has characteristics of a liability and is thus recognized as a liability in the parent company statement of financial position. The corresponding dividends on those shares are recognized as part of “Interest and other financial charges” account in the parent company statement of income. Dividends are no longer accrued when such shares have been called for redemption.

Provisions

Provisions are recognized when *MERALCO* has a present obligation, legal or constructive, as a result of a past event, and when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where *MERALCO* expects a provision, or a portion, to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only



when the reimbursement is virtually certain. The expense relating to any provision is presented in the parent company statement of income, net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liabilities.

Retirement Benefits

MERALCO has distinct, funded, noncontributory defined benefit retirement plans covering all permanent employees. *MERALCO*'s retirement plan provides for post-retirement benefits in addition to a lump sum payment to employees hired up to December 31, 2003. Retirement benefits for employees hired commencing January 1, 2004 were amended to provide for a defined lump sum payment only. *MERALCO* also has a contributory Provident Plan introduced in January 2009 in which employees hired commencing January 1, 2004 may elect to participate.

The net defined benefit liability or asset is the aggregate of the present value of the defined benefit obligation at the end of the reporting date reduced by the fair value of plan assets (if any), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling. The asset ceiling is the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The cost of providing benefits under the defined benefit plans is actuarially determined using the projected unit credit method.

Defined benefit costs comprise the following:

- Service cost
- Net interest on the net defined benefit liability or asset

Service costs, which include current service costs, past service costs and gains or losses on non-routine settlements are recognized as expense in profit or loss. Past service costs are recognized when plan amendment or curtailment occurs. These amounts are calculated periodically by independent qualified actuaries.

Net interest on the net defined benefit liability or asset is the change during the period in the net defined benefit liability or asset that arises from the passage of time, which is determined by applying the discount rate based on government bonds to the net defined benefit liability or asset. Net interest on the net defined benefit liability or asset is recognized as expense or income in profit or loss.

Remeasurements comprising actuarial gains and losses, return on plan assets excluding amounts included in the net interest cost and any change in the effect of the asset ceiling (excluding net interest on defined benefit liability) are recognized immediately in other comprehensive income in the year in which they arise. Remeasurements are not reclassified to profit or loss in subsequent periods.

Plan assets are assets that are held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the creditors of *MERALCO*, nor can they be paid directly to *MERALCO*. Fair value of plan assets is based on market price information. When no market price is available, the fair value of plan assets is estimated by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligations). If the fair value of the plan assets is higher than the present value of the defined benefit obligation, the measurement of the resulting defined



benefit asset is limited to the present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

MERALCO's right to be reimbursed of some or all of the expenditure required to settle a defined benefit obligation is recognized as a separate asset at fair value when and only when reimbursement is virtually certain.

The retirement costs under the defined contribution plan are recorded based on *MERALCO's* contribution to the defined contribution plan as services are rendered by the employee.

Termination Benefits

Termination benefits are employee benefits provided in exchange for the termination of an employee's employment as a result of either an entity's decision to terminate an employee's employment before the normal retirement date or an employee's decision to accept an offer of benefits in exchange for the termination of employment.

A liability and expense for a termination benefit is recognized at the earlier of when the entity can no longer withdraw the offer of those benefits and when the entity recognizes related restructuring costs. Initial recognition and subsequent changes to termination benefits are measured in accordance with the nature of the employee benefit, as either post-employment benefits, short-term employee benefits, or other long-term employee benefits.

Employee Leave Entitlements

Employee entitlements to annual leave are recognized as a liability when they are accrued to the employees. The undiscounted liability for leave expected to be settled wholly before 12 months after the end of the annual reporting period is recognized for services rendered by employees up to the end of the reporting period.

Long-term Incentive Plan

The liability relating to the long-term incentive plan comprises the present value of the defined benefit obligation at the end of the reporting year.

Employee Stock Purchase Plan or ESPP

Up to 2009, *MERALCO* had an employee stock purchase plan, which covered active and retired employees. Under the plan, the qualified participant may purchase fixed number of shares of stock at a pre-agreed price. The plan features include vesting requirements and payment terms.

The cost of equity-settled transactions with employees is measured by reference to the difference between the fair value of the shares on the grant date and the price at which the share may be purchased under the award or offer. In valuing equity-settled transactions, no account is taken of any performance conditions other than market conditions.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date at which the relevant employees become fully entitled to the award ('the vesting date'). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and *MERALCO's* best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or



credit for a period represents the movement in cumulative expense recognized as at the beginning and end of the reporting period.

No expense is recognized for awards that do not ultimately vest.

When the terms of the equity-settled awards are modified and the modification increases the fair value of the equity instruments granted, as measured immediately before and after the modification, the entity shall include the incremental fair value granted in the measurement of the amount recognized for services received as consideration for the equity instrument granted. The incremental fair value granted is the difference between the fair value of the modified equity instrument and that of the original equity instrument, both estimated as at the date of the modification. If the modification occurs during the vesting period, the incremental fair value granted is included in the measurement of the amount recognized for services received over the period from the modification date until the date when the modified equity instruments vest, in addition to the amount based on the grant date fair value of the original equity instruments, which is recognized over the remainder of the original vesting period. If the modification occurs after vesting date, the incremental fair value granted is recognized immediately or over the vesting period if the employee is required to complete an additional period of service before becoming unconditionally entitled to those modified equity instruments.

Revenue Recognition

Revenues are stated at amounts invoiced to customers, inclusive of pass-through components, net of discounts, rebates, *VAT* and other taxes, where applicable. Revenue is recognized to the extent that it is probable that the economic benefits will flow to *MERALCO* and the revenue can be reliably measured. In addition, collectability is reasonably assured and the delivery of the goods or rendering of the service has occurred. *MERALCO* assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent. *MERALCO* concluded that it is acting as principal in all of its revenue arrangements. The following specific recognition criteria must also be met before revenue is recognized:

Sale of Electricity

Revenues are recognized upon supply of power to the customers. The Uniform Filing Requirements or *UFR*, on the rate unbundling released by the *ERC* on October 30, 2001 specified the following bill components: (a) generation charge, (b) transmission charge, (c) *SL* charge, (d) distribution charge, (e) supply charge, (f) metering charge, (g) Currency Exchange Rate Adjustment or *CERA* I and II, where applicable and (h) interclass and lifeline subsidies. *VAT*, *LFT*, the Power Act Reduction (for residential customers) adjustment and universal charges are also separately presented in the customer's billing statement. *VAT*, *LFT* and universal charges are billed and collected on behalf of the national and local governments and do not form part of *MERALCO*'s revenues.

Interest Income

Revenue is recognized as interest accrues, using the effective interest method. The effective interest rate is the rate that discounts estimated future cash receipts through the expected life of the financial instrument.



Dividends

Revenue is recognized when *MERALCO*'s right to receive the payment is established.

Lease Income

Income arising from lease of investment properties and poles is accounted for on a straight-line basis over the lease term.

Lease income is included under "Revenues – Lease Income" account in the parent company statement of income.

Expense Recognition

Expenses are decreases in economic benefits during the financial reporting period in the form of outflows or decrease of assets or incurrence of liabilities that result in decrease in equity, other than those relating to distributions to equity participants. These are recognized when incurred.

Leases

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

Company as Lessee

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

Company as Lessor

Leases where *MERALCO* does not transfer substantially all the risk and benefits of ownership of the asset are classified as operating lease. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Contingent rents are recognized as revenue in the year in which they are earned.

Foreign Currency-Denominated Transactions and Translations

The parent company financial statements are presented in Philippine peso, which is also *MERALCO*'s functional and presentation currency. The Philippine peso is the currency of the primary economic environment in which *MERALCO* operates. This is also the currency that mainly influences the revenue from and cost of rendering services.

Transactions in foreign currencies are initially recorded in the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated using functional currency closing rate of exchange prevailing at the end of the reporting date. All differences are recognized in the parent company statement of income except for foreign exchange differences that relate to capitalizable borrowing costs on qualifying assets. Nonmonetary items that are measured in terms of historical cost in foreign currency are translated using the exchange rate as at the date of the initial transactions.



Income Taxes

Current Income Tax

Current income tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authority. The tax rate and tax laws used to compute the amount are those that are enacted or substantively enacted as at the reporting date.

Deferred Income Tax

Deferred income tax is provided using the balance sheet liability method on all temporary differences at the reporting date between the income tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized except:

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

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates and tax laws that are enacted or substantively enacted as at the reporting date.

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



Deferred income tax items are recognized in correlation to the underlying transaction either in profit or loss or directly in equity.

Earnings per Share

Basic earnings per share is calculated by dividing the net income for the year by the weighted average number of common shares outstanding during the year.

Diluted earnings per share is calculated by dividing the net income for the year by the weighted average number of shares outstanding, adjusted for the effects of any dilutive potential common shares.

Contingencies

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

Events After the Reporting Date

Post reporting date events that provide additional information about *MERALCO*'s financial position at the reporting date (adjusting events) are reflected in the parent company financial statements. Post reporting date events that are not adjusting events are disclosed in the notes to parent company financial statements, when material.

Equity

Common stock is measured at par value for all shares issued. Incremental costs incurred directly attributable to the issuance of new shares are shown as a deduction from equity, net of any related tax. The amount of proceeds and/or fair value of consideration received, net of incremental costs incurred directly attributable to the issuance of new shares in excess of par value is recognized as additional paid-in capital.

ESPP cost represents the cumulative compensation expense recognized based on the amount determined using an option pricing model. The 14th and last *ESPP*, which was awarded in 2009 fully vested in October 2012. Since 2009, there have been no *ESPPs* implemented.

Other comprehensive income comprises items of income and expense, which are not recognized in profit or loss as required or permitted by *PFRS*.

Retained earnings includes net income and is reduced by dividends declared on common stock. Dividends are recognized as a liability and deducted from retained earnings when they are declared. Dividend declarations approved after the financial reporting date are disclosed as events after the financial reporting date.



5. Management's Use of Judgments, Estimates and Assumptions

The preparation of the parent company financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent assets and liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Judgments

In the process of applying *MERALCO*'s accounting policies, management has made the following judgments, which have the most significant effect on the amounts recognized in the parent company financial statements.

Determination of Functional Currency

The functional currencies of *MERALCO* is the currency of the primary economic environment in which *MERALCO* operates. It is the currency that mainly influences the revenue and cost of rendering services.

Based on the economic substance of the underlying circumstances, the functional and presentation currency of *MERALCO* is the Philippine peso.

Operating Lease Commitments

As Lessor

As a lessor, *MERALCO* has several lease arrangements. Based on the terms and conditions of the arrangements, it has evaluated that the significant risks and rewards of ownership of such properties are retained by *MERALCO*. The lease agreements do not transfer ownership of the assets to the lessees at the end of the lease term and do not give the lessees a bargain purchase option over the assets. Consequently, the lease agreements are accounted for as operating leases.

As Lessee

As a lessee, *MERALCO* has commercial lease arrangements covering certain office spaces, payment offices and substation sites and towers. *MERALCO* has determined, based on the evaluation of the terms and conditions of the arrangements, that it has not acquired any significant risks and rewards of ownership of such properties because the lease arrangements do not transfer to *MERALCO* the ownership over the assets at the end of the lease term and do not provide *MERALCO* a bargain purchase option over the leased assets. Consequently, the lease agreements are accounted for as operating leases.

Arrangement that Contains a Lease

MERALCO's Purchased Power Agreements or *PPAs* and Purchase Supply Agreements or *PSAs* with certain power generating companies qualify as leases on the basis that *MERALCO* and these power generating companies have 'take or pay' or *TOP* arrangements where payments for purchased power are made on the basis of the availability of the power plant and not based solely on actual consumption. In determining the lease classification, it is judged that substantially all the risks and rewards incident to the ownership of the power plants are with these power generating companies. Thus, the *PPAs* and *PSAs* are classified as operating leases. Accordingly, capacity



fees, fixed operating and maintenance, and transmission line fees that form part of purchased power expense are accounted for similar to a lease.

Components of purchased power expense, which have been accounted for similar to a lease, amounted to ₱46,170 million and ₱18,946 million for the years ended December 31, 2013 and 2012, respectively. These are recognized as “Purchased Power” in the parent company statements of income.

See *Note 23 – Revenues and Purchased Power*.

Contingencies

MERALCO has possible claims from or obligation to other parties from past events and whose existence may only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within its control. Management has determined that the present obligations with respect to contingent liabilities and claims with respect to contingent assets do not meet the recognition criteria, and therefore has not recorded any such amounts.

See *Note 28 – Contingencies and Legal Proceedings*.

Estimates and Assumptions

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

Estimating Useful Lives of Utility Plant and Others, Intangible Assets with Finite Lives and Investment Properties

MERALCO estimates the useful lives of utility plant and others, intangible assets with finite lives and, investment properties based on the periods over which such assets are expected to be available for use. The estimate of the useful lives of the utility plant and others, intangible assets with finite lives and investment properties is based on management’s collective assessment of industry practice, internal technical evaluation and experience with similar assets. The estimated useful lives are reviewed at least at each financial year-end and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limitations on the use of such assets. It is possible, however, that future results of operations could be materially affected by changes in estimates brought about by changes in the factors mentioned in the foregoing. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of utility plant and others, intangible assets with finite lives and investment properties would increase recorded operating expenses and decrease noncurrent assets.

The total depreciation and amortization expense of utility plant and others amounted to ₱5,684 million and ₱5,251 million for the years ended December 31, 2013 and 2012, respectively. Total carrying values of utility plant and others, net of accumulated depreciation and amortization, amounted to ₱111,012 million and ₱107,880 million as at December 31, 2013 and 2012, respectively.

Total depreciation of investment properties amounted to ₱5 million and ₱4 million for the years ended December 31, 2013 and 2012, respectively. Total carrying value of investment properties, net of accumulated depreciation, amounted to ₱1,503 million and ₱1,608 million as at December 31, 2013 and 2012, respectively.



Total amortization of intangible assets with finite lives amounted to **₱169 million** and **₱94 million** for the years ended December 31, 2013 and 2012, respectively. Total carrying value of intangible assets with finite lives, net of accumulated amortization, amounted to **₱1,720 million** and **₱1,014 million** as at December 31, 2013 and 2012, respectively.

See *Note 6 – Utility Plant and Others*, *Note 8 – Investment Properties* and *Note 9 – Other Noncurrent Assets*.

Impairment of Nonfinancial Assets

PFRS requires that an impairment review be performed when certain impairment indicators are present. These conditions include obsolescence, physical damage, significant changes in the manner by which an asset is used, worse than expected economic performance, drop in revenues or other external indicators, among others. In the case of goodwill, at a minimum, such asset is subject to an annual impairment test and more frequently whenever there is an indication that such asset may be impaired. This requires an estimation of the value in use of the cash generating unit to which the goodwill is allocated. Estimating the value in use requires preparation of an estimate of the expected future cash flows from the cash generating unit and choosing an appropriate discount rate in order to calculate the present value of those cash flows.

Determining the recoverable amount of utility plant and others, investment properties, investments in subsidiaries and interest in joint ventures, goodwill and other noncurrent assets, requires (i) the determination of future cash flows expected to be generated from the continued use as well as ultimate disposition of such assets and (ii) making estimates and assumptions that can materially affect the parent company financial statements. Future events may cause management to conclude that utility plant and others, construction in progress, investment properties, investments in subsidiaries and interest in joint ventures, and other noncurrent assets are impaired. Any resulting impairment loss could have a material adverse impact on *MERALCO*'s parent company financial position and results of operations.

The preparation of estimated future cash flows involves significant estimations and assumptions. While management believes that the assumptions are appropriate and reasonable, significant changes in the assumptions may materially affect the assessment of recoverable values and may lead to future impairment charges under *PFRS*.

The carrying values of nonfinancial assets as at December 31, 2013 and 2012 subject to impairment review are as follows:

Account	2013	2012
	<i>(Amounts in millions)</i>	
Utility plant and others	₱111,012	₱107,880
Investments in subsidiaries and associates and interests in joint ventures	20,514	3,514
Investment properties	1,503	1,608
Intangible assets	1,720	1,014
Receivable from the <i>BIR</i>	577	577

See *Note 6 – Utility Plant and Others*, *Note 7 – Investments in Subsidiaries, Associates and Interest in Joint Ventures*, *Note 8 – Investment Properties* and *Note 9 – Other Noncurrent Assets*.



Realizability of Deferred Tax Assets

MERALCO reviews the carrying amounts of deferred tax assets at the end of each reporting period and reduces these to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred income tax assets to be utilized. Assessment on the recognition of deferred tax assets on deductible temporary differences is based on the level and timing of forecasted taxable income for the subsequent reporting periods. This forecast is based on past results and future expectations on revenues and expenses as well as future tax planning strategies. Management believes that sufficient taxable profit will be generated to allow all or part of the deferred tax assets to be utilized. The amounts of the deferred tax assets considered realizable could be adjusted in the future if estimates of taxable income are revised. The recognized deferred tax assets as of December 31, 2013 and 2012 amounted to ₱15,364 million and ₱13,307 million, respectively.

See Note 27 – *Income Taxes and Local Franchise Taxes*.

Determination of Fair Values of Financial Assets and Financial Liabilities

Where fair value of financial assets and financial liabilities recorded in the parent company statement of financial position cannot be derived from active markets, they are determined using valuation techniques including the discounted cash flows model. The inputs to these models are taken from observable markets where possible, but when this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

See Note 26 – *Financial Assets and Financial Liabilities*.

Estimating Allowance for Doubtful Accounts

If there is objective evidence that an impairment loss has been incurred in the trade and other receivables balance of MERALCO, an estimate of the allowance for doubtful accounts related to trade and other receivables that are specifically identified as doubtful of collection is made. The amount of allowance is evaluated by management on the basis of factors that affect the collectability of the accounts. In such case, use of judgment based on the best available facts and circumstances, including but not limited to, the length of MERALCO's relationship with the customer and the customer's credit status based on third party credit reports and known market factors, to record specific reserves for customers against amounts due in order to reduce MERALCO's receivables to amounts that management expects to collect is applied. These specific reserves are reevaluated and adjusted as additional information received affect the amounts estimated.

In addition to specific allowance against individually significant receivables, an assessment for collective impairment allowance against credit exposures of the customers, which were grouped based on common credit characteristics, although not specifically identified as requiring a specific allowance, have a greater risk of default than when the receivables were originally granted to customers is done. This collective allowance is based on historical loss experience using various factors, such as historical performance of the customers within the collective group, deterioration in the markets in which the customers operate, and identified structural weaknesses or deterioration in the cash flows of customers.



Total asset impairment provision for trade and other receivables and other current assets recognized in the parent company statements of income amounted to ₱481 million and ₱819 million for the years ended December 31, 2013 and 2012, respectively. Trade and other receivables, net of asset impairment, amounted to ₱29,547 million and ₱26,046 million as at December 31, 2013 and 2012, respectively.

See *Note 11 – Trade and Other Receivables* and *Note 13 – Other Current Assets*.

Estimating Net Realizable Value of Inventories

Inventories consist of materials and supplies used in the power distribution and services segments. The excess of cost over net realizable value relating to inventories consists of collective and specific provisions. The cost of inventories is written down whenever the net realizable value of inventories becomes lower than the cost due to damage, physical deterioration, obsolescence, and change in price levels or other causes. The lower of cost or net realizable value of inventories is reviewed on a periodic basis. Inventory items identified to be obsolete and unusable are written-off and charged as expense in the parent company statement of income.

The carrying values of inventories amounted to ₱2,651 million and ₱1,280 million as at December 31, 2013 and 2012, respectively.

See *Note 12 – Inventories*.

Estimation of Retirement Benefit Costs

The cost of defined benefit pension plans and other post-employment benefits as well as the present value of the pension obligation are determined using actuarial valuations. The actuarial valuation involves making various assumptions. These include the determination of the discount rates, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and its long-term nature, defined benefit obligations are highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date. The pension benefit liability and other post-employment benefit as at December 31, 2013 and 2012 amounted to ₱2,905 million and ₱6,148 million, respectively.

