RE-ENERGIZED

MERALCO

2010 ANNUAL REPORT

Contents

R E - E N E R G I Z E D

After a stellar year, Meralco is re-energized and ready to pursue new opportunities that will accelerate growth in the long-term. Despite unprecedented challenges in the past, we have prevailed, and more importantly, thrived. Thanks to the support of our shareholders and our unwavering faith in the corporate values that have sustained us through the years. We look forward to a brighter future strengthened by our strategic pillars and the extraordinary commitment of our leadership. An empowered, enlightened Meralco is ready to seize it.

A new day has come.

Our Company

Meralco marches on to its 108th year of service in 2011. Consistently in the list of the Philippines' top five corporations and cited among Asia's finest, Meralco today serves over 4.8 million residential, commercial and industrial customers. It is strategically located to serve the country's center of commerce and industry and its hub of government services and infrastructures. It services about 30 manufacturing economic zones, which also compete in the global market. Likewise, the Company caters to providers of outsourced business processes, both domestic and international.

Meralco's 9,337 sq. km. franchise area covers 31 cities and 80 municipalities including Metro Manila, the entire provinces of Bulacan, Rizal and Cavite; parts of the provinces of Laguna, Quezon, Batangas and Pampanga. Electrification level in the franchise area is 99%.

The franchise area is home to 25.5 million people, roughly a quarter of the entire Philippine population of 94 million, for whom it commits to deliver adequate, reliable, quality and affordable electric service 24 hours a day, seven days a week, year-round.

It is within Meralco's service area where almost half of the country's Gross Domestic Product (GDP) is produced, one-third from Metro Manila alone. Consequently, 54% of the total electricity usage in the Philippines, or almost three-fourths of all electricity used in Luzon, is consumed in the Meralco area.

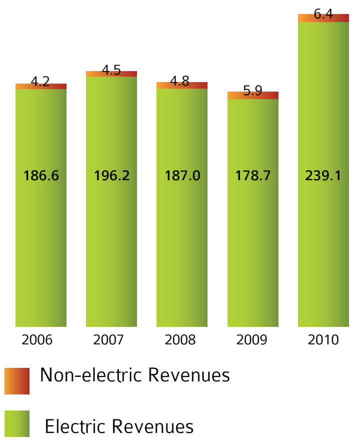
Meralco today is about extraordinary vision. The entry of new perspectives into the Company already has a significant impact on how we engage our markets, enhancing customer satisfaction at the same time providing new opportunities to create superior value for our customers, the community and the country.

Just as it has been for over a century, we continue to see Meralco as a partner for growth whose direct footprint in the communities and businesses we serve defines our continuing commitment to progress and nation-building.

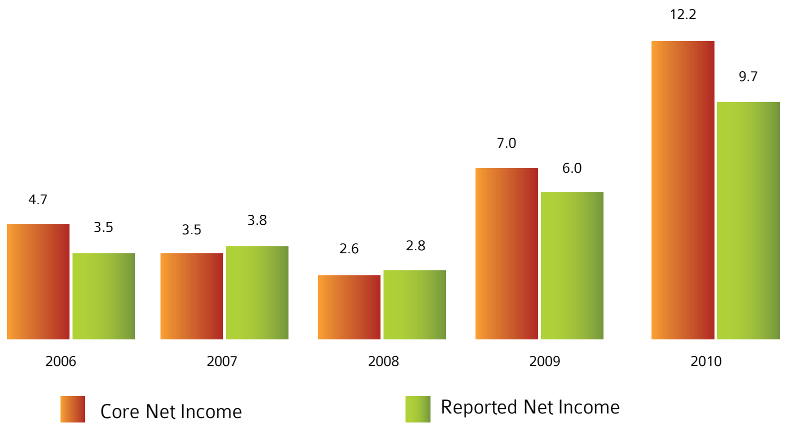
Financial and Operating Highlights

FINANCIAL INFORMATION (Amounts in Million except Cash Dividends Declared per Common Share)	2006	2007	2008	2009	2010
Revenues					
Electric revenues	Php 186,576	Php 196,171	Php 186,999	Php 178,686	Php 239,077
Non-electric revenues	4,211	4,522	4,776	5,864	6,384
	190,787	**200,693**	**191,775**	**184,550**	**245,461**
Costs and Expenses					
Purchased power	161,263	172,837	156,872	150,928	200,916
Depreciation and amortization	4,394	4,492	4,426	5,064	6,219
Operations and maintenance	10,908	13,180	13,351	13,611	15,711
Interest and other financial charges (income) - net	2,246	852	1,216	(918)	(2,197)
Others	(9,950)	3,239	10,710	6,886	10,375
	168,861	**194,600**	**186,575**	**175,571**	**231,024**
Net Income Attributable to Equity Holders of the Parent	3,465	3,759	2,800	6,005	9,685
Core Net Income	4,696	3,532	2,605	7,003	12,155
Utility Plant and Others					
Cost	135,910	141,036	146,313	152,359	156,240
Accumulated depreciation and amortization	44,194	47,340	50,609	54,128	55,231
Net book value	**91,716**	**93,696**	**95,704**	**98,231**	**101,009**
Capital Expenditures	6,099	6,869	9,175	8,890	9,053
Interest-bearing Long-term Financial Liabilities	16,015	16,291	16,359	21,303	21,072
Notes Payable	310	10,748	9,828	513	149
Equity Attributable to Equity Holders of the Parent	47,770	51,680	52,607	57,369	58,969
Cash Dividends Declared per Common Share	1.00	-	1.00	2.50	6.95
OPERATING INFORMATION					
Number of Customers	4,389,422	4,465,032	4,572,120	4,701,116	4,847,238
Energy Sales in GWh	25,078	26,219	27,049	27,516	30,247
Number of Stockholders	65,414	59,984	58,913	52,983	51,125
Number of Employees					
Electric	5,928	5,990	6,050	6,112	6,203
Non-electric	878	1,013	1,146	1,167	1,231

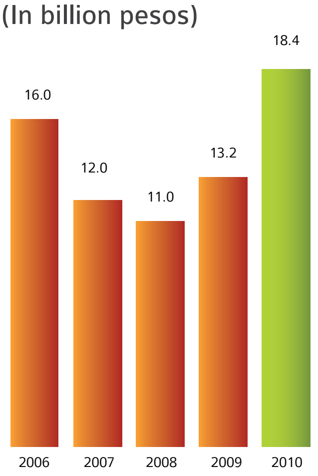
TOTAL REVENUES
(In billion pesos)



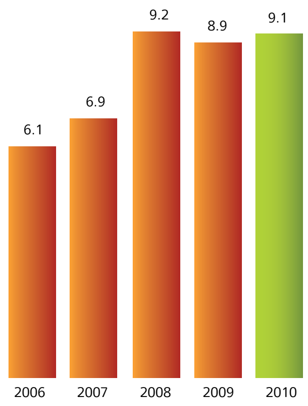
2006-2010 REPORTED/CORE NET INCOME
(In billion pesos)



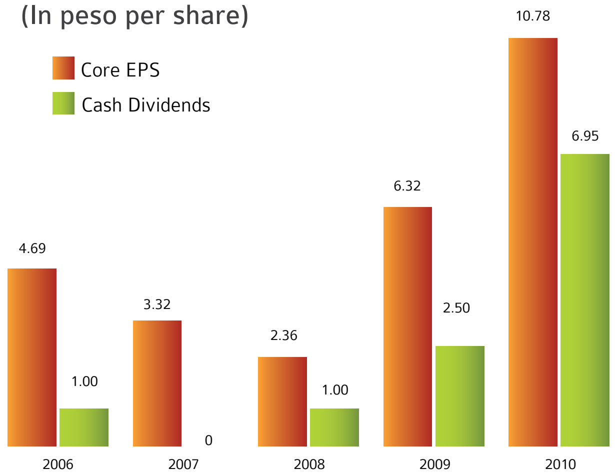
EBITDA
(In billion pesos)



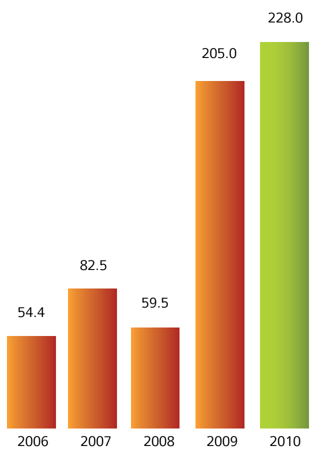
CAPEX
(In billion pesos)



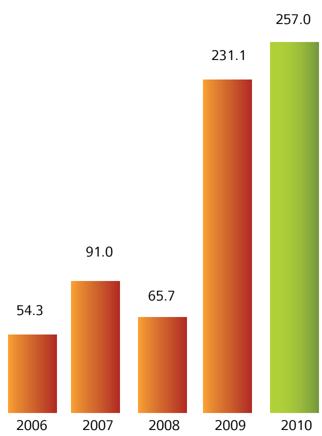
CORE EPS
(In peso per share)



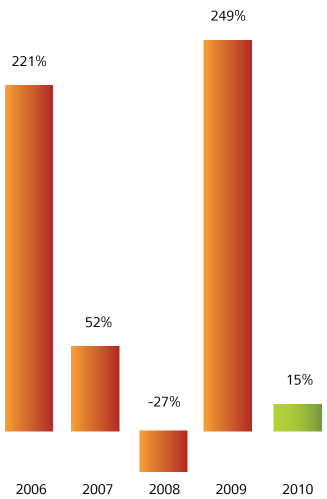
SHARE PRICE
(In peso per share)



MARKET CAPITALIZATION
(In billion pesos)



TOTAL SHAREHOLDER RETURNS
(In percentage)



Message from the Chairman

TO MY FELLOW SHAREHOLDERS,

Our Company's 2010 overall performance was another banner year. The industry we belong to has been known to be staid, stable and predictable. Meralco, our utility Company, has never been such. In its more than a century's existence, upheavals and changes have been our Company's experience.

Through them all, our employees' unwavering loyalty, management agility, organization strength and investor confidence have enabled and ensured continuous commendable customer service and a reliable distribution network performance.

As world economies recovered from the global economic slowdown, domestic businesses likewise improved, manifesting in our sales from all customer segments. Electricity sales registered the highest ever growth rate in the past five years. This upswing in power sales is clearly a demonstration of Meralco's critical role in nation-building, as the main contributors to this growth are our industrial and commercial customers, two segments that virtually give vibrance to the country's economic activities. Our distribution network ably supported this increasing demand, prepared as it has always been, with years of planning, design, maintenance and expansion of our substations and lines. Years of battling system loss has ensured continuous improvement in system loss level, benefitting our customers. The excellent performance is also evident in our Company's scoring very well in our major performance parameters vis-à-vis the standards set by the government-mandated Performance-Based Regulation (PBR).

The success of a utility lies with its strategic direction. Consistent execution of such long-term plans ensure the successful delivery of our Company's yearly commitments and targets. While our distribution business provides us with a sustainable growth pattern, our direction to go back to power generation, expand into new franchise areas and explore synergistic potentials, will propel our Company into a new growth level, further increasing our contribution to national development. MERALCO PowerGen Corporation, Meralco Industrial Engineering Services Corporation (Miescor) and its subsidiaries and, CIS Bayad Center, Inc. will be at the forefront of these plans.

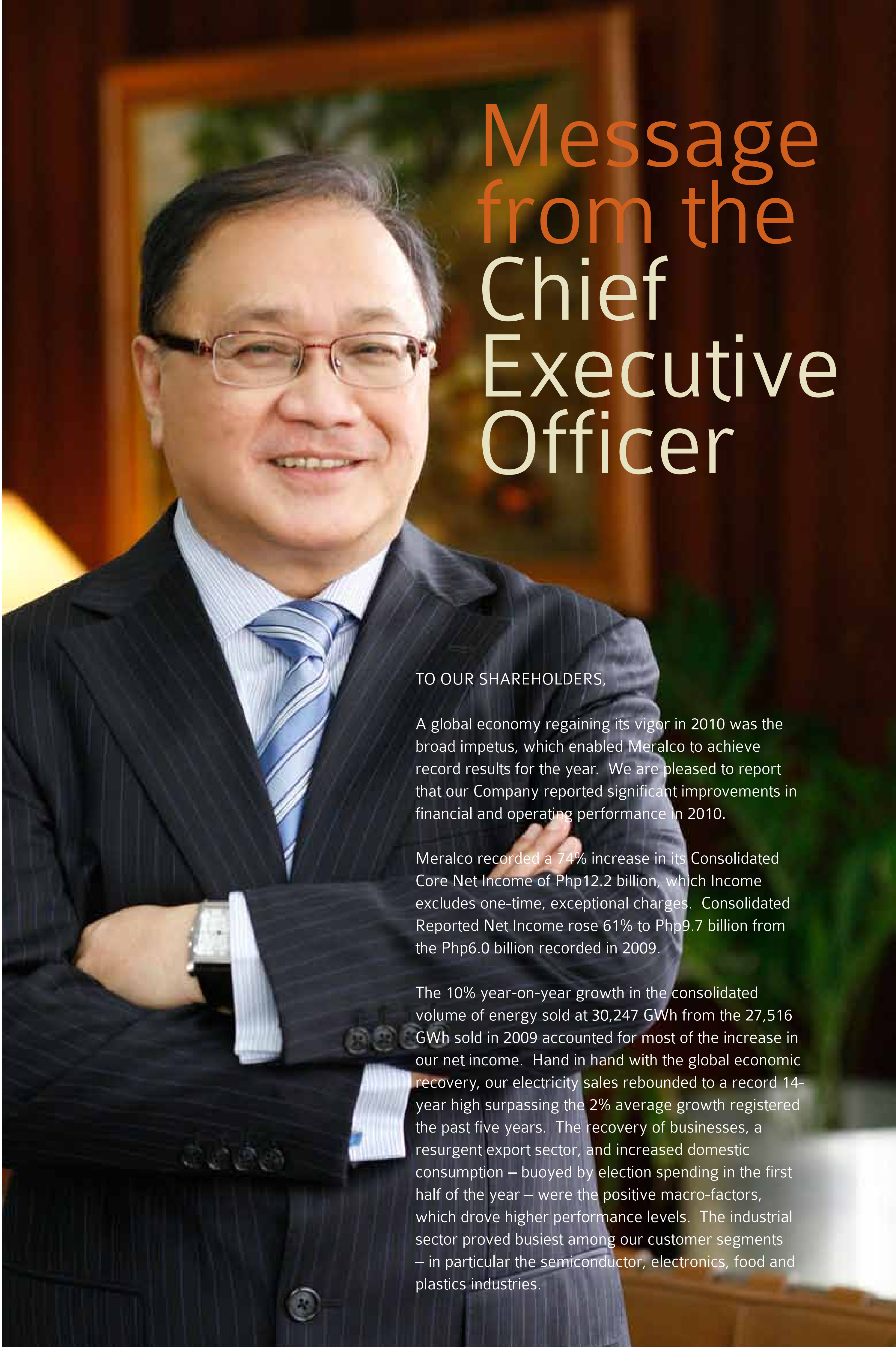
Meralco is fortunate that at various periods in the Company's history, the most apt management system is installed by its leaders. Our President and Chief Executive Officer, Mr. Manuel V. Pangilinan, is leading the Company into a new era of growth and diversity, to ensure adequate and reliable supply of power and continuous improvement in our customer service and processes.