In determining the appropriate discount rate, management considers the interest rates of government bonds in the respective currencies, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation. The underlying bonds are further reviewed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, on the basis that they do not represent high quality bonds.

The mortality rate is based on publicly available mortality tables for the specific country and is modified accordingly with estimates of mortality improvements. Future salary increases and pension increases are based on expected future inflation rates for the specific country.

See *Note 24 – Expenses and Income* and *Note 25 – Long-term Employee Benefits*.

Provision for Asset Retirement Obligations

Provision for asset retirement obligations is recognized in the period in which they are incurred if a reasonable estimate of fair value can be made. This requires an estimation of the cost to restore or dismantle, on a per area basis, depending on the location, and is based on the best estimate of the expenditure required to settle the obligation at the future restoration/dismantlement date,



discounted using a pre-tax rate that reflects the current market assessment of the time value of money and, where appropriate, the risk specific to the liability.

No asset retirement obligation was recognized since the amount is immaterial.

Provisions

MERALCO is involved in various legal proceedings as discussed in *Note 28 – Contingencies and Legal Proceedings*. *MERALCO*'s estimate for probable costs for the resolution of these claims, assessments and cases has been developed in consultation with external counsels handling the defense in these claims, assessments and cases and is based upon thorough analysis of potential outcome.

MERALCO, in consultation with its external legal counsels, does not believe that these proceedings will have a material adverse effect in the parent company financial statements. It is possible, however, that future financial performance could be materially affected by changes in the estimates or the effectiveness of management's strategies and actions relating to these proceedings.

MERALCO recognized provisions amounting to ₱10,749 million and ₱9,225 million for the years ended December 31, 2013 and 2012, respectively.

See *Note 18 – Provisions*.

Revenue Recognition

MERALCO's revenue recognition policies require the use of estimates and assumptions that may affect the reported amounts of its revenues and receivables.

Revenues from sale of electricity by *MERALCO* are billed based on customer-specific billing cycle cut-off date for each customer, while recording of related purchased power cost in the accounts is based on calendar month as provided in the terms of the *PSAs*. The recognition of unbilled revenues for billing cycles with earlier than month-end cut-off dates requires the use of estimates.

The difference between the amounts initially recognized based on provisional invoices and the settlement of the actual billings by the generators is taken up in the subsequent period. Management believes that such use of estimates will not result in material adjustments in future periods.



6. Utility Plant and Others

The movements in utility plant and others are as follows:

Note	Subtransmission and Distribution	Land	Buildings and Improvements	2013				Construction in Progress	Total
				Communication Equipment	Office Furniture, Fixtures and Equipment	Transportation Equipment	Others		
(Amounts in millions)									
Cost:									
	Balance at beginning of year	\$15,181	\$5,023	\$6,175	\$3,340	\$2,419	\$2,111	\$2,639	\$168,569
	Additions	4	—	112	511	157	138	6,192	8,886
	Transfers from construction in progress	—	54	281	1	—	—	(5,763)	—
	Disposals/retirements	—	—	(592)	(897)	(79)	(50)	(2,779)	(2,779)
	Reclassification and others	—	1	80	(31)	(4)	7	—	(200)
	Balance at end of year	\$15,185	\$5,078	\$6,056	\$2,924	\$2,493	\$2,206	\$3,068	\$174,476
Less accumulated depreciation and amortization:									
	Balance at beginning of year	—	1,949	4,456	2,656	1,483	1,115	—	60,689
	Depreciation and amortization	—	118	360	220	179	119	—	5,684
	Disposals/retirements	—	—	(592)	(897)	(79)	(50)	—	(2,779)
	Reclassification and others	—	18	14	—	—	2	—	(130)
	Balance at end of year	—	2,085	4,238	1,979	1,583	1,186	—	63,464
		\$15,185	\$2,993	\$1,818	\$945	\$910	\$1,020	\$3,068	\$111,012

2012										
	Note	Subtransmission and Distribution	Land	Buildings and Improvements	Communication Equipment	Office Furniture, Fixtures and Other Equipment	Transportation Equipment	Others	Construction in Progress	Total
(Amounts in millions)										
Cost:										
Balance at beginning of year		¥125,666	¥14,847	¥4,758	¥5,889	¥3,545	¥2,188	¥1,996	¥2,283	¥161,172
Additions		1,527	334	—	59	367	226	139	6,438	9,090
Transfers from construction in progress		5,620	—	222	240	—	—	—	(6,082)	—
Disposals/retirements		(1,173)	—	(1)	(7)	(13)	(23)	—	(1,217)	—
Reclassification and others	9	41	—	44	(6)	(559)	28	(24)	(476)	—
Balance at end of year		131,681	15,181	5,023	6,175	3,340	2,419	2,111	2,639	168,569
Less accumulated depreciation and amortization:										
Balance at beginning of year		45,825	—	1,812	4,159	2,768	1,342	971	—	56,877
Depreciation and amortization		4,203	—	114	358	268	164	144	—	5,251
Disposals/retirements		(1,030)	—	(1)	(7)	(13)	(23)	—	—	(1,074)
Reclassification and others	9	32	—	24	(54)	(367)	—	—	—	(365)
Balance at end of year		49,030	—	1,949	4,456	2,656	1,483	1,115	—	60,689
		¥82,651	¥15,181	¥3,074	¥1,719	¥684	¥936	¥996	¥2,639	¥107,880



Construction in progress pertains to on-going electric capital projects or *ECPs* and non-electric capital projects or *NEPs*. *ECPs* are capital projects involving construction of new electric distribution-related facilities and the upgrade and major rehabilitation of existing electrical facilities.

Total interest capitalized amounted to ₱122 million and ₱127 million for the years ended December 31, 2013 and 2012, respectively. The average annual interest rates used for capitalization in 2013 and 2012 ranged from 4.6% to 5.9% and 5.5% to 6.2%, respectively.

7. Investments in Subsidiaries and Associates and Interests in Joint Ventures

This account consists of the following as at December 31, 2013 and 2012:

	Place of Incorporation	Principal Business Activities	2013		2012	
			Percentage of Ownership		Percentage of Ownership	
			Direct	Indirect	Direct	Indirect
Subsidiaries						
Corporate Information Solutions, Inc., or <i>CIS</i>	Philippines	e-Transactions	100	—	100	—
<i>CIS Bayad Center, Inc.</i> , or <i>Bayad Center</i>	Philippines	Bills payment collection	—	100	—	100
<i>Customer Frontline Solutions, Inc.</i> or <i>CFSI</i>	Philippines	Teller services	—	100	—	100
Meralco Energy, Inc., or <i>MEI</i>	Philippines	Energy systems management	100	—	100	—
eMERALCO Ventures, Inc., or e-MVI	Philippines	e-Business development	100	—	100	—
<i>Paragon Vertical Corporation</i>	Philippines	Information technology and multi-media services	—	100	—	100
<i>MGen</i>	Philippines	Development of power generation plants	100	—	100	—
<i>Calamba Aero Power Corporation¹</i>	Philippines	Power generation	—	100	—	100
<i>Atimonan Land Ventures Development Corporation</i>	Philippines	Real estate	—	100	—	100
<i>Luzon Natural Gas Energy Corporation²</i>	Philippines	Power generation	—	100	—	—
<i>MPG Asia Limited</i>	British Virgin Islands	Holding company	—	100	—	—
Meralco Financial Services Corporation or <i>Finserve</i>	Philippines	Financial services provider	100	—	100	—
Republic Surety and Insurance Company, Inc. or <i>RSIC</i>	Philippines	Insurance	100	—	100	—
Lighthouse Overseas Insurance Limited or <i>LOIL</i>	Bermuda	Insurance	100	—	100	—
Miescorrail, Inc. or <i>Miescorrail³</i>	Philippines	Engineering, construction and maintenance of mass transit system	100	—	—	100
<i>MIESCOR</i>	Philippines	Engineering, construction and consulting services	99	—	99	—
<i>MIESCOR Builders Inc. or MBI</i>	Philippines	Electric transmission and distribution operation and maintenance services	—	100	—	100
<i>MIESCOR Logistics Inc. or MLI</i>	Philippines	General services, manpower/maintenance	—	100	—	100
<i>CEDC</i>	Philippines	Power distribution	65	—	65	—
Associates						
Buang Private Power Corporation or <i>BPPC</i>	Philippines	Power generation	38	—	38	—
General Electric Philippines Meter and Instrument Company, Inc. or <i>GEPMICI</i>	Philippines	Sale of metering products and services	35	—	35	—

(Forward)



	Place of Incorporation	Principal Business Activities	2013		2012	
			Percentage of Ownership		Direct	Indirect
			Direct	Indirect		
Joint Ventures						
<i>Indra Philippines</i>	Philippines	Management and information technology, or IT, consultancy	50	—	50	—
Rockwell Business Center	Philippines	Real estate	30	—	30	—

¹ Incorporated February 15, 2011 and has not started commercial operations as at December 31, 2013.

² Incorporated January 11, 2013 and has not started commercial operations as at December 31, 2013.

³ On December 26, 2013, MIESCOR assigned its entire shareholdings in Miescorrail to MERALCO.

The movements of investments in subsidiaries and associates and interest in joint ventures are as follows:

	2013	2012
	(Amounts in millions)	
Balance at beginning of year	₱3,514	₱3,071
Additions	17,000	473
Return of capital from an associate	—	(30)
Balance at end of year	₱20,514	₱3,514

CIS

CIS was incorporated in 1974 to provide information technology services and integrated business solutions to enterprise clients. In 1997, *CIS* engaged in the business of bills payment collection, which was spun off as *CIS Bayad Center, Inc.* or *Bayad Center*. *Bayad Center* offers a network of bills payment collection services in the Philippines operating nationwide with brand name “Bayad Center”.

MEI

MEI was established as a wholly-owned subsidiary of *MERALCO* in June 2000 to provide demand-side energy services to *MERALCO*’s key accounts. It offers integrated energy efficiency solutions including marketing, engineering design capability, turnkey installation management, project financing development, monitoring and performance assurance of energy management projects.

e-MVI

e-MVI is a telecommunications infrastructure anchored on a 2,000-km fiber optic network within the *MERALCO* franchise area. It offers data connectivity solutions to local and international carriers, internet service providers, data centers and other businesses.

MGen

MERALCO’s re-entry into power generation through *MGen* is through its investment in operating companies or participation in the development of power generation projects.



On July 22, 2011, *MGen* signed a Shareholders' Agreement with Therma Power, Inc. or *TPI*, and Taiwan Cogeneration International Corporation – Philippine Branch or *TCIC*, for the construction and operation of a 2 x 300 *MW* Circulating Fluidized Bed or *CFB* independent, coal-fired power plant to be located in the Subic Bay Freeport Zone. Redondo Peninsula Energy, Inc. or *RP Energy*, is a partnership among *TPI*, *MGen* and *TCIC*.

As at March 17, 2014, site preparation work is almost complete and *RP Energy* has commissioned its contractor to conduct preliminary engineering works on the power plant in order to reduce the overall construction year. The Department of Environment and Natural Resources or *DENR*, has issued the Environmental Compliance Certificate or *ECC* for the 2 x 300 *MW* coal-fired power plant following a rigorous review and public consultation process.

A Writ of Kalikasan was filed with the *SC* by certain parties opposing the *RP Energy* project. The case was remanded by the *SC* to the *CA* for hearing on the merits thereof. A decision has been issued by the *CA* denying the Writ of Kalikasan, but noting certain deficiencies in the process of the *DENR* in its issuance of the original *ECC* for the 2 x 300 *MW* coal-fired power plant and in the process of the Subic Bay Metropolitan Authority or *SBMA* in the conclusion of the original Lease and Development Agreement or *LDA* with *RP Energy*, and declaring these invalid. *DENR*, *SBMA* and *RP Energy* have filed their respective Motions to the *SC* to review the *CA* decision. On December 19, 2013, *RP Energy* filed a manifestation and Motion requesting that the *SC* deem the petitioners to have waived their rights to file their comments and requested that *RP Energy*'s Petition for Review of Certiorari which was filed with the *SC* on July 17, 2013, be submitted for resolution without the need for further submissions. As at March 17, 2014, no resolution has been issued by the *SC*. Meanwhile, *RP Energy* is proceeding with certain development activities that are not hampered by the *SC* proceedings.

While the original *LDA* was declared invalid by the *CA*, the *SMBA* is also set to ratify an Amended and Restated *LDA* to reflect additional terms.

FPM Power is 40%-owned by *MERALCO* through *MPG Asia Limited*, a subsidiary of *MGen*, and 60% owned by *First Pacific*. On March 28, 2013, *FPM Power* acquired a 70% interest in *PacificLight Power*, which owns and operates a 2 x 400 *MW* liquefied natural gas or *LNG*-fired power plant in Jurong Island, Singapore. *PacificLight Power*'s wholly owned subsidiary, *PacificLight Energy Pte. Ltd.*, is engaged in energy trading.

On August 29, 2013, *MGen* signed a Joint Development Agreement with New Growth B.V., a 100% subsidiary of Electricity Generating Public Company Limited of Thailand or *EGCO*, for the development of a new 460 *MW* (net) supercritical coal-fired power plant in Mauban, Quezon. *MGen*'s equity in the joint venture company, San Buenaventura Power Ltd. Co. or *SBPL*, is 51%, with the option to assign or transfer 2% thereof to a party or investor of its preference. *SBPL*, together with their consultants are evaluating the Engineering, Procurement and Construction or *EPC*, tenders and is expected to award the same by the second quarter of 2014. Simultaneously with its financial advisors, *SBPL* is in discussions with several banks for the financing of the project. A *PSA* is currently being negotiated between the representatives of *EGCO* and *MERALCO*, with the intent of submitting the same to the *ERC* for approval.



On October 7, 2013, *MGen* executed a Share Sale and Purchase Agreement with First Metro Investment Corporation or *FMIC*, and signed a Shareholders Agreement on October 22, 2013, for the sale by *FMIC* of a 20% equity interest in Global Business Power Corporation or *GBPC*, to *MGen*. *GBPC* owns an aggregate of 627 *MW* (gross) capacity of combined coal and diesel power plants in operation in the Visayas region. An 82 *MW* (gross) coal power plant and a 150 *MW* (gross) coal power plant in Panay are under construction and are expected to be in commercial operation by late 2014.

Finserve

Finserve has embarked on investing and managing commercial center operations with *The Strip* along Ortigas Avenue as its flagship project. *Finserve* also has in its portfolio the Integrated Direct Marketing business, which offers targeted advertising and marketing services utilizing nontraditional channels.

RSIC

RSIC is a professional non-life insurance company acquired in 2007 to align with *MERALCO*'s recognition of the imperative for a disciplined approach in managing its risk exposures.

LOIL

LOIL, a captive reinsurer, is registered as a Class 1 insurer under The Bermuda Insurance Act 1978 and Related Regulations. *LOIL* was incorporated in Bermuda in 2007 and received its license to operate in the territory in 2008.

MIESCOR

MIESCOR is a contractor - specialist engaged in engineering, construction and maintenance activities related to power generation, transmission and distribution, as well as industrial plants, water resources and telecommunications.

CEDC

CEDC is registered with Clark Development Corporation or *CDC*, under RA No. 9400, *Bases Conversion Development Act of 1992*, as a Clark Special Economic Zone or *CSEZ*, enterprise, primarily engaged in owning, operating, and maintaining a power distribution system within *CSEZ*.

BPPC

BPPC was organized in October 1992 to engage in the power generation business.

In accordance with the Build-Operate-Transfer, or *BOT* Agreement signed in 1993, First Private Power Corporation or *FPPC*, then parent company, constructed the 215*MW* Bauang Power Plant or *Bauang Plant*, and operated the same under a 15-year Cooperation Period up to July 25, 2010.

On July 26, 2010, *FPPC* turned over the *Bauang Plant* to National Power Corporation, or *NPC* without any compensation and free of any liens. Thereafter, *FPPC* and *BPPC* were legally merged, with *BPPC* as the surviving entity. Subsequent thereto, *BPPC* began winding down operations.



GEPMICI

GEPMICI was established in 1979 together with General Electric Company of U.S.A., to serve the Philippine market for ANSI-type Watt-hour meters.

Indra Philippines

Indra Philippines is an Information Technology or *IT* service provider in the country and in the Asia Pacific region, with a wide range of services across various industries. *Indra Philippines* supports *MERALCO*'s information technology requirements in the area of system development, outsourcing of *IS* and *IT* operations and management consulting.

Rockwell Business Center

The Rockwell Business Center is a joint venture between *Rockwell Land* and *MERALCO*, where *Rockwell Land* shall construct three (3) Business Process Outsourcing or *BPO*, enabled buildings in a non-regulatory asset base property of *MERALCO* over a pre-agreed cooperation period. Investment in Rockwell Business Center represents *MERALCO*'s 30% interest in the joint venture. *Rockwell Land* owns 70% interest in Rockwell Business Center.

MERALCO and *Rockwell Land* share in earnings before depreciation and amortization at 80% and 20%, respectively until 2014 or until certain operational indicators are reached, whichever comes first. Sharing of depreciation and amortization is proportionate to their contribution.

8. Investment Properties

The movements in investment properties are as follows:

	2013		
	Land	Buildings and Improvements	Total
	<i>(Amounts in millions)</i>		
Cost:			
Balance at beginning of year	₱1,535	₱176	₱1,711
Disposals	(89)	(25)	(114)
Balance at end of year	1,446	151	1,597
Less accumulated depreciation:			
Balance at beginning of year	—	103	103
Depreciation	—	5	5
Disposals	—	(14)	(14)
Balance at end of year	—	94	94
	₱1,446	₱57	₱1,503



	2012		
	Land	Buildings and Improvements	Total
	<i>(Amounts in millions)</i>		
Cost	₱1,535	₱176	₱1,711
Less accumulated depreciation:			
Balance at beginning of year	–	99	99
Depreciation	–	4	4
Balance at end of year	–	103	103
	₱1,535	₱73	₱1,608

Investment properties are stated at cost. These consist of real properties held for capital appreciation, former substation sites and other non-regulatory asset base real properties, some of which are being leased out.

The aggregate fair values of the investment properties as at December 31, 2013 and 2012 are as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Land	₱1,863	₱1,853
Buildings and improvements	131	173

Land pertains primary to properties where the *BPO* building and “Strip” mall are located and other non-regulated asset base properties.

The fair values of investment properties were determined by independent, professionally qualified appraisers. The fair value represents the price that would be received to sell an investment property in an orderly transaction between market participants at the measurement date.

The fair value disclosures of the investment properties are categorized as Level 3 as there is no active market for identical or similar properties. The inputs include price per square meter ranging from ₱500 to ₱94,000. There have been no changes in the valuation techniques used.

In conducting the appraisal, the independent professional appraisers used any of the following approaches:

a. Market Data or Comparative Approach

Under this approach, the value of the property is based on sales and listings of comparable property registered within the vicinity. This approach requires the establishment of a comparable property by reducing comparative sales and listings to a common denominator with the subject. This is done by adjusting the differences between the subject property and those actual sales and listings regarded as comparables. The properties used are either situated within the immediate vicinity or at different floor levels of the same building, whichever is most appropriate to the property being valued. Comparison was premised on the factors of location, size and physical attributes, selling terms, facilities offered and time element.



b. Depreciated Replacement Cost Approach

This method of valuation considers the cost to reproduce or replace in new condition the assets appraised in accordance with current market prices for similar assets, with allowance for accrued depreciation based on physical wear and tear and obsolescence.

9. Other Noncurrent Assets

This account consists of:

	Note	2013	2012
<i>(Amounts in millions)</i>			
Unbilled receivables	11	₱18,394	₱4,954
Intangible assets	6	1,720	1,014
Deferred input VAT		1,646	1,094
Receivable from the BIR		577	577
Advance payments to a supplier		474	325
AFS investments	26	124	299
Others		2	63
		₱22,937	₱8,326

Unbilled Receivables

This account represents unbilled generation and other pass-through costs incurred by *MERALCO* as a *DU*, which are still to be billed and which are covered by an approved recovery mechanism of the *ERC*. This also includes other unbilled generation and pass-through charges of current and prior periods, which are the subject of various applications for recovery and approval by the *ERC*.

Deferred Input VAT

The amount includes portion of input *VAT* incurred and paid in connection with purchase of capital assets in excess of ₱1 million per month. As provided for in *RA* No. 9337 or “*EVAT Law*”, said portion of input *VAT* shall be deferred and credited evenly over the estimated useful lives of the related capital assets or 60 months, whichever is shorter, against the output *VAT* due.

Intangible Assets

The movements of intangible assets are as follows:

	2013		
	Software	Franchise	Total
<i>(Amounts in millions)</i>			
Cost:			
Balance at beginning of year	₱1,517	₱49	₱1,566
Additions	875	—	875
Balance at end of year	2,392	49	2,441
Less accumulated amortization:			
Balance at beginning of year	552	—	552
Amortization	169	—	169
Balance at end of year	721	—	721
	₱1,671	₱49	₱1,720



	2012		
	Software	Franchise	Total
	<i>(Amounts in millions)</i>		
Cost:			
Balance at beginning of year	₱734	₱49	₱783
Additions	307	—	307
Reclassification	476	—	476
Balance at end of year	1,517	49	1,566
Less accumulated amortization:			
Balance at beginning of year	93	—	93
Amortization	94	—	94
Reclassification	365	—	365
Balance at end of year	552	—	552
	₱965	₱49	₱1,014

10. Cash and Cash Equivalents

This account consists of:

	2013	2012
	<i>(Amounts in millions)</i>	
Cash on hand and in banks	₱3,871	₱2,266
Cash equivalents	53,736	56,326
	₱57,607	₱58,592

Cash in banks earns interest at prevailing bank deposit rates. Cash equivalents are temporary cash investments, which are made for varying periods of up to three months depending on MERALCO's immediate cash requirements, and earn interest at the prevailing short-term investment rates.

11. Trade and Other Receivables

This account consists of:

	Note	2013	2012
		<i>(Amounts in millions)</i>	
Trade receivables:			
Billed	22	₱26,830	₱23,124
Unbilled	2 and 9	4,175	4,630
Nontrade receivables	22	1,505	848
		32,510	28,602
Less allowance for doubtful accounts		2,963	2,556
		₱29,547	₱26,046



Billed receivables from sale of electricity consist of the following:

	2013	2012
	<i>(Amounts in millions)</i>	
Commercial	₱11,870	₱11,781
Residential	9,443	6,177
Industrial	4,989	4,796
Flat streetlights	528	370
	26,830	23,124
Less allowance for doubtful accounts	2,963	2,556
	₱23,867	₱20,568

Movements of allowance for doubtful accounts are as follows:

	2013			
	Balance at Beginning of Year	Provisions (Reversals)	Write-offs	Balance at End of Year
	<i>(Amounts in millions)</i>			
Billed trade receivables:				
Commercial	₱1,028	₱175	(₱38)	₱1,165
Residential	555	742	(230)	1,067
Industrial	772	(204)	(38)	530
Flat streetlights	201	5	(5)	201
	₱2,556	₱718	(₱311)	₱2,963

	2013			
	Commercial	Residential	Industrial	Flat Streetlights
	<i>(Amounts in millions)</i>			
Individually impaired	₱123	₱762	₱294	₱30
Collectively impaired	1,042	305	236	171
Total	₱1,165	₱1,067	₱530	₱201

	2012			
	Balance at Beginning of Year	Provisions (Reversals)	Write-offs	Balance at End of Year
	<i>(Amounts in millions)</i>			
Billed trade receivables:				
Commercial	₱911	₱140	(₱23)	₱1,028
Residential	528	162	(135)	555
Industrial	73	700	(1)	772
Flat streetlights	438	(9)	(228)	201
	₱1,950	₱993	(₱387)	₱2,556

	2012			
	Commercial	Residential	Industrial	Flat Streetlights
	<i>(Amounts in millions)</i>			
Individually impaired	₱142	₱345	₱206	₱64
Collectively impaired	886	210	566	137
Total	₱1,028	₱555	₱772	₱201



Trade Receivables

Trade receivables include charges for pass-through costs. Pass-through costs consist largely of generation and transmission charges, which represent 57% and 9%, respectively, of the total billed amount in 2013 and 58% and 10%, respectively, of the total billed amount in 2012. Billed receivables are generally due 10 days after bill date.

Unbilled receivables represent electricity consumed after the meter reading cut-off dates, which will be billed to customers in the immediately following billing period. This also includes the current portion of pass-through cost under-recoveries, net of over-recoveries, which are billed to customers over the allowed recovery period approved by the *ERC*. Trade receivables are noninterest-bearing and are substantially secured by bill deposits.

See *Note 17 – Customers’ Deposits* and *Note 26 – Financial Assets and Financial Liabilities*.

12. Inventories

	2013	2012
	<i>(Amounts in millions)</i>	
Materials and supplies:		
At net realizable value	₱2,651	₱1,280
At cost	2,854	1,487
Total inventories at the lower of cost or net realizable value	₱2,651	₱1,280

13. Other Current Assets

This account consists of:

	<i>Note</i>	2013	2012
		<i>(Amounts in millions)</i>	
Short-term investments	<i>17 and 26</i>	₱4,841	₱—
Pass-through <i>VAT</i> - net		1,116	1,389
Prepaid tax		734	475
Prepaid expenses		263	46
Prepayments to suppliers		113	79
Derivative assets	<i>26</i>	—	24
		₱7,067	₱2,013

Pass-through *VAT* pertains to *VAT* on generation and transmission costs, as a *DU*. Remittance of such deferred *VAT* to the generation companies is based on collection of billed receivables from the customers.

Short-term investments are temporary cash placements which are made for varying years beyond three (3) months but not exceeding 12 months, and earn interest at the prevailing short-term placement investment rates.



14. Equity

Common Stock

The movement in the number of shares (in millions) of *MERALCO*'s common stock is as follows:

	2013	2012
	<i>(In millions, except par value)</i>	
Authorized - ₱10 par value a share	1,250	1,250
Issued and outstanding:		
Balance at beginning and end of year	1,127	1,127

The common shares of *MERALCO* were listed in the *PSE* on January 8, 1992. There are 46,409 and 47,892 shareholders of *MERALCO*'s common shares as at December 31, 2013 and 2012, respectively.

Unappropriated Retained Earnings

The unappropriated retained earnings as at December 31, 2013 and 2012 include the balance of revaluation increment in utility plant and others and investment properties carried at deemed cost, deferred tax assets and derivative assets amounting to ₱32,226 million and ₱31,286 million as at December 31, 2013 and 2012, respectively. These amounts are restricted for dividend declaration purposes as of the close of the respective reporting periods.

The following are cash dividends declared on common shares in 2013 and 2012:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
				<i>(In millions)</i>
July 29, 2013	August 27, 2013	September 20, 2013	₱4.10	₱4,621
February 25, 2013	March 26, 2013	April 24, 2013	6.10	6,875
July 30, 2012	August 29, 2012	September 24, 2012	4.00	4,508
February 27, 2012	March 23, 2012	April 23, 2012	4.10	4,621

MERALCO pays regular cash dividends equivalent to 50% of consolidated core net income for the year, which may be supplemented by a special dividend determined on a "look-back" basis. Declaration and payment of a special dividend is dependent on the availability of unrestricted retained earnings and availability of free cash. The declaration, record and payment dates shall be consistent with the guidelines and regulations of the *SEC*.

Appropriated Retained Earnings

On February 22, 2010, retained earnings of ₱6,000 million have been appropriated specifically for *MERALCO*'s business expansion into power generation. The amount appropriated was increased by ₱5,000 million to cover the new development projects and investments in power generation initiatives. The additional appropriation was approved on March 22, 2013 by the *BOD*. As at March 17, 2014, the development of the first project, a 2 x 300 MW CFB coal-fired plant through *RP Energy* is ongoing. *MERALCO* signed a Joint Development Agreement and Shareholders Agreement to develop a supercritical coal-fired power plant, which has target completion by the end of 2017.



The commercial operations date of the 600 MW power plant of *RP Energy* is dependent on the SC decision on the appeal filed by *RP Energy* and other parties in connection with the decision reached by the CA on the Writ of Kalikasan case filed against the *RP Energy* project. On the other hand, the 2 x 400 MW LNG plant of *PacificLight Power* was fully synchronized to the Singapore power grid in January 2014.

See Note 7 – *Investments in Subsidiaries and Associates and Interest in Joint Ventures*.

Treasury Shares

Treasury shares represent subscribed shares and the related rights of employees who have opted to withdraw from the *ESPP* in accordance with the provisions of the *ESPP* and which *MERALCO* purchased. For the years ended December 31, 2013 and 2012, a total of 559 shares and 25,830 shares, respectively, were acquired from employees who have opted to cancel their participation in the *ESPP*.

15. Employee Stock Purchase Plan

MERALCO has an *ESPP*, which entitles participants to purchase its common shares subject to certain terms and conditions, during a nominated offer period. There were no other *ESPP* awards since October 2009. Movements in the number of common shares subscribed by employees under the *ESPP* are as follows:

	2013			
	13 th	13 th A	14 th	Total
Balance at beginning of year	3,309	135,703	7,753,272	7,892,284
Fully paid	(3,309)	(67,370)	(2,045,911)	(2,116,590)
Cancelled	–	–	(559)	(559)
Balance at end of year	–	68,333	5,706,802	5,775,135

	2012			
	13 th	13 th A	14 th	Total
Balance at beginning of year	1,189,306	389,355	12,284,290	13,862,951
Fully paid	(1,185,997)	(251,747)	(4,507,093)	(5,944,837)
Cancelled	–	(1,905)	(23,925)	(25,830)
Balance at end of year	3,309	135,703	7,753,272	7,892,284

MERALCO allotted a total of 55 million common shares for *ESPP* awards. As at December 31, 2013, 12 million common shares are available for any future offerings.

The fair value of the offerings was estimated at the dates of the grant using the Black-Scholes Option Pricing Model.

Total expense arising from the employee stock purchase plan is nil and ₱134 million for the years ended December 31, 2013 and 2012, respectively.

See Note 24 – *Expenses and Income*.



16. Interest-bearing Long-term Financial Liabilities

This account consists of the following:

	2013	2012
	<i>(Amounts in millions)</i>	
Long-term portion of interest-bearing long-term financial liabilities -		
Long-term debt	₱20,756	₱20,466
Current portion of interest-bearing long-term financial liabilities:		
Long-term debt	9,459	766
Redeemable preferred stock	1,562	1,594
	11,021	2,360
	₱31,777	₱22,826

All of the redeemable preferred shares have been called for redemption as at June 30, 2011, consistent with the terms of the Preferred Shares Subscription Agreement. The accrued interests amounted to ₱250 million and ₱256 million as at December 31, 2013 and 2012, respectively. Interest is no longer accrued when the preferred shares have been called for redemption.

The details of interest-bearing long-term financial liabilities are as follows:

Description	2013	2012
	<i>(Amounts in millions)</i>	
<i>Bonds</i>		
₱11.5 Billion 7-year Bonds	₱11,500	₱—
₱7.0 Billion 12-year Bonds	7,000	—
<i>Fixed Rate Loans</i>		
₱5.0 Billion Note Facility Agreement	4,900	4,950
₱4.8 Billion Note Facility Agreement	3,417	4,776
₱3.0 Billion Note Facility Agreement	530	3,000
₱5.0 Billion Note Facility Agreement	—	4,900
<i>Floating Rate Loans</i>		
₱2.5 Billion Term Loan Facility	2,475	2,488
₱3.0 Billion Term Loan Facility	600	1,200
Total long-term debt	30,422	21,314
Less unamortized debt issuance costs	207	82
	30,215	21,232
<i>Redeemable Preferred Stock</i>	1,562	1,594
	31,777	22,826
Less current portion	11,021	2,360
Long-term portion of interest-bearing financial liabilities	₱20,756	₱20,466



All of *MERALCO*'s interest-bearing long-term financial liabilities as at December 31, 2013 and 2012 are denominated in Philippine pesos. The scheduled maturities of *MERALCO*'s outstanding long-term debt at nominal values as at December 31, 2013 are as follows:

	Amount (In millions)
December 31, 2014	₱9,459
December 31, 2015	13
December 31, 2016	12
December 31, 2017	12
After December 31, 2017	20,926
	<u>₱30,422</u>

Bonds

₱18.5 Billion Fixed Rate Putable Bonds

On September 23, 2013, the *BOD* of *MERALCO* authorized the offer, sale and issuance by way of public offering in the Philippines, 7-year and 12-year corporate bonds, putable in 5 and 10 years, respectively, with an aggregate principal amount of up to ₱15 billion with an overallotment option of up to ₱5.0 billion. The 12-year corporate bonds also include a call option, where *MERALCO* may redeem (in whole but not in part only) the outstanding bonds on the 7th year from issue date at the early redemption price of 101.0%. The put and call options are clearly and closely related to the host instruments, thus, were not recognized separately.

On December 12, 2013, the ₱11.5 Billion Fixed Rate Putable Bonds due in 2020 and ₱7.0 Billion Fixed Rate Putable Bonds due in 2025, were listed on the Philippine Dealing and Exchange Corporation.

The net proceeds of the bonds will be utilized for refinancing certain loans including principal payments, accrued interest, prepayment penalties and other financing costs.

Fixed Rate Loans

₱5.0 Billion Note Facility Agreement

In June 2011, *MERALCO* entered into a Fixed Rate Note Facility Agreement for its ₱500 million, 7-year Notes and ₱4,500 million, 10-year Notes due in 2018 and 2021, respectively. The principal is payable in nominal annual amortizations with a balloon payment on each of the two maturity dates.

₱4.8 Billion Note Facility Agreement

In November 2010, *MERALCO* signed a Fixed Rate Note Facility Agreement for its ₱1,997 million, 7-year fixed rate notes and ₱2,803 million, 10-year fixed rate notes. The notes were issued on December 2, 2010 and are payable in nominal annual amortizations with a balloon payment on each of the two maturity dates in December 2018 and December 2020.

In December 2013, *MERALCO* pre-terminated and settled the principal amount of ₱1,334 million. In January 2014, *MERALCO* pre-terminated and settled the remaining principal of ₱3,417 million.



₱3.0 Billion Note Facility Agreement

On January 5, 2012, *MERALCO* signed a ₱3,000 million Fixed Rate Note Facility Agreement for its ₱1,000 million, 7-year notes and ₱2,000 million, 10-year notes due in 2019 and 2022, respectively. The notes were priced off the relevant 7-year and 10-year benchmarks plus a spread and were issued on January 9, 2012. Principal repayments are through annual nominal amortizations and a balloon payment on maturity date. In December 2013, *MERALCO* pre-terminated and settled the principal amount of ₱2,440 million. In March 2014, *MERALCO* pre-terminated and settled the remaining principal of ₱530 million.

₱5.0 Billion Note Facility Agreement

In December 2010, *MERALCO* entered into a Fixed Rate Note Facility Agreement for the issuance of ₱23 million, 5-year fixed rate notes maturing in December 2015 and ₱4,977 million, 5.5-year fixed rate notes due in June 2016. The 5-year fixed rate notes are payable in full at maturity date while the 5.5-year fixed rate notes are payable in nominal annual amortizations with a balloon payment on maturity date. In December 2013, *MERALCO* pre-terminated and settled the entire principal amount of ₱4,900 million.

Floating Rate Loans

₱2.5 Billion Term Loan Facility

The ₱2,500 million, 7-year Floating Rate Term Loan Facility, was drawn in January 2011 from a local bank. Interest rate is repriced every six months based on 6-month *PDST-F* plus a spread. The principal is payable in nominal annual amortizations with a balloon payment on final maturity in January 2018.

₱3.0 Billion Term Loan Facility

The ₱3,000 million, 5-year bilateral Floating Rate Term Loan Facility, was drawn in October 2009. The principal is payable over five years with final maturity in October 2014.

Long-term debt totaling ₱3,947 million, pre-terminated between January to March 17, 2014 and ₱4,850 million to be pre-terminated in June 2014, were classified as part of the current portion of the long-term interest-bearing financial liabilities as at December 31, 2013.

The average annual interest rates for the interest-bearing financial liabilities are as follows:

	2013	2012
Bonds	4.38%-4.88%	—
Fixed Rate Loans	5.23%-6.89%	5.23%-7.47%
Floating Rate Loans	0.80%-1.74%	2.63%-2.99%

Debt Covenants

MERALCO's loan agreements require compliance with debt service coverage of 1.2 times calculated at specific measurement dates. The agreements also contain restrictions with respect to the creation of liens or encumbrances on assets, issuance of guarantees, mergers or consolidations, disposition of a significant portion of its assets and related party transactions.

As at December 31, 2013 and 2012, *MERALCO* is in compliance with all covenants of the loan agreements.



Unamortized Debt Issuance Costs

Unamortized debt issuance costs amounted to ₱207 million and ₱82 million as at December 31, 2013 and 2012, respectively.

The following presents the changes to the unamortized debt issuance costs:

	<i>Note</i>	2013	2012
<i>(Amounts in millions)</i>			
Balance at beginning of year		₱82	₱97
Additions		186	22
Amortization charged to interest and other financial charges	24	(61)	(37)
Balance at the end of year		₱207	₱82

Redeemable Preferred Stock

The movements in the number of shares of the redeemable preferred stock, which have all been called, are as follows:

	2013	2012
Balance at beginning of year	159,356,939	165,129,647
Redemptions	(3,167,771)	(5,772,708)
Balance at end of year	156,189,168	159,356,939

The original “Terms and Conditions” of MERALCO’s Special Stock Subscription Agreement, which required an applicant to subscribe to preferred stock with 10% dividend to cover the cost of extension of new distribution facilities, has been amended by the *Magna Carta* and the Distribution Services and Open Access Rule, or *DSOAR* effective June 17, 2004 and January 18, 2006, respectively. The amendment sets forth the guidelines for the issuance of preferred stock, only if such instrument is available.

17. Customers’ Deposits

This account consists of:

	2013			2012		
	Current Portion (see Note 21)	Noncurrent Portion	Total	Current Portion (see Note 21)	Noncurrent Portion	Total
<i>(Amounts in millions)</i>						
Bill deposits	₱6,125	₱21,330	₱27,455	₱4,057	₱23,144	₱27,201
Meter deposits	2,118	—	2,118	2,187	—	2,187
	₱8,243	₱21,330	₱29,573	₱6,244	₱23,144	₱29,388

Bill Deposits

Bill deposits serve to guarantee payment of bills by a customer in accordance with existing regulations.

As provided for under the *Magna Carta* and *DSOAR*, all captive customers are required to deposit with the *DU* an amount equivalent to the estimated monthly bill calculated based on applied load,



which shall be recognized as bill deposit of the customer. Such deposit shall be adjusted after one year based on the historical 12-month average bill. A customer who has paid his electric bills on or before due date for three consecutive years may now apply for the full refund of the bill deposit, together with the accrued interests, prior to the termination of his service; otherwise bill deposits and accrued interests shall be refunded within one month from the termination of service, provided all bills have been paid.

On February 22, 2010, the amended *DSOAR*, which became effective on April 1, 2010, was promulgated by the *ERC*. Under the amended *DSOAR*, interest on bill deposits for both residential and non-residential customers shall be computed using the equivalent peso savings account interest rate of the Land Bank of the Philippines or *Land Bank*, or other government banks, on the first working day of the year, subject to the confirmation of the *ERC*. Interest rate for bill deposits is 0.5% per annum from January 1, 2011 until December 31, 2012 and 0.375% per annum starting January 1, 2013.

As provided for under *ERC* Resolution No. 1, *A Resolution Adopting the Revised Rules for the Issuance of Licenses to Retail Electricity Suppliers*, a local *RES* may secure security deposits from its customers, which shall earn interest equivalent to the actual interest earnings of the total amount of deposits received from the customers.