Our efforts to further bolster products and services and enhance system reliability will be enriched by the knowledge and experience I am fortunate to have as Philippine Ambassador to Japan, a country that is a known vanguard of technological development and advancement. Our Company's gains will be the Philippines' as well, borne by Meralco's intrinsic role as a major contributor to nation-building. I am confident that we will be able to achieve our business pursuits and aspirations with the help of our determined and untiring work force, with whom I have worked for over four decades. Our employees made possible a strong institution, imbued with a spirit of service that is built on integrity and *malasakit*.

In closing, I would like to express my appreciation for the continued confidence and support of all our partners and stakeholders, as we work further together towards a more vibrant Meralco in energizing the development of this country.

MANUEL M. LOPEZ
Chairman

"Our Company's gains will be the Philippines' as well, borne by Meralco's intrinsic role as a major contributor to nation-building."



Message from the Chief Executive Officer

TO OUR SHAREHOLDERS,

A global economy regaining its vigor in 2010 was the broad impetus, which enabled Meralco to achieve record results for the year. We are pleased to report that our Company reported significant improvements in financial and operating performance in 2010.

Meralco recorded a 74% increase in its Consolidated Core Net Income of Php12.2 billion, which Income excludes one-time, exceptional charges. Consolidated Reported Net Income rose 61% to Php9.7 billion from the Php6.0 billion recorded in 2009.

The 10% year-on-year growth in the consolidated volume of energy sold at 30,247 GWh from the 27,516 GWh sold in 2009 accounted for most of the increase in our net income. Hand in hand with the global economic recovery, our electricity sales rebounded to a record 14-year high surpassing the 2% average growth registered the past five years. The recovery of businesses, a resurgent export sector, and increased domestic consumption – buoyed by election spending in the first half of the year – were the positive macro-factors, which drove higher performance levels. The industrial sector proved busiest among our customer segments – in particular the semiconductor, electronics, food and plastics industries.

Three factors further influenced our Company's record performance. These were the 3% percent rise in the number of our billed customers to 4.8 million, the implementation of the distribution rate adjustment under the Performance-Based Regulation (PBR) for the 3rd Regulatory Year of the 2nd Regulatory Period, and the significant savings in financing charges generated by the refinancing of its long-term debts with considerably lower interest rates.

Consolidated revenues rose 33% to Php245.5 billion in 2010 from Php184.6 billion in 2009. Our electricity sales accounted for 97% at Php239.1 billion, surpassing the Php178.7 billion attained in 2009. Of the total billed electricity, 68% represents pass-through generation costs and transmission costs, which averaged Php6.06 per kWh in 2010 – 16% higher than the Php5.24 per kWh billed in 2009.

The average distribution charge in 2010 was at Php1.44 per kWh. This included the rate adjustment under the 2nd Regulatory Period of the PBR implemented starting April 2010. The adjustment set the Maximum Average Price (MAP) at Php1.4917 per kWh for the Regulatory Year 2010.

Our other businesses, consisting of electro-mechanical engineering services and payment services, registered a modest increase for the year. Meralco Industrial Engineering Services Corporation (Miescor) generated service revenues from engineering contracts from both Government and private sector customers. Meanwhile, revenues of CIS Bayad Center, Inc. (Bayad Center), the country's pioneering brand leader in outsourced over-the-counter payment collection, rose as a result of the growth in the number of billers served and the higher number of transactions handled.

Our consolidated EBITDA stood at Php18.4 billion against the Php13.2 billion in 2009. EBITDA margin on distribution revenues was at 40%, reflecting the combined effect of higher energy sold and the accompanying distribution rate adjustment. The return on distribution assets was at 6% at the end of 2010 from 4% in 2009.

Our consolidated capital expenditures for 2010 amounted to Php9.1 billion with electric capital projects accounting for 57%, equivalent to Php5.2 billion. The 35 major and residual electric capital projects placed on stream further strengthened our electric system infrastructure, complementing the robust demand for adequate and uninterrupted power. Furthermore, the newly installed facilities contribute to our continuing effort at reducing system loss levels. Constituting the rest of our consolidated capital expenditures were the non-electric projects and other capital expenditures undertaken by our subsidiaries.

Consolidated free cash flows stood at Php6.5 billion for the year. Our cash position remains healthy. Average days-sales outstanding was at 24 days. Cash and cash equivalents in 2010 amounted to Php24.4 billion, 43% higher than 2009.

Our Company's excellent performance specifically in the areas of electricity sales and higher tariffs merited an upgrade in Meralco's Standard and Poor's credit rating to B+, with a 'Stable' outlook reflecting the significant and sustained improvement in the Company's financial risk profile.

Total cash dividend payout on Core Net Income amounted to 60%, representing a dividend yield of 3% on the market price realized on the last trading day of the year. This is consistent with our dividend policy of declaring regular dividends equivalent to 50% of core earnings, which may be supplemented by special dividends on a 'look back' basis.

Reinvigorated: One Team, One Meralco

Expectations have the inherent tendency to level up after a stellar year. While we choose to be cautious about our outlook for 2011, the presence of promising opportunities for Meralco provides continuing optimism. We have expressed our intent to return to power generation and to diversify into allied businesses. Our affiliation with the infrastructure businesses of the sector companies provides fertile ground for our products and services – existing and new – to grow into.

Meralco is an institution with a rich past and an auspicious future. As we reviewed our positions at the start of the year, we asked ourselves how we can build on these precious heritage and assets, and move the Company forward. What we must do and where we need to go are answered by the new business framework crafted precisely to shape the new Meralco.

First, we must focus on strengthening our core distribution utility business. Improving our efficiencies is for us a continuing agenda because of our customers' growing requirements and enduring need for reliable, quality, efficient and affordable service. The upgrading and expansion of our electric distribution system is a constant program to keep in step with current needs and provide for the future requirements of our customers. The direction to strengthen the core business also requires a refreshed organization and people with renewed vigor.

Second, we must pursue the expansion of our franchise. We want to bring the benefits of electricity to and share the Meralco brand of service with more Filipinos situated beyond our area of coverage.

Third, we must create a vertically-integrated business model with our entry into the power generation business. Our participation in generation should help alleviate the anticipated supply predicament as reserves from existing power plants tighten. This, too, will enable us to manage the perennial concern about high power rates. Our power generation portfolio carries with it a goal of building an aggregate capacity of 1,500 MW at a total estimated cost of approximately $2.3 billion over the next five years. This is a diverse package potentially consisting of baseload coal-fired power plant, liquefied natural gas and aeroderivative gas turbines that adopt the high-efficiency capabilities of aircraft engines for peaking requirements.

Fourth, as the market enters the era of open access, we must be the retail electricity supplier of choice, with specific expertise on sourcing and knowledge of specific energy requirements of every customer.

Fifth, we must place more attention on the growth prospects of our subsidiaries and affiliates. We want to harness their potential so that these can play their part in contributing to the overall growth and profitability of Meralco.

Anchoring these five focus areas are what we refer to as the seven growth pillars, which can fulfill the goal of growing our distribution utility business, of achieving the vertical integration of that business, to make ready for open market access, and of ensuring the growth of our subsidiaries and affiliates. We will report to you how all these efforts are progressing in our future Annual Reports.

It goes without saying that the growth pillars cannot be achieved without our employees being inspired and informed with a new set of corporate values revolving around customer service, performance, accountability/ empowerment, integrity/transparency, teamwork/ collegiality, malasakit and makabayan.

We see the interplay of the five focus areas, the seven growth and profitability pillars and the seven corporate values as molding the service excellence we want for our 3C's - Customer, Community and Country. And, as well, in achieving the collateral goal of ***One Team, One Meralco***.

The Road Ahead

The future we seek to shape likewise offers the imperatives of innovative technology and services. The two-way digital communication capability of the Smart Grid is one technological application our customers can look forward to. This new generation electricity network has the potential to create new products and services, elevate energy reliability and efficiency and eventually, help bring down costs. Likewise, it offers our customers a full-automation experience never before felt. This and similar undertakings help us fulfill a vision that transcends the limiting borders of electric distribution – to be our customers' energy solutions company.

The future will also see the fruition of our new strategy on Corporate Social Responsibility (CSR) that is more focused and more aligned with our business mission. We want to ensure that our CSR activities will directly affect the Customer, the Community and the Country through four means – Rural/Missionary Electrification, Grassroots Partnership, Sports and Youth Advocacy, and Disaster Relief and Emergency Preparedness (more on our new CSR on page 44 of this Report).

In closing, I would like to thank the members of our Board of Directors for their guidance as we chart a better future for all. My deep gratitude too goes to our employees and staff who were instrumental in surpassing the self-imposed goals and targets in 2010, and for being resilient amidst tough circumstances.

And finally to our shareholders, for their continued faith in and support for the Company on to its 108th year of service to the nation.

MANUEL V. PANGILINAN
President and Chief Executive Officer

Powering up to success:
Shaping the new Meralco

Report of the Chief Operating Officer

2010: FAVORABLE SETTING FOR EXCEPTIONAL GROWTH AND PROFITABILITY

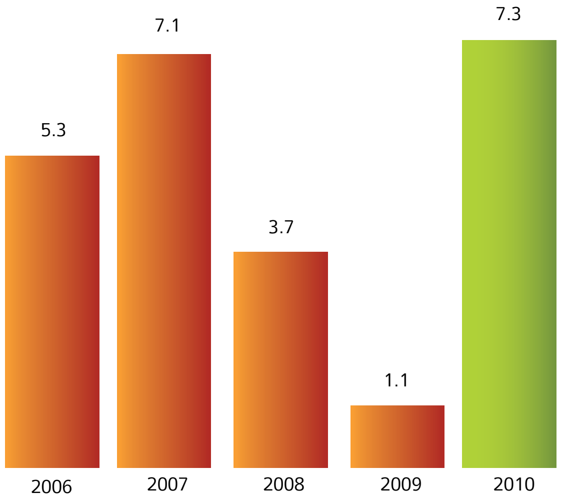
The year 2010 provided a conducive climate for exceptional sales, operating and financial performance for our Company. A strong economy, the El Niño effect and the low inflation and interest rates influenced these record results.

Strong Economy

A resurgent Philippine economy with a 34-year high 7.3% GDP growth from 1.1% in 2009, a global economic recovery to a growth rate of 5% from the financial crisis-induced contraction of 0.6% the preceding year; and an unusually long and warm weather served to fuel high industrial, commercial and residential consumption of electricity.

Overseas Filipino remittances and Business Process Outsourcing (BPO) revenues rose to US$18.1 billion and US$8.9 billion, respectively, boosting domestic consumption and investment expenditures. National elections spending and an orderly handover of government to a new administration following the country's first automated elections brought renewed optimism and triggered an increase in foreign investment inflows, which further underpinned healthy growth in the real economy and the financial markets. A buoyant commercial and residential real estate market was a prominent feature of the economy in 2010.

GROSS DOMESTIC PRODUCT (GDP)
(Growth rate in percentage)



"The year 2010 provided a conducive climate for exceptional sales, operating and financial performance for our Company."

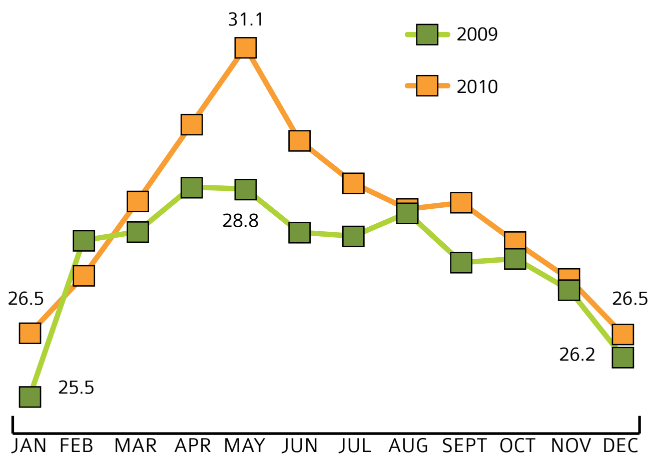
Warm Weather

The onset of El Niño in early 2010 caused temperature to rise and led to an abnormally high demand for electricity across all customer classes for an extended period during the year. Power consumption for air-conditioning, refrigeration services and other cooling appliances rose to levels significantly higher than in previous years.