The following are the movements of the bill deposits:

	2013	2012
	<i>(Amounts in millions)</i>	
Balance at beginning of year	₱27,201	₱26,271
Additions	4,731	3,188
Refunds	(4,477)	(2,258)
Balance at end of year	27,455	27,201
Less portion maturing within one year	6,125	4,057
Long-term portion of bill deposits and interests	₱21,330	₱23,144

Meter Deposits

Meter deposits were intended to guarantee the cost of meters installed.

The *Magna Carta* for residential customers (effective June 17, 2004) and *DSOAR* (effective January 18, 2006) for non-residential customers exempt all customer groups from payment of meter deposits beginning July 2004 for residential customers and April 2006 for non-residential customers.

The *ERC* released Resolution No. 8, Series of 2008, otherwise known as “Rules to Govern the Refund of Meter Deposits to Residential and Non-Residential Customers,” or *Rules*, which required the refund of meter deposits from the effectivity of the said *Rules* on July 5, 2008. Under the *Rules*, a customer has the option of receiving his refund in cash, credit to future monthly billings, or as an offset to other due and demandable claims of the *DU* against him.

The total amount of refund shall be equivalent to the meter deposit paid by the customer plus the total accrued interest earned from the time the customer paid the meter deposit until the day prior to the start of refund.



On August 8, 2008, in compliance with the *Rules*, *MERALCO* submitted to the *ERC* an accounting of the total meter deposit principal amount for refund. The actual refund of meter deposits commenced on November 3, 2008.

As at December 31, 2013 and 2012, total meter deposits refunded by *MERALCO* amounted to ₱977 million (inclusive of ₱503 million interest) and ₱908 million (inclusive of ₱466 million interest), respectively.

18. Provisions

Provisions consist of amounts recognized for probable costs, charges and expenses relating to claims against *MERALCO*, among others. The movements of provisions follow:

	2013	2012
	<i>(Amounts in millions)</i>	
Balance at beginning of year	₱19,411	₱16,919
Provisions	5,331	2,770
Settlements	(13)	(278)
Balance at end of year	₱24,729	₱19,411

The balance of provisions substantially represents the amount of claims related to a commercial contact, which remains unresolved and local taxes being contested as discussed in Note 28 to the parent company financial statements, consistent with the limited disclosure allowed in *PFRS*.

See Note 28 – *Contingencies and Legal Proceedings*.

19. Customers' Refund

This account represents the balance of the refund related to the *SC* decision promulgated on April 30, 2003, which has not yet been claimed by the customers.

In June 2003, the *ERC*, in the implementation of the *SC* decision, ordered *MERALCO* to refund to its customers an equivalent ₱0.167 per *kWh* for billings made from February 1994 to April 2003.

On February 7, 2011, the *ERC* approved *MERALCO*'s proposal for the extension of the *SC* refund process for five years up to December 31, 2015, in view of difficulties encountered by the customers in meeting the necessary documentation requirements to claim a refund and by *MERALCO* in contacting or locating customers entitled to the refund.

20. Notes Payable

Notes payable represent unsecured interest-bearing working capital peso loans obtained from various local banks. Annual interest rates ranged from 1.5% to 3.9% in 2013 and 3.9% to 6.5% in 2012 on peso-denominated loans.



Interest expense on notes payable amounted to ₱71 million and ₱3 million for the year ended December 31, 2013 and 2012, respectively.

See Note 24 – *Expenses and Income*.

21. Trade Payables and Other Current Liabilities

This account consists of the following:

	<i>Note</i>	2013	2012
		<i>(Amounts in millions)</i>	
Trade accounts payable	22 and 23	₱42,824	₱22,913
Output VAT - net		5,393	4,472
Accrued expenses:			
Employee benefits		3,621	2,595
Taxes		1,779	2,574
Interest		265	284
Others		876	741
Current portions of:			
Bill deposits and related interests	17	6,125	4,057
Meter deposits and related interests	17	2,118	2,187
Other liabilities		778	819
Refundable service extension costs		1,615	1,512
Dividends payable on:			
Redeemable preferred stock	15	250	256
Common stock	14	77	1,023
Universal charges payable		1,523	313
Refundable transmission charges		779	180
Regulatory fees payable		204	203
Other current liabilities		2,844	1,509
		₱71,071	₱45,638

Trade Accounts Payable

Trade accounts payable mainly represent obligations to power suppliers, namely, NPC/ Power Sector Assets and Liabilities Management Corporation or *PSALM*, power generating companies, National Grid Corporation of the Philippines or *NGCP*, and Philippine Electricity Market Corporation or *PEMC*, for costs of power purchased. In addition, this account includes liabilities due to local and foreign suppliers for purchase of goods and services, which consist of transformers, poles, materials and supplies, and contracted services.

Trade payables are noninterest-bearing and are generally settled within the 15 to 30-day trade term. Other payables are noninterest-bearing and are due in no more than six months from incurrence.

See Note 22 – *Related Party Transactions* and Note 29 – *Significant Contracts and Commitments*.



Refundable Service Extension Costs

Article 14 of the *Magna Carta*, specifically, “Right to Extension of Lines and Facilities,” requires a customer requesting for an extension of lines and facilities beyond 30-meter service distance from the nearest voltage facilities of the *DU* to advance the cost of the project. The amended *DSOAR*, which became effective April 1, 2010, requires such advances from customers to be refunded at the rate of 75% of the distribution revenue generated from the extension lines and facilities until such amounts are fully refunded. The related asset forms part of the rate base only at the time a refund has been paid out. Customer advances are noninterest-bearing.

As at December 31, 2013 and 2012, the noncurrent portion of refundable service extension costs of ₱5,782 million and ₱4,357 million, respectively, is presented as “Refundable Service Extension Costs - net of current portion” account in the parent company statements of financial position.

22. Related Party Transactions

The following summarizes the total amount of transactions, which have been provided and/or contracted by *MERALCO* to/with related parties for the relevant financial year. The outstanding balances are unsecured, non-interest bearing and are to be settled in cash.

Pole Attachment Contract with Philippine Long Distance Telephone Company or PLDT

MERALCO has a Pole Attachment Contract with *PLDT* similar to third party pole attachment contracts of *MERALCO* with other telecommunication companies. Under the Pole Attachment Contract, *PLDT* shall use the contacted cable position exclusively for its telecommunication cable network facilities.

Sale of Electricity under Various Service Contracts

MERALCO sells electricity to related party shareholder groups such as *PLDT*, *Metro Pacific*, *JG Summit*, and *SMC* and their respective subsidiaries, and affiliates for the latter's facilities within *MERALCO*'s franchise area. The rates charged to related parties are the same *ERC*-mandated rates applicable to customers within the franchise area.

Purchase of Telecommunication Services from PLDT and Subsidiaries

MERALCO's primary telecommunications carriers are *PLDT* for its wireline and *SMART* for its wireless services. *MERALCO* also purchases its wireline services from Digitel Mobile Philippines, Inc., a subsidiary of *PLDT*. Such services are covered by standard service contracts between the telecommunications carriers and *MERALCO*.

Purchase of Goods and Services

In the ordinary course of business, *MERALCO* purchases goods and services from its affiliates and sells power to such affiliates.



Following is the summary of related party transactions for the years ended December 31, 2013 and 2012 and the outstanding balances as at December 31, 2013 and 2012:

Category	Relationship	Amount of Transactions				Outstanding Receivable (Liability) as at December 31		Terms	Conditions
		2013	2012	2013	2012				
		(Amounts in millions)							
Sale of electricity									
PLDT Group	Stockholder	₱2,599	₱2,936	₱160	₱268	10-day; noninterest-bearing		Unsecured, no impairment	
JG Summit	Stockholder	348*	—	293	—	10-day; noninterest-bearing		Unsecured, no impairment	
SMC Group	Stockholder	851	1,040	59	83	10-day; noninterest-bearing		Unsecured, no impairment	
Metro Pacific Group	Stockholder	352	1,172	15	54	10-day; noninterest-bearing		Unsecured, no impairment	
RSIC	Subsidiary	292	85	—	—	30-day; noninterest-bearing		Unsecured	
Purchase of contracted services:									
Miescor	Subsidiary	349	269	—	(3)	30-day; noninterest-bearing		Unsecured	
MBI	Subsidiary	486	426	(10)	(13)	30-day; noninterest-bearing		Unsecured	
MLI	Subsidiary	504	277	(3)	(9)	30-day; noninterest-bearing		Unsecured	
Purchases of IT services - Indra Philippines	Joint Venture	484	423	(2)	(20)	30-day; noninterest-bearing		Unsecured	
Purchases of meters and devices - GEPMICI	Associate	290	248	—	—	30-day; noninterest-bearing		Unsecured	
Revenue from pole attachment - PLDT	Stockholder	215	206	—	—	Advance payment		Unsecured, no impairment	
Purchases of wireline and wireless services - PLDT Group	Stockholder	50	47	—	—	30-day; noninterest-bearing		Unsecured	
Purchases of power									
South Premiere Power Corporation or SPPC	Affiliate	34,885	—	(2,893)	—	30-day; noninterest-bearing		Unsecured	
San Miguel Energy Corporation or SMEC	Affiliate	13,648	—	(951)	—	30-day; noninterest-bearing		Unsecured	

* Represents sale of electricity for the month of December 2013.

Transaction with MERALCO Pension Fund

MERALCO Pension Fund holds 6,000 common shares of *RP Energy* at ₱100 par value per share, with total carrying amount of ₱600,000 or an equivalent 3% equity interest in *RP Energy*. The fair value of *RP Energy*'s common shares cannot be reliably measured as these are not traded in the financial market. As at December 31, 2013, the fair value of the total assets being managed by MERALCO Pension Fund amounted to ₱34.0 billion.

See Note 25 – Long-Term Employee Benefits.

Compensation of Key Management Personnel

The compensation of key management personnel of MERALCO by benefit type is as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Short-term employee benefits	₱517	₱432
Long-term employee and retirement benefits	283	256
Share-based payments	—	31
	₱800	₱719



Each of the directors is entitled to a per diem of ₱120,000 for every *BOD* meeting attended. Each member or advisor of the Audit and Risk Management, Remuneration and Leadership Development, Finance, Governance and Nomination Committees is entitled to a fee of ₱20,000 for every committee meeting attended.

On March 22, 2013, the *BOD* approved the amendment of *MERALCO's* By-Laws which entitles all directors to a reasonable per diems for their attendance in meetings of the *BOD* and Board Committees plus an additional compensation, provided, that the total value of such additional compensation, in whatever form so given, shall not exceed one percent of the net income before tax of *MERALCO* during the preceding year.

Consistent with the foregoing, the *BOD* approved the increase in the compensation of all members of the *BOD* up to a maximum of pre-agreed amount per annum. The increase in compensation shall be through a stock grant based on a pre-approved number of shares for each director. The implementation of the foregoing was approved by the stockholders in the annual general meeting on May 28, 2013.

There are no agreements between *MERALCO* and any of its key management personnel providing for benefits upon termination of employment or retirement, except with respect to benefits provided under the retirement and pension plans. The Pension Plan covers employees hired up to December 31, 2003 only. The Provident Plan, which is implemented on a voluntary basis, covers employees hired beginning January 1, 2004.

23. Revenues and Purchased Power

Sale of Electricity

Following is the breakdown of electricity revenues:

	2013	2012
	<i>(Amount in millions)</i>	
Generation charge	₱190,700	₱182,313
Transmission charge	28,865	31,679
System loss charge	17,026	16,353
Power Act Reduction adjustment	(8)	(24)
Interclass, lifeline subsidies and others	(128)	23
Distribution service charges	55,796	50,633
	₱292,251	₱280,977

Distribution revenue accounted for 19% and 18% of total electricity revenues in 2013 and 2012, respectively. *VAT*, *LFT* and universal charges, which are also pass-through charges are billed and collected on behalf of the national and local governments and do not form part of total electricity revenues.



Purchased Power

The details of purchased power are as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
Generation charge	₱204,620	₱197,202
Transmission charge	31,300	33,120
	₱235,920	₱230,322

Purchased power costs are pass-through costs and revenue-neutral to *MERALCO*, as a *DU*.

Generation charge is inclusive of line rentals, market fees and must-run unit charges billed by *PEMC*.

Purchased power includes capacity fees, fixed operating fees and transmission line fees that are accounted for similar to a lease under Philippine Interpretation *IFRIC 4*, “*Determining whether an arrangement contains a lease*”. The total amounts billed by the suppliers presented as part of “Purchased power” account in the parent company statements of income are ₱46,170 million and ₱18,496 million for year ended December 31, 2013 and 2012, respectively. This also includes the actual *SL* incurred but no more than 8.5%. *MERALCO*’s actual *SL* rates are 6.92% and 7.04% in 2013 and 2012, respectively.

The details of purchased power are as follows:

	2013	2012
	<i>(Amounts in millions)</i>	
First Gas Power Corporation or <i>FGPC</i> and FGP Corp. or <i>FGP</i>	₱55,360	₱58,592
<i>PEMC</i> /Wholesale Electricity Spot Market or <i>WESM</i>	40,559	28,401
<i>SPPC</i>	34,885	—
<i>TransCo</i> / <i>NGCP</i>	31,274	33,120
<i>QPPL</i>	14,251	15,147
Masinloc Power Partners Co. Ltd. or <i>MPPCL</i>	12,905	—
<i>NPC/PSALM</i> (including <i>NPC</i> Successor Generating Companies or <i>SGCs/IPPAs</i>)	12,075	94,930
<i>SMEC</i>	11,749	—
Sem-Calaca Power Corporation or <i>Sem-Calaca</i>	10,673	—
Therma Luzon, Inc. or <i>TLI</i>	9,538	—
Others	2,651	132
	₱235,920	₱230,322

Generation and transmission cost over/under-recoveries occur as a result of the lag in the billing and recovery of generation and transmission costs from consumers. As at December 31, 2013 and 2012, the total transmission cost over-recoveries included in “Other noncurrent liabilities” account in the parent company statements of financial position amounted to ₱6,358 million and ₱5,288 million, respectively.



24. Expenses and Income

Salaries, Wages and Employee Benefits

	Note	2013	2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Salaries, wages and related employee benefits		₱7,844	₱8,471
Pension expense	25	1,147	1,349
Other long-term post-employment benefits expense	25	258	261
ESPP	15	—	134
		₱9,249	₱10,215

Other Expenses

	Note	2013	2012
<i>(Amounts in millions)</i>			
Rent and utilities		₱472	₱446
Advertising expense		291	170
Insurance		290	227
Inventories		288	239
Transportation and travel		241	249
Corporate expenses		131	1,158
Communication expense	22	60	51
Others		521	366
		₱2,294	₱2,906

Interest and Other Financial Charges

	Note	2013	2012
<i>(Amounts in millions)</i>			
Interest expense on interest-bearing long-term financial liabilities, net of interest capitalized	6 and 16	₱966	₱1,197
Carrying charge on ERC-approved over-recoveries	2	112	79
Interest expense on bill deposits	17	81	90
Interest expense on notes payable	20	71	3
Amortization of debt issuance costs	16	61	37
Interest expense on meter deposits	17	2	1
Others		181	111
		₱1,474	₱1,518



Interest and Other Financial Income

	<i>Note</i>	2013	2012
<i>(Amounts in millions)</i>			
Interest income on cash and cash equivalents		₱1,047	₱1,728
Dividend income		491	58
Carrying costs on <i>ERC</i> -approved under-recoveries	2	–	755
Others		35	6
		₱1,573	₱2,547

25. Long-term Employee Benefits

Liabilities for long-term employee benefits consist of the following:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Long-term incentives	₱1,205	₱2,640	₱1,680
Pension liability	1,113	3,186	5,870
Other long-term post-employment benefits	1,792	2,962	2,966
	₱4,110	₱8,788	₱10,516

Retirement Plan

Actuarial valuation is prepared annually by an independent actuary engaged by *MERALCO*.

Net Pension Costs (included in “Salaries, wages and employee benefits” account)

	2013	2012 (As restated - see Note 4)	2011 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Current service costs	₱1,039	₱1,037	₱1,090
Net interest costs	103	309	453
Net pension costs	₱1,142	₱1,346	₱1,543

Pension Liability

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Defined benefit obligation	₱35,098	₱33,713	₱33,148
Fair value of plan assets	(33,985)	(30,527)	(27,278)
Pension liability	₱1,113	₱3,186	₱5,870



Changes in the net pension liability are as follows:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Pension liability at beginning of year	₱3,186	₱5,870	₱9,709
Net pension costs	1,142	1,346	1,543
Total amounts recognized in <i>OCI</i>	(282)	(2,591)	(1,053)
Contributions by employer	(2,933)	(1,439)	(4,329)
Pension liability	₱1,113	₱3,186	₱5,870

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

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Defined benefit obligation at beginning of year	₱33,713	₱33,148	₱32,483
Interest costs	1,971	1,942	1,899
Benefits paid	(1,693)	(1,567)	(1,689)
Current service costs	1,039	1,037	1,090
Actuarial losses (gains) due to changes in assumptions	68	(847)	(635)
Defined benefit obligation at end of year	₱35,098	₱33,713	₱33,148

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

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
<i>(Amounts in millions)</i>			
Fair value of plan assets at beginning of year	₱30,527	₱27,278	₱22,774
Return on plan assets, excluding amount included in net interest on the net defined obligation	350	1,744	418
Interest income	1,868	1,633	1,446
Benefits paid	(1,693)	(1,567)	(1,689)
Contributions by employer	2,933	1,439	4,329
Fair value of plan assets at end of year	₱33,985	₱30,527	₱27,278



The Board of Trustees or *BOT*, which manages the retirement benefit fund, is chaired by the chairman of *MERALCO*, who is neither an executive nor a beneficiary. The other members of the *BOT* are (i) an executive member of the *BOD*; (ii) two (2) senior executives; (iii) an independent member of the *BOD*; (iv) a member of the *BOD* who represents the largest shareholder group and (v) a non-executive, non-*BOD* member who represents another shareholder group, all of whom are non-beneficiaries of the Plan.

The Fund follows a generally conservative investment approach where investments are diversified to minimize risks but ensures an increase in value of the Fund assets. Substantially all of the funds of the Plan are managed by four (4) trustee banks whose common objective is to maximize the long-term expected return of plan assets. As approved by the *BOT*, the funds are invested in a guided proportion of fixed income instruments, cash investments and equities.

The major categories of plan assets of the *MERALCO* Pension Fund as a percentage of the fair value of total plan are as follows:

	2013	2012
	<i>(Amount in millions)</i>	
Cash and cash equivalents	₱5,637	₱3,100
Investments quoted in active markets		
Quoted equity investments:		
Holding firms	1,950	2,247
Electricity, energy, power and water	1,155	1,480
Food, beverages and tobacco	908	884
Banks	713	839
Property	608	660
Telecommunication	607	295
Transportation services	283	230
Construction, infrastructure and allied services	82	158
Financial institution	81	102
Gaming	75	130
Mining	66	245
Retail	44	92
Media	31	43
Hotel and leisure	15	—
Others	325	385
Quoted debt instruments:		
Government securities	11,385	10,587
“AAA” rated securities	7,399	6,256
Unquoted investments:		
Receivables	1,667	1,962
Property	954	832
Fair value of plan assets	₱33,985	₱30,527



Marketable equity securities, government securities, bonds and commercial notes are investments held by the trustee banks. The Fund does not have any direct equity interests in *MERALCO*.