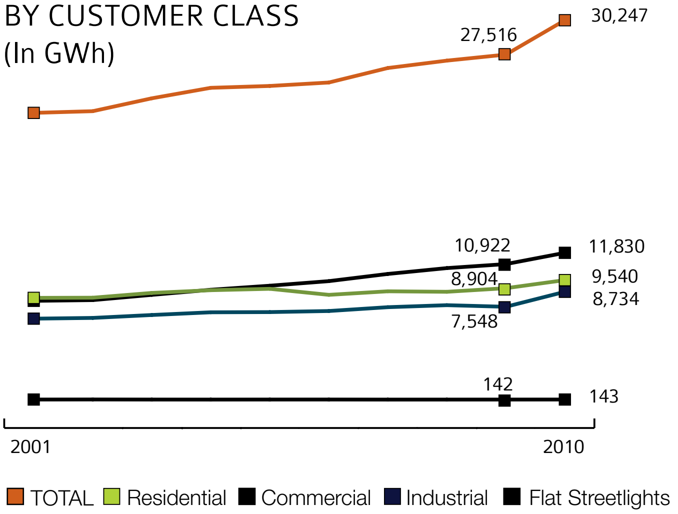
However, this cyclical weather condition also resulted in very low water elevation in the country's major reservoirs for power generation, bulk water and irrigation. Constrained hydro-electric power generation, along with non-scheduled repairs and maintenance downtime at certain power generating plants, and continued constraints in the transmission system caused occasional power supply shortages.

Periodic deficiencies in reliable power supply began as early as January 2010, due to equipment failure, preventive maintenance work and fuel supply issues in a number of power generating plants. In addition, two major typhoon disturbances, Typhoon *Basyang* in July and Typhoon *Juan* in October, affected the Meralco franchise area and disrupted power service. Typhoon *Basyang* directly hit the franchise area in July and caused the tripping of National Grid Corporation

AVERAGE TEMPERATURE
(In °C)



ENERGY SALES
BY CUSTOMER CLASS
(In GWh)



of the Philippines (NGCP) transmission lines linking the Northern Luzon and Southern Luzon plants. This immediately resulted in a total system collapse and a Luzon-wide blackout on July 14, 2010. As a result, customers in the franchise and the rest of the Luzon Grid experienced a number of manual load dropping or brownout incidents and electricity price spikes during certain months, both serving to dampen an otherwise much higher power demand.

Low Inflation and Interest Rates

Rounding out the favorable external influences on the Company's performance in 2010, was inflation which remained benign at 3.8% p.a., albeit somewhat higher than the 2009 level of 3.2% p.a. Interest rates also remained low, as the Bangko Sentral ng Pilipinas did not see the need for any urgent policy rate change, even as central banks in a few economies started to signal an upward moderate move in policy rates. The low inflation and interest rates helped contain operating and financing costs in 2010.

RECORD ENERGY SALES

The confluence of significantly better economic performance, locally and globally, the unusually warm weather, and the efficient response of Meralco's distribution system and its organization to contain power supply challenges posed by generation and transmission constraints, were important factors in achieving this sales performance.

Energy sales volume grew to a record 10% in 2010, the highest ever recorded in 14 years since 1996, which also outpaced the growth of the preceding five years averaging at around 2%.

Consolidated energy sales, which includes energy sales of Meralco's majority-owned Clark Electric Distribution Corporation (CEDC), reached 30,247 GWh in 2010, up from 27,516 GWh in 2009. This is equivalent to 75% of the total Luzon Grid energy sales of 40,519 GWh and 56% of the total Philippine energy sales of 54,441 GWh. Broken down by customer class, Commercial Sales accounted for 39%, Residential Sales contributed 32% and Industrial Sales added 29%.

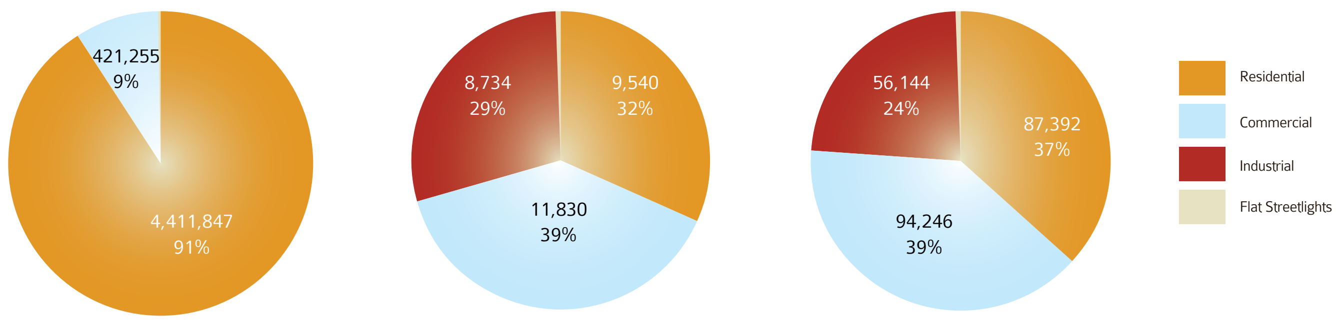
Sales to the Industrial market segment led the growth in total energy sales, rising by an impressive 16% from 7,548 GWh in 2009 to 8,734 GWh in 2010. Principal growth drivers were electrical machinery (particularly semiconductor companies), food, manufacturing and plastic products.

Sales to the Commercial segment grew by a healthy 8% from 10,922 GWh in 2009 to 11,830 GWh in 2010. Real estate (particularly commercial malls), private services (primarily BPOs, call centers and office buildings) and communications, transport and storage figured prominently in the growth of the Commercial segment.

CUSTOMER COUNT

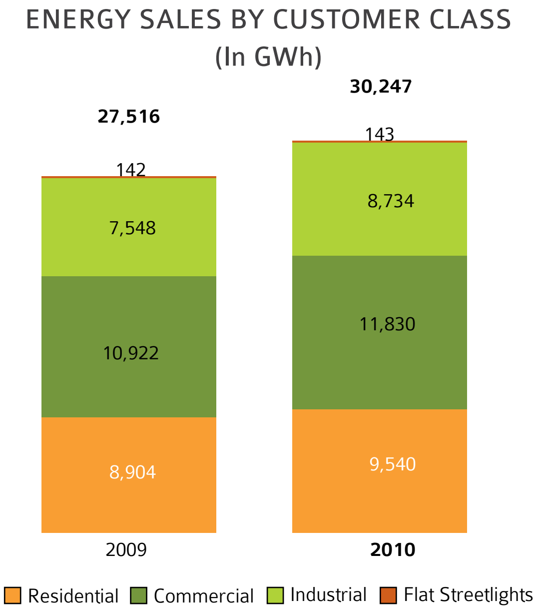
SALES in GWh

SALES IN MILLION PESOS



Industrial customers (9,879) and flat streetlights (4,217) collectively account for less than 1% of the total customer count.

Sales volume of energy sold (143 GWh) and its peso equivalent (Php1,295 million) for flat streetlights account for less than 1% of the respective totals.



Residential sales rose by 7% from 8,904 GWh in 2009 to 9,540 GWh in 2010, as a much warmer climate pushed household consumption of electricity, with heavier usage of air-conditioning, refrigeration and cooling appliances.

Contributing to the record growth of 10% in GWh sales in 2010 was the sustained increase in the number of customers of our Company. Meralco customers increased by 3% to 4,847,238 in 2010 from 4,701,116 in 2009. This rate of increase is higher than the 2% average during the preceding five years.

Residential customers constituted 91%, numbering 4,411,847 in 2010, up by 3% over 4,276,701 in 2009. They contributed 32% to the total energy sales volume. Of the Residential customers, 48% or 2,120,902 are lifeline subsidy customers consuming 100 kWh or less per month.

Semiconductor firms SunPower Philippines Manufacturing Ltd. and Rohm Electronics Philippines, Inc. greatly contributed to Meralco's total energy sales volume in the industrial segment.

Residential customers contributed 32% to the total energy sales volume.

Our electric service helps move people: spanning from North EDSA to Taft Avenue, the Department of Transportation and Communications (DOTC) - Metro Rail Transit Corporation provides efficient mass transport system to the daily commuters of the metropolis.

Commercial customers numbered 421,255 in 2010, up by 3% over the 2009 count of 410,274. This comprised 9% of the total customer count but accounted for 39% of total energy sales volume.

Industrial customer count was at 9,879 in 2010. Although small in number, industrial customers contributed 29% to Meralco's energy sales volume in 2010.

Consumption across all customer classes increased during 2010 with volume of Industrial customers reflecting the higher increase at 17% followed by Commercial at 6% and Residential at 40%.

CORRESPONDING GROWTH IN NET SYSTEM INPUT AND PEAK DEMAND

With Meralco energy sales growing to 30,247 GWh in 2010, Net System Input (NSI) rose by 9% to 32,925 GWh in 2010 from 30,173 GWh in 2009. The lower rate of increase in NSI relative to total energy sales is indicative of the further gains in System Loss reduction.

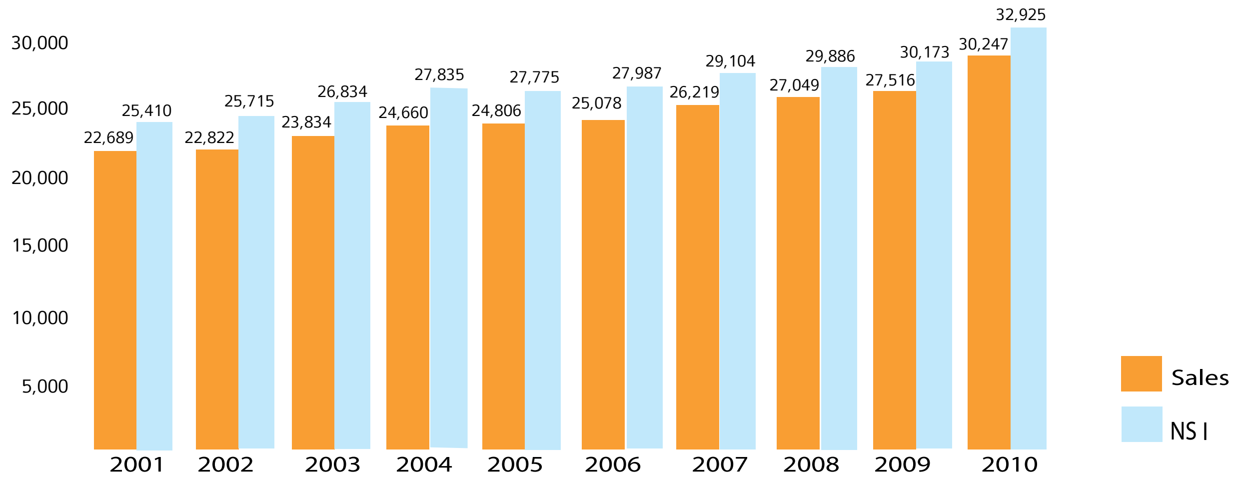
Peak demand during the year was at 5,374 MW, registered on May 26, 2010. This was 9% higher than the peak demand of 4,910 MW in 2009.

ROBUST OPERATIONAL PERFORMANCE

Complementing the exceptional energy sales performance, the Company's operational performance also reached record levels in 2010 and outperformed most of the regulatory standards set by the Energy Regulatory Commission (ERC) for the relevant regulatory period.

System Loss, System Reliability and Availability performance in 2010 were outstanding. System Loss was maintained well below the new cap of 8.5% for 2010 and showed a significant improvement over 2009, with December 2010 at 7.94% against 8.61% in December 2009.

GROWING NET SYSTEM INPUT AND ENERGY SALES
(In GWh)

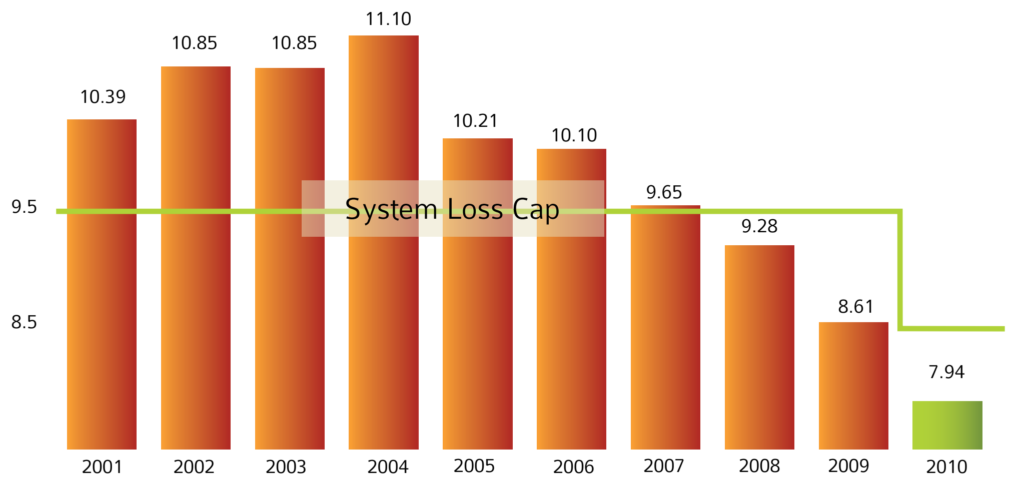


System Reliability, measured in terms of the Interruption Frequency Rate (IFR) (forced and pre-arranged), continued to improve to a new low of 4.73 times in 2010. System Availability, measured in terms of forced and pre-arranged Cumulative Interruption Time (CIT), similarly improved to new lows of 3.30 hours and 1.61 hours, respectively.

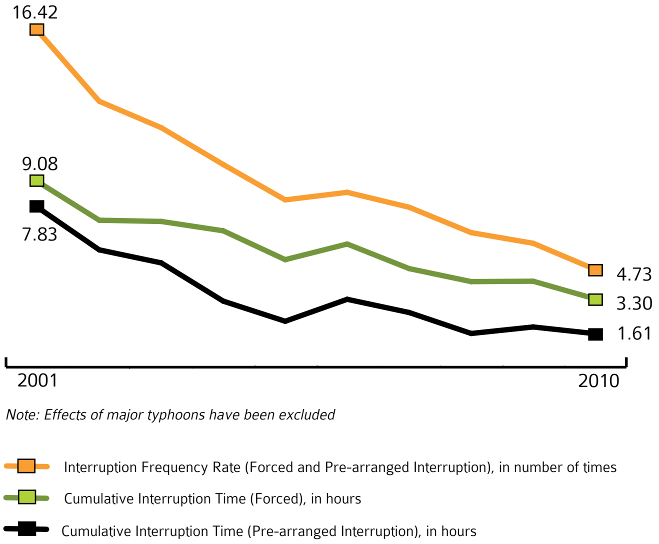
Integral components of the ERC's Performance Incentive Scheme (PIS) are the S-Factor and the Guaranteed Service Levels (GSL). These are the indicators against which the Company is measured. For 2010, the Company outperformed seven out of eight S-factor indicators while one was within the limits set by the regulator, incurring no penalties. Four GSL indicators were likewise within limits set, incurring no penalties.