Other Long-term Post-employment Benefits Expense (included in "Salaries, wages and employee benefits" account)

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
	<i>(Amounts in millions)</i>		
Interest costs	₱178	₱176	₱54
Current service costs	80	85	156
	₱258	₱261	₱210

Changes in the present value of other long-term post-employment benefits liability are as follows:

	December 31, 2013	December 31, 2012 (As restated - see Note 4)	January 1, 2012 (As restated - see Note 4)
	<i>(Amounts in millions)</i>		
Balance at beginning of year	₱2,962	₱2,966	₱2,471
Interest costs	178	176	54
Current service costs	80	85	156
Benefits paid	(53)	(73)	(75)
Actuarial losses (gains) due to change in assumptions	(1,375)	(192)	360
Balance at end of year	₱1,792	₱2,962	₱2,966

Actuarial Assumptions

The principal assumptions used as at December 31, 2013 and 2012 in determining pension and other long-term post-employment benefits obligations are shown below:

	2013	2012
Annual discount rate	4.5%	6%
Future range of annual salary increases	6%-10%	6%-8%



Sensitivity Analysis

The calculation of the defined benefit obligation is sensitive to the assumptions set above. The following table summarizes how the impact on the defined benefit obligation at the end of the reporting year would have increased (decreased) as a result of a change in the respective assumptions by:

		Effect on Present Value of Defined Benefit Obligation	
	% Change	2013	2012
(Amounts in millions)			
Annual discount rate	+1.0%	(P2,144)	(P1,107)
	-1.0%	4,445	1,107
Future range of annual salary increases	+1.0%	1,072	1,161

Funding

MERALCO shall contribute to the Fund from time to time such amounts of money under accepted actuarial principles to maintain the Fund in a sound condition, subject to the provisions of the Plan.

The amount of the annual contributions to the Fund is determined through an annual valuation report performed by the actuary.

MERALCO expects to contribute P1,690 million to its defined benefit pension plan in 2014.

The following is the maturity profile of the undiscounted benefit payments:

	<i>(Amounts in millions)</i>
Less than one year	P1,400
More than one year to five years	6,838
More than five years to 10 years	7,091
More than 10 years to 15 years	7,714
More than 15 years to 20 years	7,632
More than 20 years	19,312

Risk

The Fund is exposed to the following risks:

Credit Risk

The Fund's exposure to credit risk arises from its financial assets which comprise cash and cash equivalents, investments and rental receivable. The credit risk results from the possible default of the issuer of the financial instrument, with a maximum exposure equivalent to the carrying amount of the instruments.

The credit risk is minimized by ensuring that the exposure to the various chosen financial investment structures is limited primarily to government securities and bonds or notes duly recommended by the Trust Committees of the Fund of the appointed fund managers.



Share Price Risk

The Fund's exposure to share price risk arises from shares of stock it holds and being traded at the PSE. The price risk emanates from the volatility of the stock market. The policy is to limit investment in shares of stock to blue chip issues or issues with good fair values or those trading at a discount to its net asset value so that in the event that market falls drastically, the Fund may still consider hold on to such investments until the market recovers.

By having a balanced composition of holdings in the equities portfolio, exposure to industry or sector-related risks is reduced. The mix of various equities in the portfolio reduces volatility and contributes to a more stable return over time. Equity investments are made within the parameters of the investment guidelines approved by the BOT. The BOT of the Fund meets periodically to review the investment portfolio based on financial market conditions. Share prices are also monitored regularly.

Liquidity Risk

Liquidity risk is the risk that the Pension Fund is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. Liquidity risk is being managed to ensure that adequate fixed income and cash deposits are available to service the financial obligations of the Fund. The schedule of the maturities of fixed income investment assets are staggered by tenure or term. Policies are established to ensure that all financial obligations are met, wherein the timing of the maturities of fixed income investments are planned and matched to the due date of various obligations. Thus, for this investment class, maturities are classified into short-term, medium-term and long-term. A certain percentage of the portfolio is left in cash to manage liquidity and settle all currently maturing financial obligations.

MERALCO Defined Contribution Provident Plan

MERALCO has a contributory Provident Plan effective January 1, 2009, intended to be a Supplemental Retirement Benefit for employees hired after 2004, on a voluntary basis. Each qualified employee-member who opts to participate in the plan shall have the option to contribute up to a maximum of 25% of his base salary. MERALCO shall match the member's contribution up to the first 10% of the member's base salary. Upon resignation, the member shall be entitled to the total amount credited to his personal retirement account immediately preceding his actual retirement date, subject to provisions of the Provident Plan. MERALCO's contribution to the Provident Plan amounted to ₱5 million and ₱3 million for the years ended December 31, 2013 and 2012, respectively.

Pension Expense (included in "Salaries, wages and employee benefits" account)

	2013	2012 (As restated - see Note 4)
	<i>(Amounts in millions)</i>	
Expense recognized for defined benefit plans	₱1,142	₱1,346
Expense recognized for defined contribution plan	5	3
Pension expense	₱1,147	₱1,349



Long-term Incentive Plan or LTIP

MERALCO's LTIP covers qualified executives and based on MERALCO's achievement of specified level of consolidated core net income approved by the BOD and determined on an aggregate basis for a three year period as well as executives' attainment of a minimum level of performance rating. Executives invited to the plan must serve a minimum uninterrupted period to be entitled to any pay-out.

26. Financial Assets and Financial Liabilities

Financial assets consist of cash and cash equivalents and trade and nontrade receivables, which are generated directly from operations. The principal financial liabilities, other than derivatives, consist of bank loans, redeemable preferred shares, trade and non-trade payables, which are incurred to finance operations in the normal course of business.

The following table sets forth the financial assets and financial liabilities as at December 31, 2013 and 2012:

	Loans and Receivables	Held-to-Maturity Investments	Fair Value through Profit or Loss	Available- for-sale Financial Assets	Liabilities Carried at Amortized Cost	Total Financial Assets and Liabilities
<i>(Amounts in millions)</i>						
Assets as at December 31, 2013						
<i>Noncurrent</i>						
Other noncurrent assets	P474	P-	P-	P124	P-	P598
<i>Current</i>						
Cash and cash equivalents	57,607	-	-	-	-	57,607
Trade and other receivables	25,372	-	-	-	-	25,372
Short-term investments	4,841	-	-	-	-	4,841
Total assets	88,294	-	-	124	-	88,418
Liabilities as at December 31, 2013						
<i>Noncurrent</i>						
Interest-bearing long-term financial liabilities - net of current portion	-	-	-	-	20,756	20,756
Customers' deposits - net of current portion	-	-	-	-	21,330	21,330
Refundable service extension costs - net of current portion	-	-	-	-	5,782	5,782
<i>Current</i>						
Notes payable	-	-	-	-	1,700	1,700
Trade payables and other current liabilities	-	-	-	-	55,814	55,814
Customers' refund	-	-	-	-	6,013	6,013
Interest-bearing long-term financial liabilities - current portion	-	-	-	-	11,021	11,021
Total liabilities	-	-	-	-	122,416	122,416
Net Assets (Liabilities)	P88,294	P-	P-	P124	(P122,416)	(P33,998)
Assets as at December 31, 2012						
<i>Noncurrent</i>						
Other noncurrent assets	P325	P-	P-	P299	P-	P624
<i>Current</i>						
Cash and cash equivalents	58,592	-	-	-	-	58,592
Trade and other receivables	21,416	-	-	-	-	21,416
Derivative assets	-	-	24	-	-	24
Total assets	80,333	-	24	299	-	80,656
Liabilities as at December 31, 2012						
<i>Noncurrent</i>						
Interest-bearing long-term financial liabilities - net of current portion	-	-	-	-	20,466	20,466
Customers' deposits - net of current portion	-	-	-	-	23,144	23,144
Refundable service extension costs - net of current portion	-	-	-	-	4,357	4,357
<i>Current</i>						
Notes payable	-	-	-	-	1,700	1,700
Trade payables and other current liabilities	-	-	-	-	32,928	32,928
Customers' refund	-	-	-	-	6,127	6,127
Interest-bearing long-term financial liabilities - current portion	-	-	-	-	2,360	2,360
Total liabilities	-	-	-	-	91,082	91,082
Net Assets (Liabilities)	P80,333	P-	P24	P299	P91,082	(P10,426)



Fair Values

The fair values of the financial assets and financial liabilities are prices that would be received to sell the financial assets or paid to transfer the financial liabilities in orderly transactions between market participants at the measurement date. Set out below is a comparison of carrying amounts and fair values of *MERALCO Group's* financial instruments as at December 31, 2013 and 2012.

	2013		2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<i>(Amounts in millions)</i>				
Financial assets				
Loans and receivables -				
Advances to a supplier	₱474	₱552	₱325	₱409
Fair value through profit or loss -				
Derivative asset	—	—	24	24
Available-for-sale financial assets	161	161	331	331
	₱635	₱713	₱680	₱764
Financial liabilities				
Financial liabilities carried at amortized cost -				
Interest-bearing long-term financial liabilities	₱31,777	₱32,176	₱22,826	₱24,787

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate such value:

Cash and Cash Equivalents, Trade and Other Receivables, Short-term Investments, Trade Payables and Other Current Liabilities and Note Payable

Due to the short-term nature of transactions, the fair values of these instruments approximate their carrying amounts as at reporting date.

Advances to a Supplier

The fair values of advances to a supplier and held-to-maturity investments were computed by discounting the instruments' expected future cash flows using the rates of 3.76% as at December 31, 2013 and 4.16% as of December 31, 2012.

Bifurcated Foreign Currency Forward and Foreign Currency Forward

The fair values of embedded currency forwards and freestanding currency forwards were calculated by reference to forward exchange market rates.

AFS Investments

The fair values were determined by reference to market bid quotes as at reporting date. The unquoted equity securities were carried at cost.

Meter Deposits and Customers' Refund

Meter deposits and customers' refund are due and demandable. Thus, the fair values of these instruments approximate their carrying amounts.



Bill Deposits

The carrying amount of bill deposits approximates their fair values as bill deposits are interest-bearing.

Interest-bearing Long-term Financial Liabilities

The fair values of interest-bearing long-term debt (except for redeemable preferred stock) were computed by discounting the instruments' expected future cash flows using the rates ranging from 0.52% to 4.29% as at December 31, 2013 and 1.65% to 4.49% as at December 31, 2012.

Redeemable Preferred Stock

The carrying amount of the preferred stock represents the fair value. Such preferred shares have been called and are payable anytime upon presentation by such shareholder of their certification. This is included under "Interest-bearing long-term financial liabilities" account.

Refundable Service Extension Costs

The fair values of refundable service extension costs cannot be reliably measured since the timing of related cash flows cannot be reasonably estimated and are accordingly measured at cost.

Fair Value Hierarchy

MERALCO uses the following hierarchy in determining and disclosing the fair value of financial instruments by inputs to the valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities
- Level 2: other techniques where all inputs have significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques where inputs have significant effect on the recorded fair value that are not based on observable market data

Below is the list of financial assets and financial liabilities that are classified using the fair value hierarchy:

	2013				2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
<i>(Amounts in millions)</i>								
Financial assets								
Advances to a supplier	P-	P-	P552	P552	P-	P-	P409	P409
AFS investments	124	-	37	161	128	-	203	331
Derivative assets	-	-	-	-	-	24	-	24
	P124	P-	P589	P713	P128	P24	P612	P764
Financial liabilities								
Interest-bearing long-term financial liabilities	P-	P-	P32,176	P32,176	P-	P-	P24,787	P24,787



For the years ended December 31, 2013 and 2012, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

Financial Risk Management Objectives and Policies

The main risks arising from *MERALCO*'s financial instruments are cash flow interest rate risk, foreign currency risk, commodity price risk, credit risk and liquidity risk. The importance of managing those risks has significantly increased in light of the considerable change and volatility in the Philippine and international financial markets. The *BOD* reviews and approves policies for managing each of these risks. Management monitors the market price risk arising from all financial instruments. The policies for managing these risks are as follows:

Interest Rate Risk

MERALCO's exposure to the changes in market interest rates relate primarily to the long-term interest-bearing financial liabilities.

MERALCO's policy is to manage its interest rate risk exposure using a mix of fixed and variable rate debts. The strategy, which yields a reasonably lower effective cost based on market conditions, is adopted. Refinancing of fixed rate loans may also be undertaken to manage interest cost. Approximately 90% and 83% of the borrowings bear fixed rate of interest as at December 31, 2013 and 2012, respectively.

The following table sets out the maturity profile of the financial instruments that are exposed to interest rate risk (exclusive of debt issuance costs):

	Within 1 Year	Over 1–2 Years	Over 2–3 Years	Over 3–4 Years	Over 4–5 Years	More than 5 Years	Total
<i>(Amounts in millions)</i>							
2013	₱612	₱13	₱13	₱12	₱2,425	₱–	₱3,075
2012	613	612	13	13	12	2,425	3,688

Floating interest rate of bank loans is re-priced at intervals of less than one year. The other financial liabilities of *MERALCO* that are not included in the foregoing have fixed interest rate, or are noninterest-bearing or have no fixed or determinable maturity and are, therefore, not subject to interest rate risk. Short-term investments are not exposed to significant changes in market rates because they mature within 90 days to coincide with *MERALCO*'s monthly payment obligations.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of *MERALCO*'s profit before tax as at December 31, 2013 and 2012 through the impact on floating rate borrowings. There is no other impact on *MERALCO*'s equity other than those already affecting the parent company statement of income.

	2013		2012	
	Increase (Decrease) in Basis Points	Effect on Profit before Tax	Increase (Decrease) in Basis Points	Effect on Profit before Tax
<i>(Amounts in millions)</i>				
Floating rate loans from various banks	+100 (100)	(₱31) 31	+100 (100)	(₱37) 37



Interest expense on floating rate loans is computed for the year, taking into account actual principal movements during the year, based on management's best estimate of a +/-100 basis points change in interest rates. There has been no change in the methods and assumptions used by management in the above analysis.

Foreign Currency Risk

The revaluation of *MERALCO*'s foreign currency-denominated financial assets and financial liabilities as a result of the appreciation or depreciation of the Philippine peso is recognized as foreign exchange gains or losses as at the end of each reporting period. The extent of foreign exchange gains or losses is largely dependent on the amount of foreign currency-denominated liabilities. While an insignificant percentage of *MERALCO*'s revenues and liabilities is denominated in U.S. dollars, a substantial portion of *MERALCO*'s capital expenditures for electricity capital project and a portion of the operating expenses are denominated in foreign currencies, mostly in U.S. dollars. As such, a strengthening or weakening of the Philippine peso against the U.S. dollar will decrease or increase in Philippine peso terms, the principal amount of *MERALCO*'s foreign currency-denominated liabilities and the related interest expense, foreign currency-denominated capital expenditures and operating expenses as well as U.S. dollar-denominated revenues.

The following table shows *MERALCO*'s foreign currency-denominated financial assets and financial liabilities as at December 31, 2013 and 2012, translated to Philippine peso using ₱44.395 and ₱41.050 to \$1, respectively.

	2013		2012	
	U.S.Dollar	Peso Equivalent	U.S.Dollar	Peso Equivalent
<i>(Amounts in millions)</i>				
Financial assets:				
Cash and cash equivalents	\$65	₱2,864	\$47	₱1,913
Trade and other receivables	3	148	1	53
Advance payments to a supplier	11	474	8	325
	79	3,486	56	2,291
Financial liabilities -				
Trade payables and other liabilities	(46)	(2,043)	(139)	(5,724)
	\$33	₱1,443	(\$83)	(₱3,433)

All of *MERALCO*'s long-term financial liabilities are denominated in Philippine peso. However, an insignificant portion of its trade payables is denominated in U.S. dollar. Thus, the impact of ₱1 movement of the Philippine Peso against the U.S. dollar will not have a significant impact on *MERALCO*'s principal and interest payments. Further, *PBR* assumes a forecast level of foreign currency movements in its calculation of the regulatory asset base and expenditures. *PBR* also allows for adjustment of the rates *MERALCO* charges should there be significant deviations in the foreign exchange forecast from what is actually realized.



The following table demonstrates the sensitivity to a reasonably possible change in the U.S. dollar exchange rate vis-a-vis the peso, with all other variables held constant, of *MERALCO*'s profit before tax as at December 31, 2013 and 2012 (due to changes in the fair value of financial assets and financial liabilities). There is no other impact on *MERALCO*'s equity other than those already affecting the profit and loss.

	2013		2012	
	Appreciation (Depreciation) of U.S. Dollar	Effect on Income before Income Tax	Appreciation (Depreciation) of U.S. Dollar	Effect on Income before Income Tax
	(In %)	(In millions)	(In %)	(In millions)
U.S. dollar-denominated financial assets	+5	₱73	+5	(₱170)
and financial liabilities	-5	(₱73)	-5	170

Foreign exchange gain or loss is computed for the year based on management's best estimate of a +/-5 percent change in the closing Philippine peso to U.S. dollar conversion rate using the year-end balances of U.S. dollar-denominated cash and cash equivalents, accounts receivable, liabilities and forward contracts. There has been no change in the methods and assumptions used by management in the above analysis.

Commodity Price Risk

Commodity price risk is the risk that the fair value or cash flows of a financial instrument will fluctuate because of changes in commodity prices. *MERALCO*'s exposure to price risk is minimal. The cost of fuel is part of *MERALCO*'s generation costs that are recoverable from the customers through the generation charge in the billings to the customers.

Credit Risk

Credit risk is the risk that *MERALCO* is exposed to as a result of its customers, clients or counterparties failing to discharge their contracted obligations. *MERALCO* manages and controls credit risk by setting limits on the amount of risk that it is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

MERALCO as a franchise holder serving public interest cannot refuse customer connection. To mitigate risk, the *DSOAR* allows *MERALCO* to collect bill deposit equivalent to one month's consumption to secure credit. Also, as a policy, disconnection notices are sent three days after the bill due date and disconnections are carried out beginning on the third day after receipt of disconnection notice.

With respect to placements of cash with financial institutions, these institutions are subject to *MERALCO*'s accreditation evaluation based on liquidity and solvency ratios and on the bank's credit rating. *MERALCO* shall transact only derivatives with similarly accredited financial institutions. In addition, *MERALCO*'s deposit accounts in banks are insured by the Philippine Deposit Insurance Corporation up to ₱500,000 per bank.

Credit risk on other financial assets, which include cash and cash equivalents, trade and other receivables and certain derivative instruments, arises from default of the counterparty.

Finally, credit quality review procedures are in place to provide regular identification of changes in the creditworthiness of counterparties. Counterparty limits are established and reviewed



periodically based on latest available financial information of counterparties, credit ratings and liquidity. *MERALCO*'s credit quality review process allows it to assess any potential loss as a result of the risks to which it may be exposed and to take corrective actions.

There are no significant concentrations of credit risk in *MERALCO*.

The table below shows the maximum exposure to credit risk for the components of the parent company statements of financial position, including derivatives as at December 31, 2013 and 2012. The maximum exposure is equivalent to the nominal amount of the accounts.

	Gross Maximum Exposure	
	2013	2012
	<i>(Amounts in millions)</i>	
Cash and cash equivalents	₱57,472	₱58,585
Trade and other receivables		
Billed electricity	23,867	20,568
Nontrade receivables	1,355	848
Short-term investments	4,841	—
Advance payment to a supplier	474	325
Derivative assets	—	24
	₱88,009	₱80,350

The credit quality of financial assets is managed by *MERALCO* using “High Grade,” “Standard Grade” and “Sub-standard Grade” as internal credit ratings. The following tables show the credit quality by asset class:

2013						
	Neither Past Due nor Impaired			Past Due but not Impaired	Impaired Financial Assets	Total
	High Grade	Standard Grade	Sub-standard Grade			
	(Amounts in millions)					
Cash in banks and cash equivalents	₱57,472	₱—	₱—	₱—	₱—	₱57,472
Trade and other receivables:						
Billed electricity	5,793	3,583	9,046	5,445	2,963	26,830
Nontrade receivables	1,374	8	20	103	—	1,505
Short-term investments	4,841	—	—	—	—	4,841
Advance payment to a supplier	—	—	474	—	—	474
	₱69,480	₱3,591	₱9,540	₱5,548	₱2,963	₱91,122
2012						
	Neither Past Due nor Impaired			Past Due but not Impaired	Impaired Financial Assets	Total
	High Grade	Standard Grade	Sub-standard Grade			
	(Amounts in millions)					
Cash in banks and cash equivalents	₱58,585	₱—	₱—	₱—	₱—	₱58,585
Trade and other receivables:						
Billed electricity	5,747	3,313	8,513	2,995	2,556	23,124
Nontrade receivables	573	31	3	241	—	848
Derivative assets	24	—	—	—	—	24
Advance payment to a supplier	—	—	325	—	—	325
	₱64,929	₱3,344	₱8,841	₱3,236	₱2,556	₱82,906



Credit ratings were determined as follows:

▪ “High Grade”

‘High’ grade financial assets include cash and cash equivalents and derivative assets to counterparties with good credit rating or bank standing. Consequently, credit risk is minimal. These counterparties include large prime financial institutions, large industrial companies and commercial establishments, and government agencies. For trade receivables, these consist of current month’s billings (less than 30 days) that are expected to be collected within 10 days from the time bills are delivered.

▪ “Standard Grade”

‘Standard’ grade financial assets include trade receivables consisting of current month’s billings (less than 30 days) that are expected to be collected before due date (10 to 14 days after bill date).

“Sub-standard Grade”

‘Sub-standard’ grade financial assets include trade receivables that consist of current month’s billing, which are not expected to be collected within 60 days.

The following table shows the aging analysis of financial assets as at December 31, 2013 and 2012:

2012.

	2013						
	Neither Past	Past Due but not Impaired				Impaired	
	Due nor			Over	Financial		
	Impaired	31-60 Days	61-90 Days	90 Days	Assets	Total	



Liquidity Risk

Liquidity risk is the risk that *MERALCO* will be unable to meet its payment obligations when they fall due. *MERALCO* manages this risk through monitoring of cash flows in consideration of future payment of obligation and collection of its trade receivables. *MERALCO* also ensures that there are sufficient, available and approved working capital lines that it can draw from at any time.

MERALCO maintains an adequate amount of cash and cash placements, which may be readily converted to cash in any unforeseen interruption of its cash collections. *MERALCO* also maintains accounts with several relationship banks to avoid significant concentration of cash with one institution.

The maturity profile of bill deposits is not determinable since the timing of each refund is linked to the cessation of service, which is not reasonably predictable. However, *MERALCO* estimates that a portion of bill deposits (including related interest), amounting to ₱6,125 million, will be refunded within the year. This is shown as part of “Trade payables and other current liabilities” account in the parent company statement of financial position as at December 31, 2013.

Capital Management

The primary objective of *MERALCO*’s capital management is to enhance shareholder value. The capital structure is reviewed with the end view of achieving a competitive cost of capital and at the same time ensuring that returns on, and of, capital are consistent with the levels approved by its regulators for its core distribution business.

The capital structure optimization plan is complemented by efforts to improve capital efficiency to increase yields on invested capital. This entails efforts to improve the efficiency of capital assets, working capital and non-core assets.

MERALCO monitors capital using debt to equity ratio, which is consolidated gross debt divided by consolidated equity attributable equity holders of the parent. *MERALCO* considers long-term debt, redeemable preferred stock and note payable as debt.

	2013	2012
<i>(Amounts in millions, except debt to equity ratio)</i>		
Long-term debt	₱30,215	₱21,232
Redeemable preferred stock	1,562	1,594
Notes payable	1,814	1,787
Debt (a)	33,591	24,613
Equity attributable to the holders of the parent (b)	75,162	67,902
Debt to equity ratio (a)/(b)	0.45	0.36



27. Income Taxes and Local Franchise Taxes

Income Taxes

The components of net deferred tax assets as at December 31, 2013 and 2012 are as follows:

		2013	2012 (As restated - see Note 4)
	<i>Note</i>		
<i>(Amounts in millions)</i>			
Deferred tax assets:			
Provisions for various claims	18	₱12,681	₱9,502
Accrued employee benefits		899	1,007
Allowance for doubtful accounts	11	889	767
Unfunded pension cost and unamortized past service cost		478	1,577
Allowance for excess of cost over net realizable value of inventories	12	61	62
Others		356	392
		15,364	13,307
Deferred tax liabilities:			
Revaluation increment in utility plant and others	14	7,389	7,645
Depreciation method differential		1,082	1,124
Capitalized interest		744	751
Capitalized duties and taxes deducted in advance		651	655
Net book value of capitalized/ realized foreign exchange losses		22	37
Others		123	76
		10,011	10,288
		₱5,353	₱3,019

Provision for income tax consists of:

	2013	2012 (As restated - see Note 4)
Current	₱9,690	₱9,346
Deferred	(2,828)	(3,747)
	₱6,862	₱5,599



A reconciliation between the provision for (benefit from) income tax computed at statutory income tax rate of 30% for the years ended December 31, 2013 and 2012, and provision for (benefit from) income tax as shown in the parent company statements of income is as follows:

	2013	2012 (As restated - see Note 4)
	<i>(Amounts in millions)</i>	
Income tax computed at statutory tax rate	₱7,305	₱7,738
Income tax effects of:		
Interest income subjected to lower final tax rate	(314)	(519)
Nondeductible interest expense	130	213
Nontaxable income	(97)	(1,872)
Nondeductible expenses	30	39
Others	(192)	—
	₱6,862	₱5,599

On December 18, 2009, the *BIR* issued Revenue Regulation or *RR* No. 16-2008, which implemented the provisions of *RA* No. 9504 on Optional Standard Deductions, or *OSD*. Such regulation allows both individual and corporate taxpayers to use *OSD* in computing their taxable income. For corporations, they may elect to adopt standard deduction in an amount not exceeding 40% of gross income in lieu of the allowed itemized deductions. *MERALCO* has not availed of the *OSD* in computing its taxable income for the years ended December 31, 2013 and 2012.

LFT

Consistent with the decisions of the *ERC*, *LFT* is a recoverable charge of the *DU* in the particular province or city imposing and collecting the *LFT*. It is presented as a separate line item in the customers' bill and computed as a percentage of the sum of generation, transmission, distribution services and related system loss charges.

Furthermore, the Implementing Rules and Regulations issued by the *ERC* provide that local franchise taxes shall be paid only on its distribution wheeling and captive market supply revenues. At present, pending the promulgation of guidelines from the relevant government agencies, *MERALCO* is paying *LFT* based on the sum of the charges in the customers' bill.

28. Contingencies and Legal Proceedings

Overpayment of Income Tax related to SC Refund

With the decision of the *SC* for *MERALCO* to refund ₱0.167 per *kWh* to cover customers during the billing period February 1994 to May 2003, *MERALCO* overpaid income tax in the amount of ₱7,107 million for taxable years 1994 to 1998 and 2000 to 2001. Accordingly, *MERALCO* filed a claim on November 27, 2003 for the recovery of such excess income taxes paid. After examination of the books of *MERALCO* for the covered periods, the *BIR* determined that *MERALCO* had in fact overpaid income taxes in the amount of ₱6,690 million. However, the *BIR* also maintained that *MERALCO* is entitled to a refund amount of only ₱894 million, which pertains to taxable year 2001, claiming that the period for filing a claim had prescribed in respect of the difference between *MERALCO*'s overpayment and the refund amount *MERALCO* is entitled to.



The *BIR* then approved the refund of ₱894 million for issuance of tax credit certificates or *TCCs*, proportionate to the actual refund of claims to utility customers. The *BIR* initially issued *TCCs* amounting to ₱317 million corresponding to actual refund to customers as at August 31, 2005.

As at December 31, 2013 and 2012, the amount of unissued *TCCs* amounting to ₱577 million refund entitlement is presented as part of “Other noncurrent assets” account in the parent company statements of financial position.

See *Note 9 – Other Noncurrent Assets*.

MERALCO filed a Petition with the Court of Tax Appeals or *CTA* assailing the denial by the *BIR* of its income tax refund claim of ₱5,796 million for the years 1994 - 1998 and 2000, arising from the *SC* decision (net of ₱894 million as approved by the *BIR* for taxable year 2001). In a decision dated December 6, 2010, the *CTA*’s Second Division granted *MERALCO*’s claim and ordered the *BIR* to refund or to issue tax credit certificate in favor of *MERALCO* in the amount of ₱5,796 million in proportion to the tax withheld on the total amount that has been actually given or credited to its customers.

On appeal by the *BIR* to the *CTA* En Banc, *MERALCO*’s petition was dismissed on the ground of prescription in the Decision of the *CTA* En Banc dated May 8, 2012. On Motion for Reconsideration by *MERALCO* of the said dismissal, the *CTA* En Banc partly granted *MERALCO*’s motion and issued an Amended Decision dated November 13, 2012, ruling that *MERALCO*’s claim was not yet barred by prescription and remanding the case back to the *CTA* Second Division for further reception of evidence.

The *BIR* filed a Motion for Reconsideration of the above Amended Decision, while *MERALCO* filed its Motion for Partial Reconsideration or Clarification of Amended Decision. Both parties filed their respective Comments to the said motions, and these were submitted for resolution at the *CTA* En Banc.

In a Resolution promulgated on May 22, 2013, the *CTA* denied the said motions of the *BIR* and *MERALCO*, and the *CTA* Second Division was ordered to receive evidence and rebuttal evidence relating to *MERALCO*’s level of refund to customers, pertaining to the excess charges it made in taxable years 1994-1998 and 2000, but corresponding to the amount of ₱5,796 million, as already determined by the said court.

On July 12, 2013, the *BIR* appealed the *CTA* En Banc’s Amended Decision dated November 13, 2012 and Resolution dated May 22, 2013 via Petition for Review with the *SC*.

Overpayment of Income Tax Related to Change in Tax Basis

On February 4, 2008, the *SC* denied with finality a motion for reconsideration filed by the Commissioner of Internal Revenue or *CIR*, against *MERALCO*, with respect to the issue on excess income tax paid by the latter. The *SC* affirmed a *CA* decision and ordered the *CIR* to refund or issue a *TCC* in favor of *MERALCO* for ₱107 million representing overpaid income taxes for taxable years 1987 and 1988. The overpayment is in accordance with the effectivity of Executive Order No. 72, which subjected *MERALCO* to regular corporate income tax instead of 2% franchise tax based on gross receipts it was previously liable for. On February 5, 2013, *MERALCO* filed a Motion for Issuance of a Writ of Execution with the *CTA* to enforce the judgment of the *SC*. On February 14, 2013, the *CTA* promulgated a Resolution ordering the *CIR* and the *OSG* to comment on the Motion filed by *MERALCO*. On March 14, 2013, the *CTA* promulgated a



Resolution granting the Motion of *MERALCO* and directed the issuance of corresponding Writ of Execution.

LFT Assessments of Municipalities

Certain municipalities have served assessment notices on *MERALCO* for *LFT*. As provided in the Local Government Code or *LGC*, only cities and provincial governments may impose taxes on establishments doing business in their localities. On the basis of the foregoing, *MERALCO* and its legal counsel believe that *MERALCO* is not subject or liable for such assessments.

Real Property Tax or RPT Assessments

Several Local Government Units or *LGUs*, assessed *MERALCO* for deficiency *RPTs* on certain assets of *MERALCO*. The assets include electric poles, wires, insulators, and transformers, collectively referred to as *TWIP*. Of these *LGUs*, one has secured a favorable decision from the *CA*. Such decision was appealed by *MERALCO* to the *SC* for the benefit of *MERALCO* customers, where it is now submitted for resolution. The cases of the other *LGUs* are pending with their respective administrative bodies or government offices.

MERALCO also filed a case against the City of Manila before Regional Trial Court – Pasig branch or *RTC-Pasig*, to enjoin the collection of *RPT* on *MERALCO*'s *TWIP* and nullify *RPT* assessments made thereon based on the argument that these are not within the ambit of the definition of real property under the *LGC*. The case is set for mediation after the City of Manila filed its comments on *MERALCO*'s petition.

In the event that the assessment is sustained by the *SC* and payment is warranted or appropriate, *MERALCO* will file for the recovery of any resulting *RPT* payments from customers in the relevant *LGU* through a separate application with the *ERC*.

Mediation with NPC

The *NPC* embarked on a Power Development Program or *PDP*, which consisted of contracting generating capacities and the construction of its own, as well as private sector, generating plants, following a crippling power supply crisis. To address the concerns of the creditors of *NPC*, namely, Asian Development Bank and the World Bank, the Department of Energy or *DOE* required that *MERALCO* enter into a long-term supply contract with the *NPC*.

Accordingly, on November 21, 1994, *MERALCO* entered into a 10-year Contract for Sale of Electricity or *CSE*, with *NPC* to commence on January 1, 1995. The *CSE* and the rates and amounts charged to *MERALCO* therein were approved by the *BOD* of *NPC* and the then Energy Regulatory Board, respectively.

Separately, the *DOE* further asked *MERALCO* to provide a market for half of the output of the Camago-Malampaya gas field to enable its development and production of natural gas, which was to generate significant revenues for the Philippine Government and equally significant foreign exchange savings for the country to the extent of the fuel imports, which the domestic volume of natural gas will displace.

MERALCO's actual purchases from *NPC* exceeded the contract level in the first seven years of the *CSE*. However, the 1997 Asian crisis resulted in a significant curtailment of energy demand.



While the events were beyond the control of *MERALCO*, *NPC* did not honor *MERALCO*'s good faith notification of its off-take volumes. A dispute ensued and both parties agreed to enter into mediation.

The mediation resulted in the signing of a Settlement Agreement or *SA*, between the parties on July 15, 2003. The *SA* was approved by the respective *BODs* of *NPC* and *MERALCO*. The net settlement amount of ₱14,320 million was agreed upon by *NPC* and *MERALCO* and manifested before the *ERC* through a Joint Compliance dated January 19, 2006. The implementation of the *SA* is subject to the approval of *ERC*.

Subsequently, the Office of the Solicitor General or *OSG* filed a "Motion for Leave to Intervene with Motion to Admit Attached Opposition to the Joint Application and Settlement Agreement between *NPC* and *MERALCO*." As a result, *MERALCO* sought judicial clarification with the *RTC-Pasig*. Pre-trials were set which *MERALCO* complied with and attended. However, the *OSG* refused to participate in the pre-trial and opted to seek a *TRO* from the *CA*.

In a Resolution dated December 1, 2010, the *CA* issued a *TRO* against *RTC-Pasig*, *MERALCO* and *NPC* restraining the respondents from further proceeding with the case. Subsequently, in a Resolution dated February 3, 2011, the *CA* issued a writ of preliminary injunction enjoining the *RTC-Pasig* from conducting further proceedings pending resolution of the Petition. In a Decision dated October 14, 2011, the *CA* resolved to deny the Petition filed by the *OSG* and lifted the injunction previously issued. The said Decision likewise held that the *RTC-Pasig* committed no error in finding the *OSG* in default due to its failure to participate in the proceedings. The *RTC-Pasig* was thus ordered to proceed to hear the case *ex-parte*, as against the *OSG*, and with dispatch. The *OSG* has filed a motion for reconsideration which was denied by the *CA* in its Resolution dated April 25, 2012. The *OSG* filed a Petition for Review of the Certiorari with the *SC*. In a Resolution dated July 25, 2012, the *SC* required *MERALCO* to file a Comment. *MERALCO*'s Comment was filed on October 29, 2012. The *SC* then issued a Resolution dated November 26, 2012 requiring the *OSG* to file a Reply. On February 19, 2013, the *OSG* filed a motion for extension to file a consolidated reply.

With the dismissal of the petition filed by the *OSG* with the *CA*, *MERALCO* filed a motion for the reception of its evidence *ex-parte* with the *RTC-Pasig* pursuant to the ruling of the *CA*. In a Decision dated May 29, 2012, the *RTC-Pasig* declared the *SA*, independent of the pass-through for the settlement amount which is reserved for the *ERC*, valid and binding. The *OSG* has filed a Notice of Appeal with the *RTC-Pasig* on June 19, 2012. Both parties have filed their respective appeal briefs. The case is deemed submitted for resolution by the *CA*.

On January 22, 2014, *MERALCO* received a Notice of Judgment from the *SC* stating that a Decision dated December 11, 2013 was rendered by the First Division of the *SC* denying the Petition for Review on Certiorari by the *OSG* and affirming the decision promulgated by the *CA* on October 14, 2011.

Sucat-Araneta-Balintawak Transmission Line

The Sucat-Araneta-Balintawak transmission line is a two-part transmission line, which completed the 230kV-line loop within Metro Manila. The two main parts are the Araneta to Balintawak leg and the Sucat to Araneta leg, which cuts through Dasmariñas Village, Makati City.

On March 10, 2000, certain residents along Tamarind Road, Dasmariñas Village, Makati City or plaintiffs, filed a case against *NPC* with the *RTC-Makati*, enjoining *NPC* from further installing high voltage cables near the plaintiffs' homes and from energizing and transmitting high voltage electric current through said cables because of the alleged health risks and danger posed by the



same. Following its initial status quo Order issued on March 13, 2000, *RTC-Makati* granted on April 3, 2000 the preliminary injunction sought for by the plaintiffs. The decision was affirmed by the *SC* on March 23, 2006, which effectively reversed a decision of the *CA* to the contrary. The *RTC-Makati* subsequently issued a writ of execution based on the order of the *SC*. *MERALCO*, in its capacity as an intervenor, was constrained to file an Omnibus Motion to maintain status quo because of the significant effect of a de-energization of the Sucat-Araneta line to the public and economy. Shutdown of the 230-kV line will result in widespread and rotating brownouts within *MERALCO*'s franchise area with certain power plants unable to run at their full capacities.

On September 8, 2009, the *RTC-Makati* granted the motions for intervention filed by intervenors, *MERALCO* and *NGCP* and dissolved the Writ of Preliminary Injunction issued, upon the posting of the respective counter bonds by defendant *NPC*, intervenors, *MERALCO* and *NGCP*, subject to the condition that *NPC* and intervenors pay all damages, which the plaintiffs may incur as a result of the Writ of Preliminary Injunction.

Thereafter, the plaintiffs questioned the *RTC-Makati* order before the *CA*. As at March 17, 2014, this case remains pending for resolution in the *CA*.

Moreover, in its Order dated February 5, 2013, the *RTC-Makati* granted plaintiffs' motion and directed the re-raffle of the case to another court after the judicial dispute resolution failed.

Petition for Dispute Resolution against PEMC, TransCo, NPC and PSALM

On September 9, 2008, *MERALCO* filed a Petition for Dispute Resolution, against *PEMC*, *TransCo*, *NPC* and *PSALM* with the *ERC* as a result of the congestion in the transmission system of *TransCo* arising from the outages of the San Jose-Tayabas 500kV Line 2 on June 22, 2008, and the 500kV 600 Mega volt-ampere Transformer Bank No. 2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The Petition seeks to, among others, direct *PEMC* to adopt the *NPC-TOU* rate or the new price determined through the price substitution methodology of *PEMC* as approved by the *ERC*, as basis for its billing during the period of the congestion and direct *NPC* and *PSALM* to refund the transmission line loss components of the line rentals associated with *NPC/PSALM* bilateral transactions from the start of *WESM* operation on June 26, 2006.

In a Decision dated March 10, 2010, the *ERC* granted *MERALCO*'s petition and ruled that there is double charging of the Transmission Line Costs billed to *MERALCO* by *NPC* for the *TSC* quantities to the extent of 2.98% loss factor, since the start of the *TSC* in November 2006. Thus, *NPC* was directed to refund/collect line rental adjustment to/from *MERALCO*. In the meantime, the *ERC* issued an Order on May 4, 2011 directing *PEMC* to submit an alternative methodology for the segregation of line rental into congestion cost and line losses from the start of the *WESM*. *PEMC* has filed its compliance submitting its alternative methodology.

On September 8, 2011, *MERALCO* received a copy of *PEMC*'s compliance to *ERC*'s directive and on November 11, 2011, *MERALCO* filed a counter-proposal which effectively simplifies *PEMC*'s proposal.

On November 11, 2011, *MERALCO* filed its Motion to Implement the Decision dated March 10, 2010 by immediately effecting the refund/collection of line rental adjustments to consumers. On December 21, 2011, *PSALM* filed its comment on *MERALCO*'s said Motion. Then, in an Order dated January 24, 2012, the *ERC* directed *PEMC*, *Transco* and *NPC* to submit their respective comments on *MERALCO*'s motion within five days from receipt.



In an Order of the *ERC* dated June 21, 2012, *MERALCO* was directed to submit its computation of the amount of the double charging of line loss on a per month basis from June 26, 2006 up to June 2012. On July 4, 2012, *MERALCO* filed its Compliance to the said Order. Thereafter, the *ERC* issued an Order directing the parties to comment on *MERALCO*'s submissions.