The continued improvements in system loss, reliability and availability performance are the result of: (1) continuing major investments in Meralco's distribution system and customer service infrastructure; (2) disciplined implementation of Networks performance and system loss management processes and procedures; and (3) close cooperation and coordination with customers, local government units (LGUs) and police agencies. These contributed to contain and reduce technical and non-technical losses.

RECORD-LOW SYSTEM LOSS LEVEL
(In percentage)



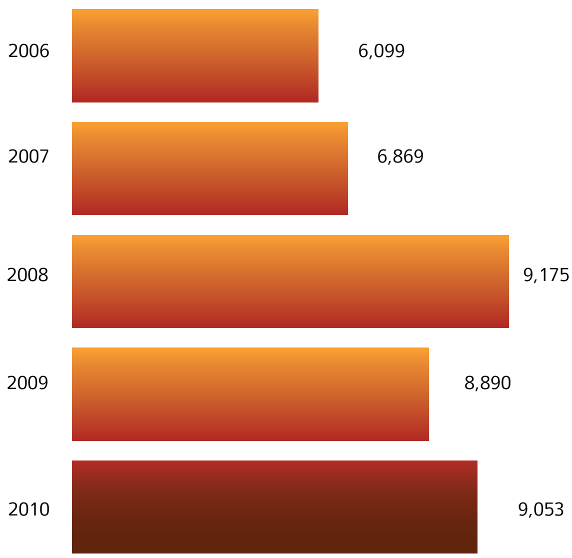
IMPROVED SYSTEM RELIABILITY/ AVAILABILITY PERFORMANCE



Note: Effects of major typhoons have been excluded

CONTINUING INVESTMENTS (CAPITAL EXPENDITURES)

(In million pesos)



CAPITAL EXPENDITURES

The Company continues to invest heavily in electric capital projects, customer service facilities and other distribution service capital expenditures. These investments are geared to: (1) meet increasing power demand from new and existing customers; (2) enhance the robustness of Meralco's power distribution network for better reliability and quality of power services; (3) contain system loss; and, (4) improve operating and customer service efficiencies.

Project Name	Commissioning Date
Substation Construction	
Expansion	
Central Business Park Island-A Gas Insulated Switchgear (GIS) Substation	January 15, 2010
BF Parañaque Substation	February 25, 2010
Balintawak Delivery Point Substation Phase 1 (115kV)	March 26, 2010
Balintawak Delivery Point Substation Phase 2 (230kV)	
Paco Modular Substation	April 30, 2010
Dolores Substation	May 28, 2010
Batangas City Substation	May 31, 2010
Development	
Tagaytay West Substation	June 29, 2010
Fort Bonifacio Global City (FBGC) GIS Substation Sub-Transmission Lines	October 15, 2010
FBGC GIS Substation	
Marilao Substation	December 15, 2010
Veinte Reales Substation	December 21, 2010
Sub-Transmission Line Construction	
Laguna International Industrial Park - ROHM Electronics 115kV Line	April 29, 2010
Amadeo-Tagaytay West 115kV Line	June 29, 2010
Tagaytay West-Tagaytay 115kV Line	August 12, 2010
Looping of Dasmarinas and Amadeo Substation thru Silang-Tagaytay West Line	October 26, 2010
NAIA 115kV Line	November 19, 2010
Uprating of Kaybiga-Novaliches 115kV Line	December 22, 2010

Total capital expenditures in 2010 amounted to Php9.1 billion, an increase of 2% over the 2009 capital expenditures of Php8.9 billion. The majority of these investments have been for electric capital projects.

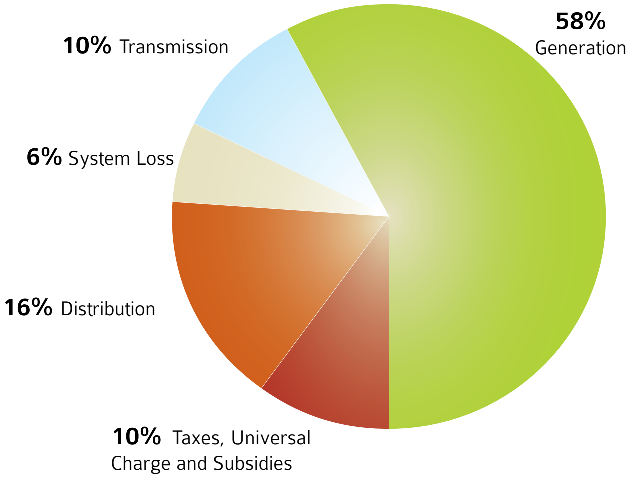
CUSTOMER BILL

The average customer bill across all customer classes amounted to Php8.94 per kWh in 2010, a 17% rise over the average bill of Php7.65 per kWh in 2009.

The largest component of the Meralco bill is the Generation Charge, constituting 58% of the total bill at Php5.19 per kWh in 2010. Meralco's distribution charge accounted for 16% of the average bill at Php1.44 per kWh. Taxes, Universal Charge and Subsidies contributed 10% of the bill at 89 centavos per kWh. Transmission Charge of 87 centavos per kWh, and system loss of 55 centavos per kWh was 10% and 6% of the total average bill, respectively.

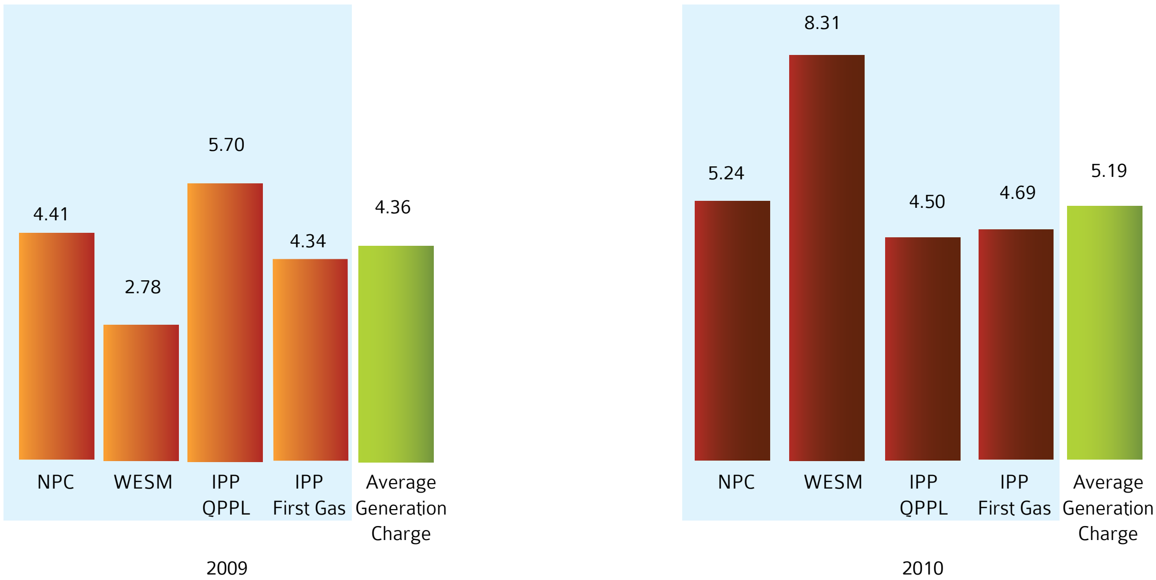
The Company is actively pursuing major initiatives aimed at containing and potentially reducing the Generation Charge component of customer bills, and assuring adequate power supply for Meralco customers. Discussions are underway with various power generation companies for long-term bilateral power purchase contracts with competitive prices and terms. These are intended to replace current transition supply contract before or when it expires. New bilateral power purchase contracts will be referred to the Energy Regulatory Commission (ERC) for approval.

AVERAGE CUSTOMER BILL COMPONENTS



The Company has also stated its strategic intent to re-enter into power generation. It has formed a new subsidiary, MERALCO Powergen Corporation, and has a strong management team on-board to develop a portfolio of new cost-competitive baseload, mid-merit and peaking power generating plants with an aggregate capacity of 1,500 MW, with potential strategic partners. These are intended to enhance the Company's ability to provide adequate, reliable and affordable power and to contain the Generation Charge to customers in the franchise area.

GENERATION COST AND CHARGE
(In pesos per kWh)



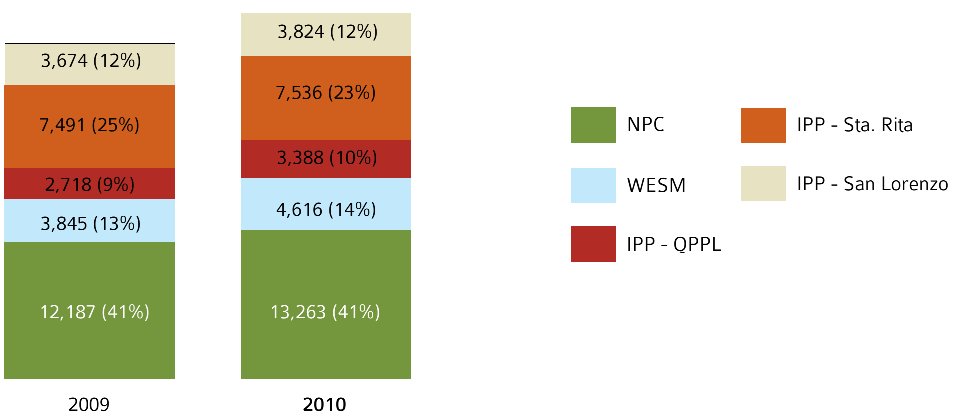
PURCHASED POWER AND GENERATION CHARGE

Meralco sources power from (1) Independent Power Producers (IPPs) with whom the Company has long-term Power Purchase Agreements (PPAs); (2) National Power Corporation (NPC); and (3) the Wholesale Electricity Spot Market (WESM). Meralco's main IPPs are First Gas Power Corporation and FGP Corp. with their 1,000 MW Sta. Rita and 500 MW San Lorenzo (collectively known as First Gas) combined cycle gas plants in Batangas, respectively; and Quezon Power (Philippines), Limited Co. (QPPL) with its 460 MW coal-fired power plant in Mauban, Quezon.

In 2010, Meralco sourced 45% of its Net System Input of 32,643 GWh from its contracted IPPs, 41% from NPC transition supply contract (TSC), and 14% from the WESM, compared to 46%, 41%, and 13% from the same sources, respectively, in 2009.

The average Generation Charge for power purchased from these various sources was Php5.19 per kWh in 2010, a hefty increase of 19% over the average Generation Charge of Php4.36 per kWh in 2009. The WESM cost spiked from a low of Php2.78 per kWh in 2009 to Php8.31 per kWh, close to a 200% increase in 2010. Purchased power under NPC TSC had an average Generation cost of Php5.24 per kWh in 2010, up by 19% from Php4.41 per kWh in 2009. Meralco IPPs proved to be the most cost-effective source with the Generation cost from the First Gas natural gas-fired plants averaging Php4.69 per kWh in 2010, an increase of 8% over Php4.34 per kWh in 2009. QPPL's average Generation cost decreased by 21% from their high of Php5.70 per kWh in 2009 to Php4.50 per kWh in 2010.

POWER SUPPLY MIX
(In GWh)



The power purchased from other IPPs of 17 GWh and 7 GWh in 2010 and 2009, respectively, represent less than 1% of the total purchased power for both years.

REGULATORY DEVELOPMENTS

Starting January 2010, the maximum level of system loss that the ERC allows a private distribution utility to pass on to its customers was lowered to 8.5% from the previous cap of 9.5%. Since the Company managed to operate below this new system loss cap of 8.5% in 2010 due to the disciplined implementation of its system loss management program and related capital and operating expenditures, this lower cap did not result in unrecoverable purchased power cost to Meralco. The improved system loss performance also benefitted customers.

On April 22, 2010, the Expanded Senior Citizens Act of 2010 took effect, granting (1) registered senior citizens with a monthly consumption not exceeding 100 kWh a minimum 5% discount on their monthly electric bill; and (2) senior citizens center and residential care/group homes a discount of 50% on their monthly electricity bill. The related Implementing Rules and Regulations (IRR) were issued by the ERC on January 5, 2011 and took effect on January 22, 2011.

On May 1, 2010, the applicable distribution rate of Php1.4917 per kWh for the 3rd Regulatory Year (July 1, 2009 to June 30, 2010) of the 2nd Regulatory Period (July 1, 2007 to June 30, 2011) was finally implemented. This provided the Company an increase of 26.9 centavos per kWh over the previous rate of Php1.2227 per kWh approved for the 2nd Regulatory Year of this Regulatory Period.

On June 18, 2010, Meralco filed with the ERC its Application for the Approval of its Annual Revenue Requirement (ARR) and PIS for the 3rd Regulatory Period (July 1, 2011 to June 30, 2015). On December 6, 2010, the ERC approved Meralco's distribution rate of Php1.6464 for the 4th Regulatory Year (July 1, 2010 to June 30, 2011) of the 2nd Regulatory Period, which was implemented in the January 2011 billing cycle.