In an Order dated March 4, 2013, the *ERC* approved the methodology proposed by *MERALCO* and *PEMC* in computing the double charged amount on line losses by deducting 2.98% from the *NPC-TOU* amount. Accordingly, the *ERC* determined that the computed double charge amount to be collected from *NPC* is ₱5.2 billion, covering the period November 2006 to August 2012 until actual cessation of the collection of the 2.98% line loss charge in the *NPC-TOU* rates imposed on *MERALCO*, while the amount to be collected from the *SGCs* is ₱4.7 billion. Additionally, *MERALCO* was directed to file a petition against the following *SGCs*: *MPPCL*, Aboitiz Power Renewables, Inc. or *APRI*, *TLI*, *SMEC* and *Sem-Calaca*, within thirty (30) days from receipt thereof, to recover the line loss collected by them. *MERALCO* filed a motion for clarification with the *ERC* regarding the directives contained in the March 4, 2013 Order. On April 30, 2013 and May 8, 2013, *PSALM* and *NPC*, respectively, filed motions seeking reconsideration of the March 4, 2013 Order.

In an Order dated July 1, 2013, the *ERC* issued the following clarifications/resolutions: 1) *SPPC* should be included as one of the *SGCs* against whom a petition for dispute resolution should be filed by *MERALCO*; 2) Amount to be refunded by *NPC* is not only ₱5.2 billion but also the subsequent payments it received from *MERALCO* beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates; and Petition to be filed by *MERALCO* against the *SGCs* should not only be for the recovery of the amount of ₱4.7 billion but also the subsequent payments beyond August 2012 until the actual cessation of the collection of the 2.98% line loss charge in its *TOU* rates. ; 3) "SCPC Ilijan" pertains to *SPPC* instead. Thus, the refundable amount of ₱706 million pertaining to "SCPC Ilijan" should be added to *SPPC*'s refundable amount of ₱1.1 billion; 4) Grant the "Motion for Extension" filed by *MERALCO* which was directed to file a petition against the following *SGCs*: *MPPCL*, *APRI*, *TLI*, *SMEC*, *Sem-Calaca* and *SPPC*, otherwise, it shall be the one liable to refund the subject amount to its customers; and 5) deny the respective "Motions for Reconsideration" filed by *NPC* and *PSALM*.

On September 12, 2013, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking approval of its proposal to offset the amount of ₱74 million against some of its monthly remittances to *PSALM*. *PSALM* and *NPC* filed their comments *ad cautelam* on *MERALCO*'s Manifestation and Motion. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion. On November 4, 2013, *MERALCO* filed its Reply. *MERALCO* is awaiting the resolution of the *ERC* on its Manifestation and Motion.

On October 24, 2013, *MERALCO* received *PSALM*'s Petition for Certiorari with the *CA* (With Urgent *TRO* and/or Writ of Preliminary Mandatory Injunction Applications) to question the March 4, 2013 and July 1, 2013 Orders of the *ERC*. In a Resolution dated December 29, 2013, the *CA* gave *MERALCO* until December 26, 2013, within which to submit its Comment on the Petition for Certiorari and to show cause why the prayer for the Application for *TRO* and/or Preliminary Injunction should not be granted ("*Comment and Opposition*"). On December 23, 2013, January 5, 2014 and January 15, 2014, *MERALCO* requested for an additional period of ten (10) days each, within which to submit its *Comment and Opposition*.

On February 2, 2014, *MERALCO* filed its Comment to said Petition. As at March 17, 2014, the *CA* has yet to rule on the Petition.



Petition for Dispute Resolution Against SPPC, MPPCL, APRI, TLI, SMEC and Sem-Calaca

On August 29, 2013, *MERALCO* filed a Petition for Dispute Resolution against *SPPC*, *MPPCL*, *APRI*, *TLI*, *SMEC* and *Sem-Calaca*. Said Petition seeks the following: a) Refund of the 2.98% transmission line losses in the amount of ₱5.4 billion from said *SGCs*; and 2) approval of *MERALCO*'s proposal to correspondingly refund to its customers the aforementioned line loss amounts, as and when the same are received from the *SGCs*, until such time that the said over-recoveries are fully refunded, by way of automatic deduction of the amount of refund to the computed monthly generation rate. On September 20, 2013, *MERALCO* received the *SGCs*' Joint Motion to Dismiss. On October 7, 2013, *MERALCO* filed its Comment on the said Joint Motion. On October 8, 2013, *MERALCO* received the *SGCs* Manifestation and Motion. On October 14, 2013, *MERALCO* filed its Opposition thereto. On October 24, 2013, *MERALCO* received the *SGC*'s Reply to its Comment. On October 29, 2013, *MERALCO* filed its Rejoinder.

PSALM versus PEMC and MERALCO

Due to the unusually large increases in *WESM* prices during the 3rd and 4th months of the *WESM* operations, *MERALCO* raised concerns with the *PEMC* to investigate whether *WESM* rules were breached or if anti-competitive behavior had occurred.

While resolutions were initially issued by the *PEMC* directing adjustments of *WESM* settlement amounts, a series of exchanges and appeals with the *ERC* ensued. *ERC*'s decision directing the *WESM* settlement price for the 3rd and 4th billing months to be *NPC-TOU* rates prompted *PSALM* to file a Motion for Reconsideration with the *CA*, which was denied on November 6, 2009. In December 2009, *PSALM* filed a Petition for Review on Certiorari with the *SC*.

As at March 17, 2014, *PSALM*'s petition for review is pending resolution by the *SC*.

Petition for Dispute Resolution with NPC on Premium Charges

On June 2, 2009, *MERALCO* filed a Petition for Dispute Resolution against *NPC* and *PSALM* with respect to *NPC*'s imposition of premium charges for the alleged excess energy it supplied to *MERALCO* covering the billing periods May 2005 to June 2006. The premium charges amounting to ₱315 million during the May-June 2005 billing periods have been paid but are the subject of a protest by *MERALCO*, and premium charges of ₱318 million during the November 2005, February 2006 and April to June 2006 billing periods are being disputed and withheld by *MERALCO*. *MERALCO* believes that there is no basis for the imposition of the premium charges. The hearings on this case have been completed and *MERALCO* is now awaiting the resolution of the *ERC* on the petition.

SC Temporary Restraining Order on MERALCO's December 2013 Billing Rate Increase

On December 9, 2013, the *ERC* gave clearance to the request of *MERALCO* to implement a staggered collection over three (3) months covering the December 2013 billing month for the increase in generation charge and other bill components such as *VAT*, *LFT*, transmission charge, and *SL* charge, which reflected a total increase of ₱4.15 per *kWh* for a 200-*kWh* residential consumer. The generation costs for the November 2013 supply month increased significantly because of the use of the more expensive liquid fuel by the natural gas-fired power plants that were affected by the Malampaya Gas Field or *Malampaya*, shutdown from November 11 to December 10, 2013. This was compounded by the aberrant spike in the *WESM*, charges on account of the scheduled and extended shutdowns, and the forced outages of several base load



power plants, as well as the non-compliance with *WESM* Rules by certain plants resulting in significant power generation capacities not being offered and dispatched.

The Department of Justice commenced an investigation while the House of Representatives and the Senate conducted separate hearings to determine the underlying reasons for the price increase, including any possible collusion among the power firms. In the meantime, *MERALCO* proceeded with billing its captive customers with the *ERC* approval.

On December 19, 2013, several interest groups filed a Petition against *MERALCO*, *ERC* and the *DOE* before the *SC*, questioning the *ERC* clearance granted to *MERALCO* to charge the ₱4.15 per *kWh* price increase, alleging the lack of hearing and due process. It also sought for the declaration of the unconstitutionality of the *EPIRA*, which essentially declared the generation and supply sectors competitive and open, and not considered public utilities. A similar petition was filed by a consumer group and several private homeowners associations challenging also the legality of the *AGRA* that the *ERC* had promulgated. Both petitions prayed for the issuance of a *TRO*, and a Writ of Preliminary Injunction.

On December 23, 2013, the *SC* consolidated the two (2) Petitions and granted the application for *TRO* effective immediately and for a period of sixty (60) days, which effectively enjoined the *ERC* and *MERALCO* from implementing the ₱4.15 per *kWh* price increase. The *SC* also ordered *MERALCO*, *ERC* and *DOE* to file their respective comments to the Petitions and set the hearing for Oral Arguments on January 21, 2014. The *SC* further set two more Oral Arguments on February 4, 2014 and February 11, 2014. After the conclusion of the Oral Arguments, the *SC* gave all the Parties to the consolidated Petitions to file their respective Memorandum on or before February 26, 2014 after which the Petitions will be deemed submitted for resolution of the *SC*. *MERALCO* complied with said directive and filed its Memorandum on said date.

On February 18, 2013, acting on the motion filed by the Petitioners, the *SC* extended for another period of 60 days or until April 22, 2014, the *TRO* that it originally issued against *MERALCO* and *ERC* last December 23, 2013. The *TRO* was also similarly applied to the generating companies, specifically *MPPCL*, *SMEC*, *SPPC*, *FGPC*, and the or *NGCP*, and the *PEMC* (the administrator of *WESM* and market operator) who were all enjoined from collecting from *MERALCO* the deferred amounts representing the ₱4.15 per *kWh* price increase for the November 2013 supply month.

In the meantime, on January 30, 2014, *MERALCO* filed an Omnibus Motion with Manifestation with the *ERC* for the latter to direct *PEMC* to conduct a re-run or re-calculation of the *WESM* prices for the supply months of November to December 2013. Subsequently, on February 17, 2014, *MERALCO* filed with the *ERC* an Application for the recovery of deferred generation costs for the December 2013 supply month praying that it be allowed to recover the same over a six (6)-month period.

On March 3, 2014, the *ERC* issued an Order voiding the Luzon *WESM* prices given that the prices in *WESM* during the November and December 2013 supply months could not qualify as reasonable, rational and competitive. *PEMC* was given seven (7) days upon receipt of the Order to calculate these regulated prices and implement the same in the revised *WESM* bills of the concerned.

As at March 17, 2014, *MERALCO* is still awaiting decisions of the *SC* on the *TRO*.



Others

Management and its internal and external counsels believe that the probable resolution of these issues will not materially affect *MERALCO*'s financial position and results of operations.

29. Significant Contracts and Commitments

NPC

MERALCO and *NPC* entered into a Transition Supply Contract or *TSC*, effective the earlier of five years from November 16, 2006 up to December 25, 2011 or one year after the introduction of Open Access, should *RCOA* be in place within the five-year contract period. Two addenda for additional contracted volumes were signed, the most recent being in 2010. The adjusted contracted volume was for a total of more than 40,000 *GWh* up to 2011.

On December 26, 2011, the *TSC* with *NPC* was extended until December 25, 2012 or three months after the implementation of the *RCOA*, whichever comes first.

As a result of the extension of the *TSC*, the Customer Choice Program or *CCP*, which is a joint program of *NPC* and *MERALCO* aimed at providing *NPC* time-of-use or *TOU*, benefits to qualified customers, has also been extended to be co-terminus with the *TSC*. The *CCP* program expired on December 25, 2012.

With respect to the *TSC*, *MERALCO*, *NPC* and *PSALM* then executed a Memorandum of Agreement or *MOA* which further extended the *TSC* until June 25, 2013.

On June 26, 2013, *MERALCO*'s *TSC* with *NPC* was terminated.

Assignment of TSC Volume to SGCs

From 2008 to 2009, *NPC* privatized a number of its generating assets and *IPP* contracts in favor of the successful bidders. As a result, the contracted energy volume under the original *TSC* between *MERALCO* and *NPC* was assigned by *NPC* to the respective new owners and *IPPs*. Following are the privatized plants and *IPP* contracts:

Year	Power Plant	Successor Owner/ <i>IPPs</i>	% of Total Volume
2008	Masinloc coal-fired power plant – 600 <i>MW</i>	<i>MPPCL</i>	21.3
2009	Tiwi-Makban geothermal power plants – 289 <i>MW</i>	<i>APRI</i>	8.1
	Pagbilao power plant – 735 <i>MW</i>	<i>TLI</i>	25.0
	Sual coal-fired power plant – 1,000 <i>MW</i>	<i>SMEC</i>	8.6
	Coal-fired Calaca power plant – 600 <i>MW</i>	<i>Sem-Calaca</i>	10.4
2010	Combined cycle gas turbine, natural gas-fired Ilijan power plant – 1,200 <i>MW</i>	<i>SPPC</i>	15.2

NPC/PSALM remains the contracting party of record for the supply of power to *MERALCO*. Payments of the contracted volume are made based on the billing instructions from *NPC/PSALM* received by *MERALCO*.



PSAs with Privatized Plants and IPPAs

MERALCO entered into separate *PSAs* with *SPPC*, *Sem-Calaca* and *MPPCL* on December 12, 20 and 21, 2011, respectively. Also, a *PSA* with *TLI* was executed on February 29, 2012. These *PSAs* are for a period of seven years, extendable for three years upon agreement of the parties.

In March 2012, the application for approval of the *PSAs* was filed with the *ERC*. On June 26, 2012, *MERALCO BOD* approved the grant of authority to *MERALCO* to enter into a *PSA* with *SMEC* for a period of seven years, extendable for three years upon agreement of the parties.

On March 16, 2012, *MPower* signed a new *PSA* with *MPPCL* for 30MW of contracted capacity from the Masinloc coal-fired power plant in Zambales for seven years, extendable for three years upon agreement of the parties.

On April 26, 2012, the *BOD* approved the *PSA* with Pangea Green Energy Philippines, Inc., or *PGEP*, a biogas power plant located in Payatas, Quezon City using methane gas extracted from the Payatas Landfill as its fuel. Its plant has a total nominal generating capacity of 1,236 kW.

In separate Decisions dated December 17, 2012, the *ERC* approved with modifications the *PSAs* of *MERALCO* with *MPPCL*, *SPPC*, *Sem-Calaca*, *TLI* and *SMEC*.

Motions for Reconsideration were filed regarding the *ERC* decisions on the *PSAs* with *SPPC*, *Sem-Calaca* and *SMEC*. *MERALCO* is awaiting the decision of the *ERC*.

On December 27, 2012, *MERALCO* executed the *PSAs* with *TLI* and *APRI* to cover the volume needed by *MERALCO* during the six-month transition period before the start of the commercial operations of *RCOA*. Under the *PSAs* with *TLI* and *APRI*, *MERALCO* will procure power from *TLI* and *APRI* from the expiration of the *TSC* until June 25, 2013 conditioned upon *ERC* approval. The said *PSAs* had been submitted to the *ERC* for approval on January 2, 2013. However, on September 26, 2013, *MERALCO* filed Motions to withdraw the said *PSAs*, considering that the *TSC* was extended up to June 25, 2013. The *ERC* granted said Motions in separate Orders dated September 27, 2013.

Under the *PSAs*, fixed capacity fees and fixed operating maintenance fees are recognized monthly based on their contracted capacities. The annual projection of these payments is shown in the table below:

Year	Contracted Capacity	Fixed Payment Amount
	<i>(In Megawatt)</i>	<i>(In million)</i>
2014	3,000	₱35,419
2015	3,084	37,775
2016	3,114	39,865
2017	3,114	39,574
2018	2,880	39,198
2019	2,460	33,864



FGPC and FGP

In compliance with the DOE's program to create a market for Camago-Malampaya gas field and enable its development, *MERALCO* was committed to contract 1,500-MW of the 2,700 MW output of the Malampaya gas field.

Accordingly, *MERALCO* entered into separate 25-year *PPAs* with *FGPC* (March 14, 1995) and *FGP* (July 22, 1999) for a minimum number of *kWh* of the net electrical output of the Sta. Rita and San Lorenzo power plants, respectively, from the start of their commercial operations. The *PPA* with *FGPC* terminates on August 17, 2025, while that of *FGP* ends on October 1, 2027.

On January 7, 2004, *MERALCO*, *FGP* and *FGPC* signed an Amendment to their respective *PPAs*. The negotiations resulted in certain new conditions including the assumption of *FGP* and *FGPC* of community taxes at current tax rate, and subject to certain conditions increasing the discounts on excess generation, payment of higher penalties for non-performance up to a capped amount, recovery of accumulated deemed delivered energy until 2011 resulting in the non-charging of *MERALCO* of excess generation charge for such energy delivered beyond the contracted amount but within a 90% capacity quota. The amended terms under the respective *PPAs* of *FGP* and *FGPC* were approved by the *ERC* on May 31, 2006.

Under the respective *PPAs* of *FGP* and *FGPC*, the fixed capacity fees and fixed operating and maintenance fees are recognized monthly based on the actual Net Dependable Capacity tested and proven, which is usually conducted on a semi-annual basis.

QPPL

MERALCO entered into a *PPA* with *QPPL* on August 12, 1994, which was subsequently amended on December 1, 1996. Under the terms of the amended *PPA*, *MERALCO* is committed to purchase a specified volume of electric power and energy from *QPPL*, subject to certain terms and conditions. The *PPA* is for a period of 25 years from the start of commercial operations up to July 12, 2025.

In a Letter Agreement signed on February 21, 2008, the amount billable by *QPPL* included a transmission line charge reduction in lieu of a previous rebate program. The Letter Agreement also provides that *MERALCO* make advances to *QPPL* of US\$2.85 million per annum for 10 years beginning 2008 to assist *QPPL* in consideration of the difference between the transmission line charge specified in the *TLA* and the *ERC*-approved transmission line charge in March 2003. *QPPL* shall repay *MERALCO* the same amount at the end of the 10-year period in equal annual payments without adjustment. However, if *MERALCO* is able to dispatch *QPPL* at a plant capacity factor of no less than 86% in any particular year, *MERALCO* shall not be required to pay US\$2.85 million in that year. This arrangement did not have any impact on the rates to be charged to consumers and hence, did not require any amendment in the *PPA*, as approved by *ERC*.



See Note 9 – Other Noncurrent Assets.

Committed Energy Volume to be Purchased

The following are forecasted purchases/payments to *FGPC*, *FGP* and *QPPL* corresponding to the Minimum Energy Quantity or *MEQ*, provisions of the contracts. The forecasted fixed payments include capacity charge and fixed operation and maintenance cost escalated using the US and Philippine Consumer Price Index or *CPI*.

Year	Minimum Energy Quantity (MEQ) <i>(In Million Kilowatt-Hours)</i>	Equivalent Amount <i>(In millions)</i>
2014	14,955	₱21,476
2015	14,955	21,577
2016	14,855	21,592
2017	14,855	21,817
2018	14,855	22,011
2019-2025	103,984	159,967

Montalban Methan Power Corporation or MMPC

MMPC operates an 8 *MW* (designed capacity of 11 *MW*) renewable energy generating facility, which utilizes landfill gas.

On May 13, 2009, *MERALCO* filed an application for the approval of the *CSE* with *MMPC* with the *ERC*. On June 9, 2009, *ERC* issued an order dated June 1, 2009 provisionally approving the *CSE* subject to the following conditions: (i) any amendments to the *CSE* shall be filed with the *ERC* for approval and the implementation shall be prospective; and (ii) in the event the rates approved are higher than the final rates, the amount corresponding to the excess shall be refunded by *MERALCO* to its customers by crediting the same in their electric bills.

On June 11, 2009, *MMPC* began delivering energy to *MERALCO* under a two year *CSE*. The *CSE* is a “take and pay” arrangement, without a minimum energy volume. Energy is billed to *MERALCO* on an hourly basis at the *ERC*- approved *NPC TOU* rate plus certain pre-agreed cost components. Being an embedded renewable energy generator, purchases from *MMPC* are *VAT* zero-rated. Energy deliveries from *MMPC* are exempt from power delivery service charge.

After a series of negotiations, on May 23, 2011, *MERALCO* and *MMPC* signed a Letter Agreement extending the *CSE*. Said Agreement likewise contained minor amendments to the *CSE* that were intended to benefit the consumers. On June 3, 2011, *MERALCO* filed a Manifestation with Motion with the *ERC* seeking the approval of the Letter Agreement, pursuant to the condition contained in the *ERC* Order dated June 1, 2009. On February 19, 2013, the *ERC* issued its Decision approving the application.

BEI

MERALCO signed a *CSE* with *BEI* on November 12, 2010. *BEI* owns and operates a 4*MW* renewable energy generation facility powered by landfill gas in San Pedro, Laguna.

The terms of the *CSE* with *BEI* are similar to that signed with *MMPC*. Purchases from *BEI*, an embedded renewable energy generator, are *VAT* zero-rated and exempt from power delivery service charge. *MERALCO* filed an application for the approval of the *CSE* with the *ERC*, for the provisional implementation of the contract on December 15, 2010. In an order dated



January 31, 2011, the *ERC* provisionally approved the said application which extended the implementation indefinitely. The said case is pending decision by the *ERC*.

Therma Mobile, Inc. or TMO

On March 4, 2013, *MERALCO* signed an Interconnection Agreement with Therma Mobile Inc. or *TMO* for their 242 *MW* generating facility at the Navotas Fish Port Complex, Navotas City, which is an interconnection at *MERALCO*'s Grace Park - Malabon 115kV line. *TMO* is thus an embedded generator. *TMO* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*'s system.

On September 27, 2013, *MERALCO* signed a *PSA* with *TMO* for the output of the barge-mounted, bunker oil-fired diesel engines moored at the Fishport Complex in Navotas, Manila. On November 4, 2013, the application for approval of the *MERALCO-TMO PSA* was provisionally approved by the *ERC*.

Interconnection Agreement with Alternergy Philippine Holdings Corporation or Alternergy

On March 1, 2012, *MERALCO* signed an Interconnection Agreement with *Alternergy* for their 90*MW* Wind Farm Renewable Energy plant in Pililla, Rizal, which is an interconnection at *MERALCO*'s Malaya-Teresa 115kV line, *Alternergy* is thus an embedded generator. *Alternergy* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*'s system.

Interconnection Agreement with Maibarara Geothermal, Inc. or MGI

On December 6, 2012, *MERALCO* signed an Interconnection Agreement with *MGI* for their 20*MW* (with max capacity of 40 *MW*) Geothermal Facility plant in Sto. Tomas, Batangas, which is an interconnection at *MERALCO*'s FPIP - Los Banos 115kV line. *MGI* is thus an embedded generator. *MGI* shall construct at its own cost, operate and maintain the 115kV line connecting its generating facility to *MERALCO*'s system.

30. Earnings Per Share

Basic and diluted earnings per share or *EPS* are calculated as follows:

	2013	2012 (As restated - see Note 4)
<i>(Amounts in millions, except per share data)</i>		
Net income (a)	₱17,487	₱20,193
Weighted average number of common shares outstanding (b)	14 1,127	1,127
Basic/diluted <i>EPS</i> (a/b)	₱15.52	₱17.92



Basic and diluted earnings per share amounts are calculated by dividing net income for the year by the weighted average number of common shares outstanding during the year. There are no potential dilutive common shares in 2013 and 2012. There are no other transactions involving common shares or potential common shares between the reporting date and the date of completion of these parent company financial statements.

31. Other Matters

Revised SL Caps

On December 8, 2008, the ERC promulgated a resolution providing for a lower maximum rate of SL (technical and non-technical) that a utility can pass on to its customers. The revised SL cap is 8.5% for private utilities, effective January 2010 billing. This is one percentage point lower than the SL cap of 9.5% provided under RA No. 7832. The actual volume of electricity used by MERALCO (administrative loss) is treated as part of the operation and maintenance expense beginning July 2011. The manner by which the utility is rewarded for its efforts in SL reduction is addressed by the ERC in the PIS under PBR.

On December 8, 2009, MERALCO filed a Petition to amend the said Resolution with an urgent prayer for the immediate suspension of the implementation of the new SL cap of 8.5% starting January 2010. The proposed amendment is aimed at making the Resolution consistent with the provisions of RA No. 9136 and RA No. 7832, by increasing the SL cap to not less than 9%. The hearing on the Petition was conducted on November 18, 2010. Thereafter, MERALCO was directed to submit its FOE. MERALCO has submitted its FOE and is awaiting ERC decision on the Petition.

Benefit Sharing Scheme to Lower System Loss

On January 26, 2011, MERALCO, together with Private Electric Power Operators Association, Inc. or PEPOA and Philippine Rural Electric Cooperative Association or PHILRECA, filed a joint petition to the ERC to initiate rule-making to adopt the *Proposed Guidelines for the Implementation of an Incentive Scheme to Lower the System Losses of Private Distribution Utilities and Electric Cooperatives to Level Below the System Loss Cap, for the Benefit of End-Users*. This was aimed to encourage the DUs to reduce system loss levels below the cap set by the ERC and benefit the end-users through lower system loss charges. Public hearings were conducted and completed on June 15, 2011.

On December 11, 2012, the ERC posted on its website second draft of the *Rules to Govern the Implementation of a Benefit Sharing to Lower the System Losses of Electric Distribution Utilities*. The salient points of the second draft rules include calculation of System Loss Charge using the prevailing system loss cap or the lowest consecutive five year average system loss, whichever is lower, and an equitable sharing (50-50) of incentives between the customer and the DU on the savings which is the difference between the lower of this system loss level and the DU's actual system loss. Any system loss reward from the PIS under the RDWR for private DUs shall be offset from the rewards the DU will receive from this Benefit-Sharing scheme, except when the net benefit from this scheme is less than the PIS rewards of the DU, in which case the DU will retain the rewards under the PIS and forego its share under this Benefit-Sharing Scheme. The foregone share of the DU shall be added to the End-user share correspondingly. As at March 17, 2014, MERALCO and PEPOA are awaiting the action of the ERC on this matter.



Retail Competition

On February 24, 2012, the *DOE* issued a circular designating the *PEMC* as the Central Registration Body, or *CRB* under the *RCOA*. The *CRB* is tasked to develop market infrastructure, systems and processes capable of supporting *RCOA* registration, customer switching and information exchange among industry participants.

On May 9, 2012, the *DOE* issued another circular prescribing the general policies for the implementation of *RCOA*. The circular provides the overall direction *DOE* intends to take in developing the policy framework for *RCOA* implementation.

On September 27, 2012, the *DOE* and the *ERC* issued a joint statement setting the initial *RCOA* implementation on December 26, 2012. The joint statement clarified that the *RCOA* commencement is on a phase-in and partial implementation of the program, with the first six (6) months of *RCOA* implementation (December 26, 2012 – June 25, 2013) allotted as the Transition Period to allow all concerned parties to undertake their respective preparations to operationalize the mechanism for *RCOA*. An initial *RCOA* Commercial Operation using an interim IT system started on June 26, 2013.

On December 17, 2012, the *ERC* issued Resolution No. 16 series of 2012 adopting the Transitory Rules for the implementation of *RCOA*. The resolution provides the detailed responsibilities of industry participants during the *RCOA* transition period.

On January 9, 2013, the *DOE* issued Department Circular No. DC2013-01-0002, "Promulgating the Retail Rules for the Integration of Retail Competition and Open Access in the Wholesale Electricity Spot Market", to provide rules for the integration of retail competition in the operations and governance processes of the *WESM*, the management of the transactions of Suppliers and Contestable Customers, and the operations of the Central Registration Body.

On March 22, 2013, the *ERC* released a resolution that directed all *DUs* and licensed *RES* in Luzon and Visayas to disclose to the *ERC* their capacity and energy allocations for the customers they intend to serve. *MERALCO* complied with the directive.

On March 26, 2013, *PEMC* began the *RCOA* Trial Operations Program, a nine-week test period participated in by the various entities and service providers of *RCOA*.

On May 6, 2013, the *DOE* issued Department Circular No. DC2013-05-0006, "Enjoining all Generation Companies, Distribution Utilities, Suppliers and Local Suppliers to Ensure an Effective and Successful Transition towards the Implementation of Retail Competition and Open Access", which required generation companies, suppliers and *DUs* to disclose their supply portfolio and capacity allocation to determine the available energy supply for Contestable Customer in the market. *MERALCO* submitted its first compliance to said Circular last June 7, 2013.

On June 19, 2013, the *ERC* issued a resolution adopting the Supplemental Rules to the Transitory Rules for the implementation of *RCOA*. The resolution seeks to prevent contestable customers who have yet to execute a Retail Supply Contract or *RSC*, with a *RES* from being disconnected or transferred to *SOLR* service upon the commencement of initial commercial operations of *RCOA*. Qualified contestable customers who fail to enter into a *RSC* with a *RES* shall be deemed to stay with their current *DU* until December 26, 2013 or until such time that it is able to find a *RES* provided that they inform the *DU*.



In accordance with the *ERC*'s "Transitory Rules for the Initial Implementation of Open Access and Retail Competition", commercial operations of *RCOA* began on June 26, 2013. Nineteen *RESs* were licensed by the *ERC* to provide competitive retail supply service to eligible contestable customers. As at December 31, 2013, 287 customers have opted for contestability and are now being supplied by competitive retail electricity suppliers.

On July 22, 2013, the *DOE* issued a circular promulgating the Retail Market Manuals for the following: Registration Criteria and Procedures, Market Transactions Procedures, Disclosure and Confidentiality of Contestable Customer Information, and Metering Standards and Procedures.

On September 4, 2013, the *ERC* conducted a public consultation on its proposed amendments to the *RES Licensing Rules*, for which *MERALCO* submitted comments and participated in the public consultation.

As at December 31, 2013, there are about 782 contestable customers in *MERALCO*'s franchise area and 287 have already switched to their respective *RESs*.

Philippine Export Zone Authority or PEZA – ERC Jurisdiction

On September 13, 2007, *PEZA* issued "Guidelines in the Registration of Electric Power Generation Facilities/Utilities/Entities Operating Inside the Ecozones" and "Guidelines for the Supply of Electric Power in Ecozones." Under these Guidelines, *PEZA* effectively bestowed upon itself franchising and regulatory powers in Ecozones operating within the legislative franchise areas of *DUs* which are under the legislatively-authorized regulatory jurisdiction of the *ERC*. The Guidelines are the subject of an injunction case filed by the *DUs* at the *RTC-Pasig*.

In support of the government's objective of providing lower cost to Ecozone locators, *MERALCO* entered into a *MOA* with *NPC* on September 17, 2007 for the provision of special Ecozone rates to high load factor *PEZA*-accredited industries. The *ERC* authorized the immediate implementation of the Ecozone Rate Program or *ERP*. The program expired in December 2012.

The *ERP* was initially scheduled to expire by December 25, 2011 but has been extended twice and was terminated on December 25, 2012.

In January 2013, *MERALCO* entered into a tripartite agreement with *PEZA* and Trans-Asia Oil and Energy Development Corporation for the sale of power to *CEZ* and its locators beginning January 26, 2013.

Purchase of Subtransmission Assets or STAs

On November 25, 2009, *MERALCO* signed a Contract to Sell with *TransCo* for the sale and purchase of certain subtransmission assets for ₱86 million. On February 25, 2010, the *ERC* approved this Contract to Sell. On June 1, 2012, the *ERC* rendered a decision dated March 6, 2012, approving the sale of the said *STAs* in favor of *MERALCO* for ₱85 million.

On April 17, 2012, *MERALCO* and *TransCo* filed a joint application for the approval of the Batch 4 contract to sell with the *ERC*. On April 22, 2013, the *ERC* issued a Decision on *MERALCO*'s joint application for the acquisition of the Batch 4 contract to sell. On June 21, 2013, *MERALCO* filed a motion for partial reconsideration regarding the exclusion of certain facilities for acquisition, which has yet to be resolved by the *ERC*.



On December 12, 2011, *MERALCO* signed various agreements for the acquisition of certain sub-transmission assets of *TransCo* within the *MERALCO* franchise area for its sole account, as well as with a consortium with Batangas II Electric Cooperative, Inc., or *BATELEC II* and First Bay Power Corporation. On September 18, 2012, an amended consortium agreement was executed between *MERALCO* and *FBPC*. On October 17, 2012, *MERALCO* signed two separate amended consortium agreements with *BATELEC II*, and with *FBPC* and *BATELEC II*. These amended consortium agreements superseded the ones signed on December 12, 2011. On December 27 and 28, 2012, the Contract to Sell and Consortium Agreements, respectively, covering these sub-transmission assets were filed with the *ERC* for approval.

MERALCO's Peak/Off-Peak or POP Program

On November 15, 2012, *MERALCO* filed an application with the *ERC* for the approval of its revised Time of Use or *TOU* rates program, also known as the *POP* Program. The *POP* is a rate program being offered by *MERALCO* to customers whose load characteristics can benefit from *TOU* rates as well as to those that can shift their loads from peak to off-peak hours. The proposed revised *POP* Rate aims to provide better savings to avalees by providing them with a *TOU* program that has a wider pricing difference between peak and off-peak rates.

In an Order dated December 17, 2012, the *ERC* provisionally approved the *POP* Program.

Feed-in-Tariff (FIT)

Pursuant to Republic Act No. 9513, or the Renewable Energy Act of 2008 or *RE Act*, the *ERC* issued Resolution No. 16, Series of 2010, Adopting the Feed-in-Tariff or *FIT* Rules, on July 23, 2010. As defined under the *FIT* Rules, the *FIT* system is as a renewable energy policy that offers a guaranteed payment on a fixed rate per kilowatt-hour for electricity from wind, solar, ocean, hydropower and biomass energy sources.

On May 16, 2011, the National Renewable Energy Board or *NREB* filed its Petition to Initiate Rule Making for the Adoption of *FIT*. The Petition proposed a specific *FIT* Rate for each emerging renewable resource. On July 27, 2012, after undergoing several public consultations and public hearings, the *ERC* approved *FIT* Rates that are significantly lower than the rates applied by the *NREB*.

To fund the *FIT* payments to eligible *RE* developers, a *FIT*-Allowance charge will be imposed on all end-users. The *FIT*-Allowance will be established by the *ERC* upon petition by the *TransCo*, which had been designated as the *FIT* Fund Administrator. The *FIT*-Allowance Petition will go through the process of public hearings and consultations.

To supplement the *FIT* Rules, the *ERC* is currently drafting *FIT*-Allowance Payment and Collection Guidelines. This set of guidelines will govern how the *FIT*-Allowance will be calculated using the formulae provided. It will also outline the process of billing and collecting the *FIT*-Allowance from the electricity consumers, the remittance to a specified fund, the disbursement from the *FIT*-Allowance fund and the payment to eligible *RE* developers. The draft is currently undergoing public consultations.

Net Metering Program

The *RE Act* mandates the *DUs* to provide the mechanism for the “physical connection and commercial arrangements necessary to ensure the success of the *RE* programs”, specifically the Net Metering Program. The *RE Act* defines Net Metering as “a system, appropriate for distributed



generation, in which a distribution grid user has a two-way connection to the grid and is only charged for his net electricity consumption and is credited for any overall contribution to the electricity grid". By their nature, net metering installations will be small (less than 100 kW) and will likely be adopted by the households and small business end-users of DUs.

On September 4, 2012, the ERC released the first draft of the Proposed Net Metering Rules. The proposed rules will govern the implementation of the Net Metering program for RE sources. It also seeks to establish the standards for interconnecting these RE sources to the DUs' systems. The pricing methodology, however, will be addressed in another set of rules and will be endorsed to the ERC in due course. Meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. On September 21, 2012, the ERC conducted the first public consultation on the proposed rules.

After consultations with stakeholders, the ERC issued on July 3, 2013 its Resolution No. 09, Series of 2013, entitled, "A Resolution Adopting the Rules enabling the Net Metering Program for Renewable Energy". The rules will govern the DUs' implementation of the Net Metering program. Included in Rules are the Interconnection Standards that shall provide technical guidance to address engineering, electric system reliability, and safety concerns for net metering interconnections. The final pricing methodology, however, will be addressed in another set of rules and will be endorsed to the ERC in due course. In the meantime, the distribution utilities' blended generation cost equivalent to the generation charge, shall be used as the preliminary reference price in the net metering agreement. The rules shall took effect on July 24, 2013. MERALCO started accepting net metering applications on the same day. As at March 17, 2014, MERALCO has already energized five Net Metering customers, the country's first participants to the Net Metering Program.

32. Supplementary Information Required Under Revenue Regulations No. 15-2010

In compliance with the requirements set forth by RR No. 15-2010, hereunder are the information on taxes, duties and license fees paid and accrued during the taxable year.

Output VAT

MERALCO is a VAT-registered company with total VAT output tax declared of ₱6,315 million in 2013 based on the following revenue streams:

Revenue Item	Amount
	(In Millions)
Distribution revenues	₱57,339
Leases and others	563
	₱57,902

MERALCO has zero-rated distribution revenues of ₱2,025 million pursuant to the provisions of RA No. 7916 as amended by RA No. 8748, RA 9337 Section 108B, RR No. 16-2005 Section 4.108-5 and Section 4.108-6.

Generation, transmission, and system loss charges, which are part of MERALCO's revenues are pass-through items. VAT on such revenues are remitted mainly to IPPs, PSALM and its successor generator companies, PEMC and NGCP, who are responsible for ultimate remittance to the BIR.



Input VAT

The amount of *VAT* input taxes claimed are broken down as follows:

	Amount (In Millions)
Balance at beginning of the year	₱832
Add input <i>VAT</i> on 2012 purchases from:	
Goods for resale/ manufacture or further processing	₱463
Capital goods subject to amortization	430
Services lodged under other accounts	1,438
	2,331
	3,163
Less input <i>VAT</i> claimed:	
From goods other than capital goods and services	1,901
Amortization of <i>VAT</i> input tax on capital goods	342
	2,243
Balance at end of year	₱920

MERALCO also applied against its Output *VAT* the amount of *VAT* withheld on payments to non-residents for services rendered in the Philippines of ₱5.4 million which are duly supported by *BIR* Form 1600.

Documentary Stamp Tax or DST

In 2013, *MERALCO* issued bonds totaling to ₱18.5 billion and entered into other transactions subject to *DST*. *DST* paid in 2013 amounted to ₱14 million. The related *DST* of the bonds issued amounting to ₱92.5 million was paid in January 2014.

Withholding Taxes

The amount of withholding taxes in 2013 amounted to the following:

	Amount (In Millions)
Creditable withholding taxes	₱8,063
Tax on compensation and benefits	1,952
Expanded withholding taxes	2,348
Final withholding taxes	178

Tax Assessments

MERALCO does not have any pending assessments for deficiency taxes as at December 31, 2013.

Tax Cases

MERALCO's tax cases as at December 31, 2013 are discussed in *Note 28 – Contingencies and Legal Proceedings*.



33. Supplementary Information Required Under Revenue Regulations No. 19-2011

In compliance with the requirements set forth by *RR* No. 19-2011, following are the information on taxable income and deductions during the taxable year 2012 (*Amounts in millions*):

Taxable Revenues

Sale of electricity	₱292,251
Lease income	550
	₱292,801

Cost of Services

Purchased power	₱235,920
Depreciation and amortization	3,632
Salaries, wages and employee benefits	2,130
Contracted services	1,375
Inventories	178
Utilities	173
Transportation	84
	₱243,492

Taxable Other Income

Gain on sale of scrap	₱147
Rental income	82
Others	290
	₱519

Itemized Deductions

Salaries, wages and employee benefits	₱10,139
Contracted services	2,591
Interest	1,360
Depreciation and amortization	906
Taxes, fees and permits	507
Rent and utilities	300
Insurance	291
Inventories	115
Transportation and travel	157
Corporate expenses	131
Bad debts	74
Others	957
	₱17,528

Taxes, Fees and Permits

ERC supervision and permits fees	₱260
Customs duties	120
Real property taxes	91
Fees, permits and licenses	19
Documentary stamp taxes	14
Fringe benefits taxes	3
	₱507



34. Event After the Reporting Date

On March 17, 2014, the *BOD* declared a final cash dividend of ₱6.45 per share to all shareholders of record as at April 15, 2014, payable on May 8, 2014.