On February 18, 2011, the ERC issued an Order setting the dates of public hearings for the purpose of determining whether Open Access and Retail Competition (OARC) may already be declared. The initial hearing was set on March 7, 2011. OARC will be implemented upon compliance with the conditions of the EPIRA under Section 31, provided, the necessary rules, infrastructures and systems are in place. Under the first phase of the OARC, customers with a 12-month average peak demand of 1 MW and above, considered contestable customers, will be allowed to contract and procure their electricity supply directly from Retail Electricity Suppliers (RES). Meralco, as the distribution company in the franchise area, will continue to wheel their electricity at the approved distribution rate.

CUSTOMER-CENTRIC SERVICE

Gains in the Company's 2010 service performance were best manifested by the growth in energy sales and customer count, coupled by its strong performance against regulatory metrics related to customer experience.

Closer interaction with customers, proactive communication as well as new and innovative service and product offerings translated to positive customer feedback. However, the higher cost of electricity in 2010 relative to 2009, primarily due to increased cost of purchased power dampened an otherwise higher level of customer satisfaction.

"Gains in the Company's 2010 service performance were best manifested by the growth in energy sales and customer count, coupled by its strong performance against regulatory metrics related to customer experience."

On its way to achieving a more customer-centric Company, Meralco recast its customer segmentation into the Corporate Business Group, Small Medium Enterprise (SME) and Home & MicroBiz. More focus on these segments enables Meralco to understand its customers better and create customized, more responsive products and services.

Among the service offerings are rate options to qualified commercial and industrial consumers through the Customer Choice Program (CCP). An online simulator, an application in the Meralco website, allows qualified customers to explore alternative pricing-options. Customers who availed of the program grew by 21% from 3,293 in 2009 to 3,975 in 2010. Other customer service initiatives enhanced the level of customer experience. The Business Centers underwent renovation to provide more convenience and comfort. The Business Center Look Enhancement Program involves the renovation of façade and lobby of 30 business centers and seven auxiliary offices.

Another venue to bring service closer to customers is the Meralco Consumer Assistance Office (MCAO). The MCAO is the first ancillary office of any distribution utility to work closely with the ERC in providing customer service with cost effective and enhanced service delivery. Located in the same building where the ERC is situated, this one-stop shop makes Meralco service more accessible.

Complementing these avenues to elevate customer experience are services that include the Meralco Mobile Services (MMS), a partnership with Smart Communications, Inc. The MMS is a communication tool that connects customers with Meralco anytime, anywhere. Through this new service offering, launched in August 2010, customers receive broadcasts of pre-arranged power interruption schedules, emergency interruptions and typhoon-related safety tips, as well as business center contact numbers and a facility where customers can send feedback, queries, reports and messages to Meralco. Further work is being done to explore the potential for expanding the service. The Meralco Appliance Calculator (MAC), a web-based program, helps our customers manage their electricity consumption since they are able to estimate their electricity costs when operating common appliances. The program has been enhanced to allow for more mobile applications.

Meralco continues to explore the Smart Grid and Smart Metering applications as a way of integrating technology and the electricity distribution business. It is envisioned to overlay the electrical system with information and metering system using digital technology and provide more value to customers and more efficient operations for the Company.

In line with the campaign to promote energy efficiency, Meralco continuously provides expertise in the assessment and evaluation of energy efficiency projects and conducts energy audits for its customers. Company representatives hold seminars and lectures in industry forums and gatherings, appear in television and radio programs to impart energy efficiency pointers to the public. In 2010, Meralco released ads in radio, print and television on energy efficiency tips for common home appliances.

The year 2010 was not without challenges where service to customers was concerned. Towards the middle of July, major disturbances occurred one after the other, including the wrath of typhoon *Basyang* and the system blackout that followed due to a transmission system failure. The Business Continuity Management (BCM) Plan was activated to ensure that business operations and service to customers go unhampered during and after the calamity. Call Center and Business Center telephone hotlines were made available round the clock to receive reports of operating troubles, which were immediately relayed to the field crews who patiently repaired damaged facilities and restored power amidst bad weather conditions. The typhoon caused damage to 251 poles and hardware, 195 distribution lines and 132 line equipment. Notwithstanding the magnitude of the damage to our facilities, Meralco was able to restore 100% of the main circuits in two days and bring back power to our customers.

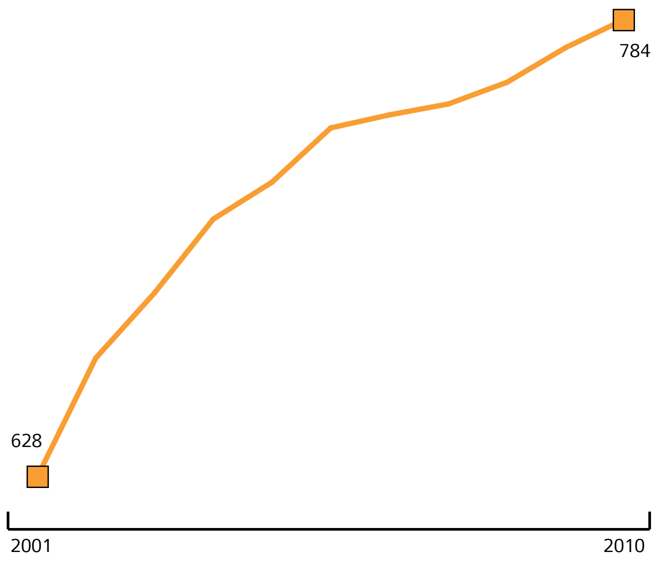
HUMAN RESOURCES

Major initiatives aimed at driving transformation towards a much higher performing organization were implemented in 2010. Three key Human Resources (HR) priorities and thrusts served to enable this process.

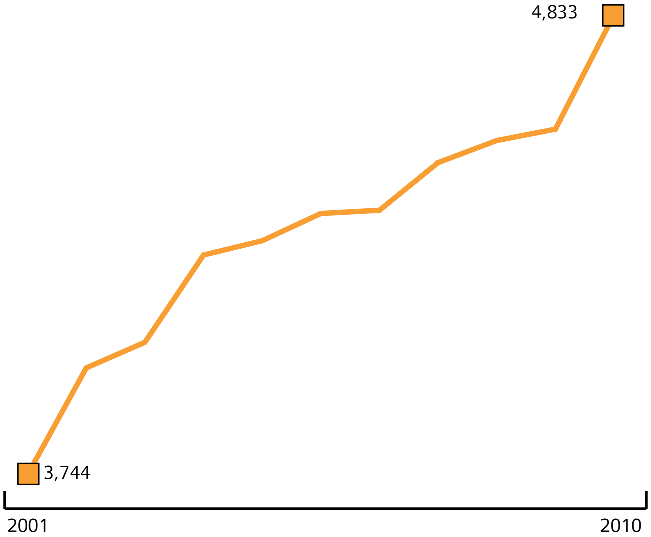
First, HR strategic partnerships with the business organizations through the (1) proactive organizational review and development leading to changes, particularly for critical functions and organizations, supportive of the new strategic initiatives and directions; (2) shift from seniority-based to a more performance based compensation plan that is aligned to the Company's annual and long-term strategic goals and targets; and (3) continuous process improvement through systematic challenging and questioning of our ways of working.

Second, is culture alignment through (1) management assimilation programs for senior leaders recently invited to join the Company; (2) employee development programs to accelerate competency development and personal growth; and (3) an enhanced set of Corporate Values, defined as Customer Service, Performance, Accountability/Empowerment, Integrity/Transparency, Teamwork/Collegiality, *Malasakit* and *Makabayan*.

CUSTOMER PER EMPLOYEE RATIO (CPER)



SALES* PER EMPLOYEE RATIO (SPER)



*In MWh

Third is the adoption of leading-edge HR practices resulting in employee engagement, and manpower productivity and development. This fostered harmonious relationships with the Company's employees which were highlighted by the successful completion of the collective bargaining agreements for both rank and file and supervisory unions in record time. Moreover, it yielded manpower efficiencies through value-creating outsourcing, work process improvements and employee capability development. In 2010, Meralco achieved its highest Customer per Employee Ratio (CPER) at 784 and Sales per Employee Ratio (SPER) of 4,833.

The highest levels of performance in safety and environment management are sustained through various seminars, programs and other interventions. In 2010, Lost Time Accident (LTA) frequency rate improved to 0.58% as we continued to instill environment, safety and health as a way of life. Dialogues with various Local Government Units (LGUs) were held to prevent/address public incidents involving our line facilities. Construction of Sewage Treatment Plants (STPs) in seven operating offices was fast-tracked for environmental compliance and impact mitigation.

The McKinley Cyberpark, a hub for BPOs, figured prominently in the growth of the commercial segment.

The Company continues to invest in electrical capital projects, customer service facilities and other distribution service capital expenditures such as the Fort Bonifacio Global City GIS Substation.

SUBSIDIARIES AND ASSOCIATES

Contributing to the favorable financial performance of the Company were the improved results of Meralco subsidiaries and associates in the power distribution, electro-mechanical construction and engineering services, real estate, financial services, including payments collection and non-life insurance; energy management services, technology facilities management and information technology services.

Aggregate revenues of subsidiaries amounted to Php7.3 billion in 2010, an increase of 9% over the previous year. Related costs and expenses were Php6.4 billion in 2010 against Php6.0 billion in 2009.

The top three contributors in the 2010 consolidated net income among subsidiaries were Rockwell Land with Php801.2 million, CEDC with Php110.3 million, and Miescor with Php109.1 million. Rockwell Land's net income increased by 26% brought about by progress in the construction of its residential condominium projects led by One Rockwell. CEDC's net income was up by 33% in 2010 due to an increase in electricity sales by 12% to 271 GWh in 2010 compared with 241 GWh in 2009. Miescor's net income in 2010 was higher by 8% compared with Php100.9 million in 2009 due to higher revenues generated from electro-mechanical engineering contracts with the government and private sector customers.

Collectively, associates contributed Php282.6 million to the 2010 Reported Net income.

Corporate Governance

Corporate Governance (CG) is an integral component in the Company's management framework as Meralco pursues its business aspirations for all its stakeholders. Meralco's corporate governance framework is anchored on the principles of fairness, accountability, integrity and transparency. In 2010, the Company made corporate governance a major thrust and institutionalized the "Be Right" communication policy in the Meralco culture.

As a public utility, Meralco is subject to regulation, legislation and public scrutiny. All directors, officers and employees of the Company and its subsidiaries are therefore committed to observe all Company policies and relevant regulations and laws. The Company adheres to these imperatives, both in substance and form, as its commitment to stakeholders: shareholders, customers, government, employees, business partners, suppliers, creditors, contractors and the community.

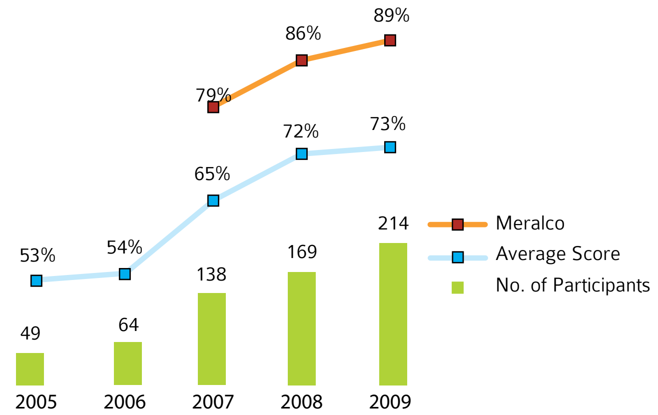
A Corporate Governance Office (CGO) was created on March 16, 2010 to manifest Meralco's dedication to pursue excellence in corporate governance. Its mandate is to support the Board of Directors and Management in the formulation and implementation of CG plans, programs and initiatives, and in monitoring compliance to achieve the highest standards of competence and ethical culture among directors, officers and employees of the Company.

I. GOVERNANCE COMPLIANCE AND PERFORMANCE

Meralco has consistently complied with the disclosure and reportorial requirements of the Securities and Exchange Commission (SEC). In 2010, these included:

- Certification by the Compliance Officer of the Company's compliance with the Revised Manual of Corporate Governance.
- Disclosure requirements on direct and indirect ownership of securities under the Securities Regulation Code (SRC), and the reporting of trading transactions of directors and concerned officers of the Company by the Compliance Officer not later than the following day after the required event or transaction. There has never been any case of insider trading involving directors and Management of the Company.
- The certification of Board attendance, reports involving financial statements, disclosure of material information and events, and trainings attended by key officers and Board members on corporate governance.

Meralco's Performance



Source: The 2009 Corporate Governance Scorecard for Publicly Listed Companies – ICD.

Every year, Meralco participates in the CG Scorecard Assessment conducted by the SEC together with the Philippine Stock Exchange (PSE) and the Institute of Corporate Directors (ICD). The CG Scorecard is administered to determine the level of CG practices of Publicly Listed Companies (PLCs) relative to global and regional standards. Meralco's performance since its initial assessment in 2007 has shown significant improvement, surpassing the average performance of participating companies.

Meralco was awarded the "Best in Investor Relations" in the Philippines in the 1st Asian Excellence Recognition Awards 2011 of Corporate Governance Asia. The award was based on the results of a regional survey conducted between August to December 2010 among investors in Asia. The award is given to companies exhibiting excellent performance in the areas of investor communications, business ethics, corporate social responsibility, environmental practices and financial performance.

The Company sends participants to CG Circle activities, e.g., Good Governance Advocates and Practitioners of the Philippines (GGAPP) meetings, ICD seminars and workshops as part of the corporate governance build-up in Meralco. The Company also cooperates with the regulatory agencies in the development of CG policies for Philippine companies by providing feedback on proposed policies by the PSE and SEC.

II. OUR POLICIES

Meralco believes that well-defined policies should cascade governance principles to business operations and processes.

These policies were based on best CG practices and adapted to the Meralco business environment:

a. **Revised Manual of Corporate Governance (MCG)** is the foundation of Meralco's governance policies, which complies with the amended SEC Corporate Governance Code under SEC Memorandum Circular No. 6, series of 2009 dated June 22, 2009. The revised manual was approved on April 12, 2010 and took effect on May 1, 2010.
b. **Revised "Standards of Business Conduct and Ethics" (Code of Ethics or COE)** prescribes that ethical values and standards of behavior are observed by all directors, officers and employees of the Company as they perform their respective duties and responsibilities. The 2003 version of our COE was revised to include important provisions such as risk management and internal control. A Company-wide orientation was conducted for all employees for a thorough understanding of and personal commitment to the revised COE.
c. **Conflict of Interest Policy** sets requirements for all directors, officers and employees to observe the highest degree of transparency, selflessness and integrity in the performance of their duties, free from any form of conflict with personal interest. This took effect on August 23, 2004.
d. **Policy on Disclosure of Relatives** aims to ensure fairness, transparency and objectivity in decision-making and avoidance of situations that may give rise to conflict of interest. This was approved and implemented on February 1, 2010.
e. **Policy on Blackout Period/Restriction on Trading of Shares** regulates trading of shares by Company executives, officers and employees with direct access to unpublished information relating to the Company's financial and operating results, in the interest of CG and transparency. This policy took effect on July 16, 2010.
f. **"Be Right" Communication Policy** promotes open lines of communication between Management and employees, enabling Management to relay directions and for employees to express their ideas and concerns to Management. This policy also provides a framework and guidance for good faith reporters on violations of governance principles, policies, codes of conduct, misstatement of financial transactions and accounts, fraud, and other potential whistleblowing type of incidents without exposure to retaliation. The "Be Right" policy was approved on August 10, 2010.
g. **Policy on Solicitation and Acceptance of Gifts** regulates the acceptance of gifts offered and given by third parties to prevent all directors, officers and employees from putting themselves in situations that could affect the fair, objective and effective performance of their duties. This policy was approved on December 13, 2010.

These policies on corporate governance are available at the Corporate Governance Intranet Portal of Meralco. Copies of the Corporate Governance Handbook, which compiles the above-mentioned policies, were distributed to all offices.

III. BOARD OF DIRECTORS

The Board of Directors (Board) has the primary responsibility of championing the principles of corporate governance. The Board also oversees the risk management function and the adequacy of internal control mechanisms to ensure the reliability of financial reporting, efficiency and effectiveness in operations, protection of assets and compliance with applicable laws and regulations.

There are 11 members of the Board with complementing expertise and experience necessary to act on various issues and matters affecting the Company. Of these directors, two are executive directors, two are independent and seven are non-executive directors. The Board structure and practices provide clear division of responsibilities at the top of the corporation – between the Board exercising oversight function and Management discharging its executive responsibilities. All the directors also fully comply with Energy Regulatory Commission (ERC) Resolution No. 1, Series of 2004, entitled "Program to Promote Good Corporate Governance in Distribution Utility," which requires attendance in seminars on corporate governance.

A. Board independence

The elected independent directors for 2010 are retired Chief Justice Artemio V. Panganiban and Mr. Pedro E. Roxas. This is in accordance with the SRC requiring at least two independent directors or 20% of the members of the Board, whichever is lesser. They were nominated and elected in compliance with Rule 38 of the Implementing Rules of the SRC, as amended.

To further strengthen the Board's independence, the Company separated the posts of the Chairman of the Board from that of the President and the CEO. Each position has distinct and separate duties and responsibilities in accordance with the Company's amended By-Laws and Revised Manual of Corporate Governance. The Chairman of the Board is Amb. Manuel M. Lopez, while the President and CEO is Mr. Manuel V. Pangilinan.

B. Election of directors

In accordance with the provisions of the Company's By-Laws and Manual of Corporate Governance, the Corporation Code of the Philippines and the SRC, nominees to the Board go through a nomination and screening process. The final list of nominees is determined after pre-screening and evaluation of qualifications. The directors are elected by stockholders who are entitled to vote during the Annual General Meeting (AGM). They serve for a period of one year and until their successors are qualified and elected.

C. Board remuneration

The Company's directors do not receive any compensation other than the Board-approved per diem for their attendance in Board and Board committee meetings. In 2010, each director was entitled to a director's fee of Php120,000 for each Board meeting attended. Each member or advisor of the Audit and Risk Management, Compensation and Benefits, Finance, Nomination and Governance Committees was entitled to a fee of Php20,000 for each committee meeting attended. The fees were last adjusted in April 2010.

D. Board performance

The Board holds monthly meetings and special Board meetings, if so required, with agenda that include updates by the Chairman and the Board committees; reports on financial performance by the Chief Finance Officer; and operational performance by the President and CEO, the Senior Executive Vice President and COO, among other major Company issues.

The table shows the participation of the Board in the Annual General Meeting, Organizational Meeting and its regular meetings.

Member	Designation	Annual General Meeting May 25, 2010	Organizational Meeting May 25, 2010	Board Meetings
Manuel M. Lopez	Chairman	Present	Present	10/12
Ramon S. Ang	Vice-Chairman and Director	Present	Present	12/12
Manuel V. Pangilinan	Director	Present	Present	11/12
Ray C. Espinosa	Director	Present	Present	12/12
Artemio V. Panganiban	Director (Independent)	Present	Present	12/12
Vicente L. Panlilio[1]	Director	Present	-	11/12
Estelito P. Mendoza	Director	Present	Present	7/12
Napoleon L. Nazareno	Director	Present	Present	11/12
Eric O. Recto [2]	Director	-	-	6/7
Oscar S. Reyes [3]	Director	-	-	6/6
Pedro E. Roxas [4]	Director (Independent)	-	Present	6/7
Elpi O. Cuna[5]	Past Director	Present	Present	5/5
Jose P. de Jesus [6]	Past Director	Present	Present	6/6
Elenita D. Go[5]	Past Director	Present	Present	5/5

[1] Director until May 25, 2010 AGM and reappointed on June 28, 2010
[2] Appointed, June 28, 2010
[3] Appointed, July 1, 2010
[4] Elected, May 25, 2010
[5] Resigned, June 30, 2010
[6] Resigned, June 28, 2010

On February 28, 2011, the directors conducted its Annual Board Self-Assessment to evaluate their specific and overall performance for 2010. Board members assessed their individual and collective performance on Board structures, processes and responsibilities.

The Board also conducted an evaluation of the 2010 performance of the President and CEO in the January 14, 2011 Board meeting. It was based on the attainment of key corporate goals for 2010, relative to his leadership, management, communication and working relationship with the Board.

IV. BOARD COMMITTEES

The Company's Board has five standing committees: the Executive Committee; Nomination and Governance Committee; Audit and Risk Management Committee; Compensation and Benefits Committee; and Finance Committee. All committees have approved charters defining and specifying the scope of their responsibilities.

The functions, authority and responsibilities of each Board committee, their accomplishments and Board committee members' attendance are as follows:

A. Executive Committee (ExCom) – composed of five directors, one of whom is an independent director. The ExCom may act, by majority vote of all its members, on such specific matters within the competence of the Board, as may be delegated to it in the By-Laws or on a majority vote of the Board, subject to the limitations provided by the Corporation Code of the Philippines.

B. Nomination and Governance Committee (Nom & GovCom) – composed of four directors with an independent director as chairman. It is responsible for screening qualified nominees for election as directors; assessing the independence of directors; introducing improvements on Board organization and procedures; setting-up of mechanisms for performance evaluation of the Board and Management; and providing programs for continuing education of the Board.

In 2010, the Nom & GovCom accomplished the following: review and selection of the nominees for election as members of the Board; review of rules on nomination of candidates, validation of proxies, and appreciation of ballots; proposal of amendments to the Company's By-Laws; review of revisions to the Manual of Corporate Governance and the Code of Ethics; review of CG policy approval procedures; approval and conduct of the Board self-assessment; and approval of the Policy on Solicitation and Acceptance of Gifts.

C. Audit and Risk Management Committee (AuditCom) – composed of five directors with accounting and finance backgrounds, two of whom are independent, and another director who has audit experience. The AuditCom assists the Board in its oversight responsibility in the financial reporting process, system of risk management and internal control, audit process, and monitoring compliance with applicable laws, rules and regulations.

In 2010, the AuditCom accomplished the: review of the Company's 2009 audited financial statements and 2010 quarterly financial statements; review of the financial performance of subsidiaries and affiliates; review and approval of the 2009 Audit and Risk Management Committee Report to the Board; endorsement of the nomination of the external auditor for 2010; review and approval of the 2010 internal audit plan, budget and covenant; review of 2009 internal audit performance, approval of external quality assessment review for the internal audit activity; review and approval of external auditor's 2010 financial statement audit plan and fees; and evaluation of the Company's risk profile and management structure, systems and processes.

D. Compensation and Benefits Committee (Comp & BenCom) – composed of three directors, one of whom is an independent director. The Comp & BenCom assists the Board in the development of the Company's overall compensation and retirement policies and programs based on the Board-approved philosophy and budget.

The committee's major accomplishments for 2010 include the review and endorsement to the Board of the Company's total compensation policy, philosophy and design; 2009 incentive program; 2009 performance evaluation, results, proposals for the 2010 performance management system and incentive plans and the Company's balanced scorecard results; 2009 performance evaluation of the Chairman and CEO, and President and COO; nomination and appointments to the pension fund Board of trustees; and review of the Employee Stock Purchase Plan.

E. Finance Committee (FinCom) – composed of three directors, one of whom is an independent director, with the Company's Chief Finance Officer as ex-officio member. It reviews the financial operations of the Company and matters regarding acquisition of or investments in companies, businesses or projects.

Among the accomplishments of the FinCom in 2010 are the approval of the 2011 corporate budget; review and approval of the medium-term financial plans; approval of cash dividend declaration for common and preferred shares; review of financial performance of subsidiaries and investment returns; review of quarterly cash projections and finance operations report; redemption on preferred shares; evaluation of debt refinancing; contribution to the pension fund; divestment of shareholdings in affiliate company; review of major purchases and contracts; and approval of bank accreditation and signing authorities.

F. Board Committee Meeting and Attendance

2010 Board Committee Meeting and Attendance					
Member	Executive	Nomination and Governance	Audit and Risk Management	Compensation and Benefits	Finance
Manuel M. Lopez	1/2	-	-	1/1	5/8
Ramon S. Ang	1/2	-	-	-	-
Manuel V. Pangilinan	2/2	-	-	3/3	-
Ray C. Espinosa	-	4/4	-	-	13/13
Artemio V. Panganiban[1]	1/1	-	2/2	-	-
Vicente L. Panlilio	-	-	7/9	0/1	-
Estelito P. Mendoza	-	4/6	-	-	-
Napoleon L. Nazareno	1/1	5/6	8/9	2/2	-
Eric O. Recto	1/1	-	2/2	2/2	7/7
Pedro E. Roxas[1]	-	6/6	2/2	2/2	7/8
Elpi O. Cuna	1/1	-	-	1/1	5/5
Jose P. de Jesus	-	-	-	-	5/5
Elenita D. Go	-	-	6/6	-	4/4
Aurora T. Calderon[2]	-	-	2/7	-	-
Elpidio L. Ibanez[2]	-	-	6/7	-	-
Ferdinand K. Constantino[2]	-	-	-	-	11/13
Anabelle L. Chua[2]	-	-	2/2	-	10/13

[1] Independent Director
[2] Non-Director Member

V. MANAGEMENT

Management is primarily accountable to the Board. It is responsible for the Company's successful implementation of the strategy and direction as approved by the Board.

Management is represented by a Management Committee (ManCom) composed of the corporate officers and executives headed by the President and CEO, or in his absence, the Senior Executive Vice President and COO. Weekly meetings are conducted by the ManCom to ensure implementation of major policies and directions governing the Company and its subsidiaries. It reports to the Board during regular Board meetings or during special meetings through the President and CEO and/or the Senior Executive Vice President and COO.

The annual performance of Management is assessed through the achievement of the Company's established Balanced Scorecard indicators.

To ensure continued success in managing Company operations, Management attended a structured executive training and development, including training on compensation and benefit plans and on succession planning. In addition, similar training programs were provided for senior management and the executive levels.

VI. ENTERPRISE RISK MANAGEMENT

Since 2005, the Company has been conducting periodic strategy and self assessments to evaluate risks and their likely impact on its business performance.

In 2010, the Company adopted an expanded approach to manage various business risks to cover its subsidiaries and associate companies. Management embarked on a series of briefings and workshops aimed at building competencies, identifying threats, exploiting opportunities and managing risks among its core business units. Using the Meralco Enterprise Risk Management Framework contained in the Meralco Risk Management Policy Manual, an enterprise risk management capability development program for subsidiaries and associate companies was conducted with the assistance of an expert from the Asian Institute of Management.

An executive briefing on Corporate Governance for the Board, the Management, and key officers of subsidiaries and affiliates was conducted on December 15, 2010 by the Asian Risk Management Institute (ARiMI), which discussed the integration of Corporate Governance and Enterprise Risk Management to foster sustainable effective performance.

VII. ACCOUNTABILITY AND AUDIT

A. Independent Public Accountants

SyCip Gorres Velayo & Co. (SGV & Co.) was reappointed as the independent external auditor of the Company, through the approval of the shareholders in the Annual General Meeting. The engagement partner assigned to the Company since 2008 is Mr. Gemilo J. San Pedro, who has extensive accounting and auditing experience. The appointment is in accordance with the SEC regulation that the audit partner principally handling the Company's account is rotated every five years or sooner.

In addition to serving as external auditor, SGV & Co. was engaged to provide non-audit services that included information and communication technology (ICT) security risk assessment in 2010, and for agreed upon procedures for the stockholders' meeting in 2009.

The following consolidated fees (exclusive of VAT) were incurred by the Company and its subsidiaries for SGV & Co.'s services:

Consolidated Audit Fees (in million Php)

	2010	2009
Regular audit of the annual financial statements	**8.8**	11.2
Other audit-related services	**-**	1.0
Other services	**1.5**	2.4
TOTAL	**10.3**	14.6

Other audit-related services in 2009 referred to under external auditors' services are in relation to the Company's filing of the Business Separation and Unbundling Plan Report and the Annual Report required by the ERC.

There has been no disagreement with the independent auditors on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure.

B. Internal Auditor

The Company has an independent internal audit organization, which provides objective assurance and consulting services designed to add value and improve the organization's operations. It helps organizations by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management in the Company, control and governance processes.

Internal Audit conducts its activities guided by the Institute of Internal Auditors' (IIA) Professional Practices Framework primarily consisting of the International Standards, the Definition of Internal Auditing and the Code of Ethics, and the Company's Code of Ethics. In the last quarter of 2010, Internal Audit subjected its activities to an External Quality Assessment Review (EQAR) as part of its quality assurance and improvement program and as prescribed by the Standards. Punongbayan and Araullo (P&A) performed the EQAR and declared that the Corporate Audits of Meralco "generally conforms" to the IIA Standards. This further validates that these internal audit activities were in accordance with the International Standards for the Professional Practice of Internal Auditing (ISPPIA).

The head of Corporate Audits reports functionally to the Audit and Risk Management Committee and administratively to the President and CEO.

C. Internal Control

The primary responsibility for the design, implementation and maintenance of internal control rests on Management; while the Board and its Audit and Risk Management Committee oversee the actions of Management and monitor the effectiveness of the controls put in place. The independent mechanisms to monitor and evaluate the existence and effectiveness of internal controls are provided by the external auditor and the internal auditor. The external auditor provides an independent and objective assurance on the preparation and presentation of the Company's financial statements, while the internal auditor functions as an independent audit that provides reasonable assurance on the achievement of the Company's internal control objectives, specifically on the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with the applicable laws and regulations.

VII. FINANCIAL REPORTING

The Company's consolidated financial statements were prepared in accordance with the Philippine Financial Reporting Standards (PFRS). PFRS includes statements named PFRS and Philippine Accounting Standards, including interpretations issued by the Philippine Financial Reporting Standards Council. The audited financial statements are reviewed by the Audit and Risk Management Committee to ensure that they present fairly, in all material aspects, the financial position of the Company and are recommended for approval by the Board. In 2010, the review of the Company's consolidated financial statements was conducted by the external auditor. The results of the review were discussed by the Audit and Risk Management Committee and presented to the Board, after which, the financial statements were filed with the SEC and released to the public.

IX. DISCLOSURES ON OWNERSHIP STRUCTURE

The Company ensures that it consistently complies with the required disclosure on shareholdings of its securities. It discloses the top 20 shareholders of its common shares annually. It also provides an annual disclosure of security ownership at certain record and beneficial owners who hold more than 5% of its equity shares. In compliance with the SEC requirements, a quarterly report of the Company's top 100 shareholders is disclosed in its website.

Based on Meralco's stock and transfer book, the security ownership as at December 31, 2010 of certain record and beneficial owners of more than 5% of any class of its voting securities is as follows:

Name	No. of Shares	Percentage
Beacon Electric Asset Holdings, Inc.	392,502,961	34.8%
Government Service Insurance System	332,172,311	29.5%
PCD Nominee Corporation (Filipino)	74,974,453	6.7%
PLDT Communications and Energy Ventures, Inc.	68,800,000	6.1%
Social Security System	62,990,689	5.6%

Details are found in the "List of Top 100 Stockholders as at December 31, 2010" as disclosed to PSE on January 17, 2011.

The Company's public ownership level as at December 31, 2010 as posted in the PSE website is at 22%. As of the said date, the outstanding shares of the Employee Stock Options Purchase Plan represents 1.29% of the total capital stock of the Company.

X. SHAREHOLDER RELATIONS

The Company upholds the rights of its shareholders, as well as the general investing public, to obtain relevant information about the Company in a timely and regular basis.

The Company's financial performance and prospects are regularly reported to the SEC and PSE. These reports are immediately made public upon submission to the SEC through press releases and postings in the Company's website. These include disclosures on related party transactions in compliance with Company policy. No disputes in connection with such related party transactions were reported in the past two years.

Investors' briefings are held quarterly, where equity and credit analysts of both local and foreign-based institutions are invited. Analysts unable to attend in person participate through a teleconference facility with playback feature available up to three days after the event.

Members of Senior Management make themselves available for meetings with institutional investors through Company visits, teleconferences, briefings and attendance in local and international investor conferences.

Press/media briefings are likewise held regularly to report on Meralco's operating and financial results to the various representatives of media, particularly from the broadsheets and wire agencies. The briefings become venues for Management to answer questions and clarify issues prior to the release of information to the public.

Shareholders and investors are provided with adequate facility to communicate with the Company such as telephone, mail, electronic mail, and its website, www.meralco.com.ph. The Investor Relations Office supervises the investors' briefings and attends to institutional investors' needs; while the Stockholder Affairs Office attends to the inquiries and other concerns of shareholders, including the distribution of Notice and Agenda of the AGM at least 30 days before the said meeting. For the 2010 AGM, notices were sent on March 30, 2010, 56 days before the AGM on May 25, 2010.

The AGM serves as a venue for the shareholders to clarify Company issues in the presence of the Board, the Chairman, the CEO, Management and external auditors. Shareholders are encouraged to personally attend the AGM and if unable to do so, are advised of their right to appoint a proxy on their behalf. Notarization of a proxy is not required but has to comply with the requirements of law, in particular, the Corporation Code and SRC, pertinent rules and regulations, By-Laws, and rules and policies adopted by the Board.

The voting procedure in the AGM is as follows: (a) the matters in the agenda require the affirmative vote of qualified stockholders. Each common stockholder shall be entitled to one vote for each share; (b) in the election of directors, each qualified stockholder may accumulate and distribute his votes in accordance with the Corporation Code of the Philippines; (c) voting and counting of votes shall be by balloting, show of hands or viva voce. Auditors and inspectors appointed by the Board will be present to canvass and inspect ballots.

During the May 25, 2010 AGM, the shareholders ratified the dividend policy approved by the Board, which called for payment of regular dividends equivalent to 50% of core earnings, which may be supplemented by a special dividend determined on a 'look-back' basis. Any declaration and payment of a special dividend is dependent on the availability of unrestricted retained earnings and cash. Details of the cash dividend pay-outs are contained in the Notes to Consolidated Financial Statements.

XI. EMPLOYEE RELATIONS

The Company is committed to the development and welfare of its employees. All personnel and staff are properly informed, trained and empowered to perform well, in the spirit of malasakit and teamwork/collegiality. They are engaged and compensated based on qualifications, merit and performance. Their professional growth and career advancement are ensured through the development and implementation of competency-based training, skills enrichment opportunities, and performance evaluation and job promotion plans and programs. Adequate provisions for medical and health support, essential benefits, rewards and recognition, and workplace safety are constantly provided for their protection, well-being and motivation. Uprightness and impartiality are observed in the resolution of conflicts. Management promotes openness and encourages employees to give suggestions and comments on corporate, administrative and operational improvements.

XII. OBLIGATIONS TO OTHER STAKEHOLDERS

Meralco seriously considers the impact of business decisions on the interests of its shareholders and other stakeholders. The Declaration of Corporate Principle of the Company's Revised Manual of Corporate Governance specifically mentions: "The Company...uphold(s) an ethical culture that will protect and promote the best interest of the Company for the common benefit of the Company's stockholders and other stakeholders."

The Company also protects and maintains good relations with its suppliers and creditors based on mutual respect and benefit. The Company strives to foster long-term stability, direct and open relation, and continuous development with suppliers to attain quality, competitiveness, process efficiency and performance reliability; foster governance principles in all of its business dealings with them; and seek, encourage and prefer suppliers whose business practices respect human dignity and the environment.

XIII. GOVERNANCE OF SUBSIDIARIES

The contribution of Meralco's subsidiaries has always been significant in boosting shareholder value. The Subsidiary Management Policy continues to be the standard set of rules for creating and managing subsidiaries based on the criteria and principles embodied in the Company's Manual of Corporate Governance, Code of Ethics, and existing laws, rules and regulations. In 2010, the Company introduced policy changes to strengthen good governance practice of subsidiaries. Specifically, a transparent process for the nomination and selection of Board members in subsidiaries was defined, ensuring that the criteria for Board directorship are followed including qualifications, composition and conflict of interest situations. The Company also encourages its subsidiaries to adopt their own Manual of Corporate Governance and Code of Ethics.

XIV. OUTLOOK FOR 2011 ONWARDS

Meralco aims for excellence that goes beyond compliance. The Company commits to strengthening its culture of good governance and responsible management practices, while benchmarking with the international community and global companies. Meralco believes that the reward of good governance is not just recognition but the continuous improvement on Company operations, breakthrough performance and sustainable growth that will serve the best interest of all our stakeholders.

MANUEL M. LOPEZ, 67
Director (since April 14, 1986)
Chairman (since July 1, 2001)
CEO (from July 1, 2001 to June 30, 2010)
Mr. Lopez is the Chairman and CEO of Lopez Holdings Corporation and is the Chairman of Bayan Telecommunications, Inc.; Indra Philippines, Inc.; Rockwell Land Corporation and Rockwell Leisure Club. He is the Chairman and President of Meralco Millennium Foundation Inc. and Meralco Management and Leadership Development Center; Vice Chairman of First Philippine Holdings Corporation and a member of the Board of Directors of ABS-CBN Corporation. He is the President of Eugenio Lopez Foundation Inc. Mr. Lopez was sworn in as the Philippine Ambassador to Japan in December 2010.

MANUEL V. PANGILINAN, 64
Director (since May 26, 2009)
President and CEO (since July 1, 2010)
Mr. Pangilinan is the Chairman of Philippine Long Distance Telephone Company and Smart Communications, Inc., the country's dominant telecommunications company and the largest mobile phone operator in the Philippines, respectively. He is the Chief Executive Officer and Managing Director of First Pacific Company Limited. Mr. Pangilinan has contributed significantly to the Philippine economy through achievements in business and society. He was Chairman of the Board of Trustees of the Ateneo de Manila University and is the Chairman of the Board of Trustees of San Beda College. Mr. Pangilinan holds a Masters in Business Administration degree from Wharton School of Finance and Commerce at the University of Pennsylvania, where he was a Procter & Gamble Fellow.

OSCAR S. REYES, 64
Director, Senior Executive Vice President and COO (since July 26, 2010)
Mr. Reyes is a member of the Board of Directors of the Philippine Long Distance Telephone Company (PLDT). He is Chairman of MRL Gold Phils., Inc. and Link Edge, Inc.; and is a member of the Board of Directors of Bank of the Philippine Islands, Manila Water Company, Inc., Ayala Land, Inc., Smart Communications, Inc. and Pepsi Cola Products Philippines, Inc. among other firms. He also served as Country Chairman of the Shell Companies in the Philippines and President of Pilipinas Shell Petroleum Corporation concurrently. He is a Managing Director of Shell Philippines Exploration B.V. and a member of the Board of Trustees of Pilipinas Shell Foundation, Inc., SGV Foundation, Inc. and El Nido Foundation, Inc. He completed his Bachelor of Science degree in Economics at the Ateneo de Manila University and finished his post-graduate studies at the Ateneo Graduate School of Business, Waterloo Lutheran University and the Harvard Business School.

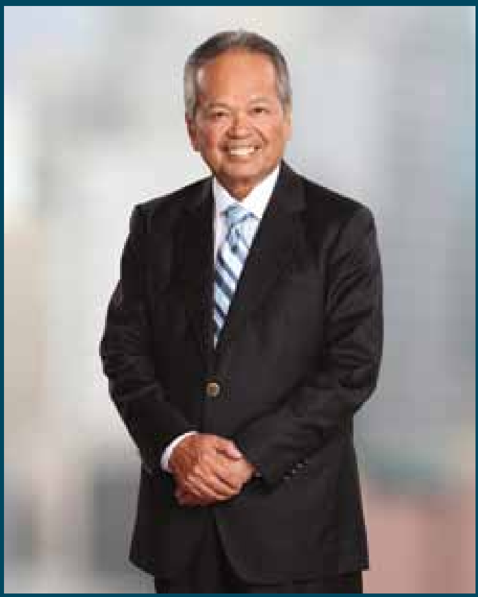
Board of Directors

RAMON S. ANG, 57
Director and Vice Chairman (since February 1, 2009)
Mr. Ang is the President and Chief Operating Officer of San Miguel Corporation. He is the Chairman and Chief Executive Officer of Petron Corporation, San Miguel Brewery, Inc., San Miguel Beverages, Inc., San Miguel Energy Corporation; San Miguel International Ltd. (Bermuda), San Miguel Holdings Limited (BVI) and San Miguel Beverages Pte. Ltd. (Labuan, East Malaysia). He is Chairman of Petrogen Insurance Corporation and La Lucas Development Corporation; and Managing Director of Ginebra San Miguel, Inc., San Miguel Pure Foods Company, Inc. and San Miguel Insurance Co., Ltd. (Bermuda). He finished his Bachelor of Science degree in Mechanical Engineering at the Far Eastern University.

RAY C. ESPINOSA, 55
Director (since May 26, 2009)
Atty. Espinosa is the President and Chief Executive Officer of ABC Development Corporation (TV5), Mediascape, Inc. (Cignal TV) and Mediaquest Holdings, Inc. (the investment arm of the PLDT Beneficial Trust Fund). He is a member of the Board of Directors of Philippine Long Distance Telephone Company and Lepanto Consolidated Mining Company; Chairman of its Audit and Nominations Committee; and Head of PLDT Regulatory Affairs and Policy. He was a Partner and member of the Executive Committee of the law firm, SyCip Salazar Hernandez & Gatmaitan. He was cited as one of the leading capital market lawyers and project finance lawyers by Asia Law Leading Lawyers and Euromoney Guide to the World's Leading Project Finance Lawyers. He finished his Bachelor of Laws degree at the Ateneo de Manila University and obtained his Master of Laws degree at the University of Michigan Law School as a Clyde Alton Dewitt Fellow.

ESTELITO P. MENDOZA, 81
Director (since February 1, 2009)
Atty. Mendoza heads the law firm, Estelito P. Mendoza and Associates. He is a member of the Board of Directors of San Miguel Corporation, Petron Corporation, Philippine National Bank and Philippine Airlines, Inc. and Chairman of Prestige Travel, Inc. He was a former Undersecretary of the Department of Justice, Minister of Justice and Solicitor General of the Republic of the Philippines and Governor of the Province of Pampanga. He was Chairman of the Sixth (Legal) Committee, 31st Session, United Nations General Assembly and Vice Chairman of the Philippine Delegation to the United Nations Seabed Committee and to the Conference on the Law of the Sea. He completed his Bachelor of Laws degree at the University of the Philippines and Master of Laws degree at Harvard University.

NAPOLEON L. NAZARENO, 61
Director (since May 26, 2009)
Mr. Nazareno is the President and Chief Executive Officer of Philippine Long Distance Telephone Company (PLDT), Smart Communications, Inc.; and PLDT Communications and Energy Ventures, Inc. and Connectivity Unlimited Resources Enterprise, Inc. He also serves as Chairman of the Board of Smart Broadband, Inc., Wolfpac Mobile, Inc., i-Contacts Corporation and Airborne Access, Inc. He is a member of the Board of Directors of PLDT Global Corporation and ePLDT, Inc.; and a non-executive Director of First Pacific Company Limited. He finished his Bachelor of Science degree in Mechanical Engineering at the University of San Carlos in Cebu City and holds 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, 74
Independent Director (since May 27, 2009)
Justice Panganiban was a former Chief Justice of the Supreme Court of the Philippines. He was a Chairperson of the Presidential Electoral Tribunal, Judicial and Bar Council and Philippine Judicial Academy. He is an Independent Director of Petron Corporation, Bank of the Philippine Islands, First Philippine Holdings Corporation, Metro Pacific Investments Corporation; Metro Pacific Tollways Corporation, Robinsons Land Corporation, GMA Network, Inc., GMA Holdings, Inc. and Asian Terminals, Inc.. He is a Senior Adviser of Metropolitan Bank and Trust Company, Chairman of the Board of Advisers of Metrobank Foundation 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.

VICENTE L. PANLILIO, 65
Independent Director (from May 27, 2008 to May 25, 2010)
Director (since June 28, 2010)
Mr. Panlilio is a member of the Board of Directors of San Fernando Light and Power Company, Philippine Stock Exchange, Inc.; Bacnotan Steel Industries, Inc. and Island Power Corporation; and a member of the Board of Trustees and Treasurer of Tulay sa Pag-Unlad Foundation, Inc. He was the Chairman of PNB Forex, Inc.; a member of the Board of Directors of BDO Leasing and Finance, Inc., Equitable PCIBank, Inc., Philippine National Bank, PNB Securities, Inc. and Bulawan Mining Corporation. He was Chief Operating Officer and member of the Advisory Board of Far East Bank & Trust Company. Mr. Panlilio graduated from the University of the Philippines with a Bachelor of Science degree in Economics. He attended the Advanced Bank Management Program of the Asian Institute of Management.

PEDRO E. ROXAS, 55
Independent Director (since May 25, 2010)
Mr. Roxas is Chairman and a member of the Board of Directors of Roxas Holdings, Inc., Roxas and Co., Inc. and Roxaco Land Corporation. He is the Chairman of Roxol Bionergy Corporation, Club Punta Fuego Inc. and Fuego Land Corporation. He is a member of the Board of Directors of Philippine Long Distance Telephone Company, BDO Private Bank and Brightnote Assets Corporation. He completed his Bachelor of Science degree in Business Administration at the University of Notre Dame in Indiana, USA.

ERIC O. RECTO, 47
Director (since June 28, 2010)
Mr. Recto is President of Petron Corporation, Top Frontier Investment Holdings, Inc., Q-Tech Alliance Holdings, Inc. and ISM Communications Corporation. He is also a member of the Board of Directors of San Miguel Corporation, and Vice Chairman of Atok-Big Wedge Co., Inc.; Alphaland Corporation and Philweb Corporation. He was a Director of Philex Petroleum Corporation, Maynilad Water Services, Inc.; Bulawan Mining Corporation and Philippine National Bank. He finished his Bachelor of Science degree in Industrial Engineering at the University of the Philippines and holds a Masters in Business Administration degree (Finance and Operations Management) from Cornell University, Johnson Graduate School of Management in Ithaca, New York, USA.

SIMEON KEN R. FERRER, 54
Corporate Secretary and Compliance Officer (since May 26, 2009)
Atty. Ferrer is a member of the Board of Directors and Corporate Secretary of Habibi Cove Realty Corporation, Marbelene Realty Corporation and Park Lane Assets, Inc. among others. He is a Senior Partner of SyCip Salazar Hernandez & Gatmaitan, the largest law firm in the Philippines. He completed his Bachelor of Science degree in Business Economics and Bachelor of Laws degree at the University of the Philippines. He holds a Master of Laws degree from the University of Michigan, USA as a DeWitt Fellow.

Ms. Elenita D. Go and Mr. Elpi O. Cuna completed their terms on June 30, 2010. Mr. Jose P. de Jesus completed his term on June 28, 2010.

ROBERTO R. ALMAZORA, 50
Senior Vice President
Energy Market Adviser of the Office of the Chief Operating Officer
Mr. Almazora holds a Bachelor of Science degree in Electrical Engineering from the University of the Philippines and completed his Masters in Business Management from the Asian Institute of Management. He is a member of the Board of Directors of Indra Philippines, Inc. and Meralco Energy, Inc. Prior to his current position, he was President and Director of Miescor Builders, Inc.; and was a member of the Board of Directors of Clark Electric Distribution Corporation, Meralco Industrial Engineering Services Corporation, Landbees Corporation, General Electric Philippines Meter & Instrument Company, Inc.; Conference of the Electric Power Supply Industry (CEPSI) Philippines, Inc. and Association of Electricity Supply Industry of East Asia and the Western Pacific.

RAFAEL L. ANDRADA, 50
First Vice President and Treasurer
Head, Investment Management
Mr. Andrada holds a Bachelor of Science degree in Management from De La Salle University. He is a member of the Board of Directors of CIS Bayad Center, Inc., Clark Electric Distribution Corporation, General Electric Philippines Meter & Instrument Co., Inc.; Republic Surety and Insurance Company, Inc., Meralco Industrial Engineering Services Corporation, Rockwell Leisure Club, Inc., Rockwell Land Corporation, First Private Power Corporation and Bauang Private Power Corporation. He is Treasurer of Clark Electric Distribution Corporation, MERALCO PowerGen Corporation and Treasurer-In-Trust of Calamba Aero Power Corporation. Prior to joining Meralco, he was Vice President for Finance of Benpres Holdings Corporation, Director for Project Finance in a property development company and Deputy General Manager for Corporate Banking Group of a Philippine commercial bank.

RUBEN B. BENOSA, 54
First Vice President and Head,
Corporate Logistics Office
Mr. Benosa holds a Bachelor of Science degree in Electrical Engineering from the Mapua Institute of Technology and completed his Masters in Management at the Asian Institute of Management. He is a member of the Board of Directors of Miescorrail, Inc., Meralco Energy Inc. and e-Meralco Ventures, Inc.; Trustee of the Meralco Management and Leadership Development Center Foundation, Inc. and the Meralco Millennium Foundation, Inc. He was the Chairman of the Outsourced Telleserve Corporation.

Corporate Officers

RICARDO V. BUENCAMINO, 66
Executive Vice President and Head,
Networks
Mr. Buencamino holds a Bachelor of Science degree in Electrical Engineering from the Mapua Institute of Technology and completed his Masters in Management at the Asian Institute of Management. He underwent training in General Management of Electric Utilities in Texas, USA. He was cited as Most Outstanding Electrical Engineer in the Corporate Management Category in 2005 by the Institute of Integrated Electrical Engineers of the Philippines, Inc. He is a member of the Board of Directors of Clark Electric Distribution Corporation, General Electric Philippines Meter & Instrument Company, Inc., Meralco Energy, Inc.; Conference of the Electric Power Supply Industry Philippines, Inc. and Association of Electricity Supply Industry of East Asia and the Western Pacific (AIESIEAP).

IVANNA G. DE LA PEÑA, 56
First Vice President and Head,
Regulatory Management
Ms. de la Peña holds a Bachelor or Science degree in Statistics and a Masters in Business Administration from the University of the Philippines. She attended the Public Utility Research Center-World Basnk Training Course on Utility Regulation and Strategy at the University of Florida and the General Management of Electric Utilities training program at the International Management Development Center in Texas, USA. She is a member of the Board of Directors of Clark Electric Distribution Corporation, e-Meralco Ventures, Inc., Share An Opportunity Philippines, Inc. and Medical Ambassadors' Philippines, Inc.

MARTIN L. LOPEZ, 38
Vice President and Chief Information Officer
(until December 31, 2010)
Mr. Lopez holds a Bachelor of Science degree in Business Administration from Menlo College and has an Executive Masters in Business Administration from the Asian Institute of Management. Mr. Lopez was appointed Chief Information Officer of Meralco in 2009. He was the President and a member of the Board of Directors of e-Meralco Ventures, Inc. He is a member of the Board of Directors of Adtel and Lopez, Inc.

ALFREDO S. PANLILIO, 47
Senior Vice President and Head,
Customer Retail Services and Corporate Communications
(since September 16, 2010)
Mr. Panlilio holds a Bachelor of Science degree in Business Administration (Computer Information Systems) at the California State University – San Francisco State University and his Masters in Business Administration at J. L. Kellogg School of Management at Northwestern University and The Hong Kong University of Science and Technology. He is a member of the Board of Directors of PLDT Global Corporation, ATH Holdings, Inc. (Malaysia), Mabuhay Satellite Corporation, Aces Philippines Cellular Satellite Corp., CIS Bayad Center, Inc. and Outsourced Telleserve Corporation; Vice Chairman, Meralco Management & Leadership Development Center (MMLDC) Foundation, Inc.; Trustee, Meralco Millennium Foundation, Inc.; President of the MVP Sports Foundation; and member of the Management Association of the Philippines. He has 25 years of experience with telecommunications and information systems. Prior to joining Meralco, he was President and CEO of PLDT Global based in Hong Kong.

ANTHONY V. ROSETE, 54
Vice President and Assistant Corporate Secretary
Information Disclosure Officer and Head, Legal
Atty. Rosete holds a Bachelor of Arts degree in Political Science and Bachelor of Laws degree from the Ateneo de Manila University. He is the Corporate Secretary of MERALCO PowerGen Corporation and Calamba Aero Power Corporation, Assistant Corporate Secretary of Clark Electric Distribution Corporation; a member of the Board of Directors of Miescorrail, Inc.; and was Corporate Secretary of e-Meralco Ventures, Inc. Prior to joining Meralco in 1992, he had an extensive practice of law for 10 years under well-known Philippine trial lawyers, Ramon Quisumbing, Jr. & Associates and N.J. Quisumbing & Associates.

RAMON B. SEGISMUNDO, 53
Senior Vice President and Head,
Human Resources and Corporate Services
Mr. Segismundo holds a Bachelor of Science degree in Industrial Engineering and completed his Masters in Business Administration at the University of the Philippines. He has over 25 years experience in human resources and business consulting in the Philippines, Singapore, United Kingdom and the United States for major companies such as GlaxoSmithKline, Arthur Andersen, SyCip Gorres Velayo & Co., Wyeth Pharmaceuticals, SmithKline Beecham and Sterling Winthrop. He is presently a Governor of the Philippine Basketball Association (PBA); Chairman of Outsourced Telleserve Corporation, Trustee and Vice President of Meralco Millennium Foundation, Inc. and Meralco Management and Leadership Development Center Foundation, Inc. and Trustee of Meralco Pension Fund; and a member of the Board of Directors of Meralco Industrial Engineering Services Corporation and CIS Bayad Center, Inc. and General Electric Philippines Meter & Instrument Company, Inc.

BETTY C. SIY-YAP, 49
Senior Vice President
Chief Finance Officer
Ms. Siy-Yap holds a Bachelor of Science in Business Administration and Accountancy degrees from the University of the Philippines and a Masters in Business Administration at J.L. Kellogg School of Management at Northwestern University and The Hong Kong University of Science and Technology. She also attended the Special Executive Program in Corporate Restructuring and Finance at the Arthur D. Little Management Institute in Cambridge, Massachusetts, USA. She is a member of the Board of Directors of Republic Surety and Insurance Company, Inc., Meralco Industrial Engineering Services Corporation, Clark Electric Distribution Corporation, General Electric Philippines Meter & Instrument Co. Inc.; CIS Bayad Center Inc., Miescorrail Inc., Rockwell Land Corporation, Meralco Financial Services Corporation, e-Meralco Ventures, Inc., Indra Philippines, Inc; MERALCO PowerGen Corporation and Calamba Aero Power Corporation. Prior to joining Meralco, she was a Partner at SyCip Gorres Velayo & Co.

MIGUEL L. LOPEZ, 41
Vice President and Head,
Corporate Marketing and Communications
(until August 31, 2010)
Mr. Lopez holds a Bachelor of Science degree in Business Administration from Menlo College and attended an Executive Development Program from the Asian Institute of Management. He is a member of the Board of Directors of Philippine Commercial Capital, Inc., Rockwell Land Corporation and Indra Philippines, Inc. He was a member of the Board of Directors of Meralco Industrial Engineering Services Corporation, Outsourced Telleserve Corporation, Lopez Group Foundation, Inc.; and was an Executive Director of Meralco Millennium Foundation, Inc.

LEONISA C. DE LA LLANA, 56
Senior Vice President and Head,
Customer Retail Services (until June 30, 2010)
Ms. de la Llana holds a Bachelor of Arts degree in Economics from the University of the Philippines and completed her Master of Arts in Economics at the Utah State University. She was the Executive Director and Vice President of Meralco Management and Leadership Development Foundation Inc. and a Trustee and Vice President of Meralco Millennium Foundation, Inc. She was a member of the Board of Directors of General Electric Philippines Meter & Instrument Co., Inc., Clark Electric Distribution Corporation and Indra Philippines, Inc.

Subsidiaries

MERALCO POWERGEN CORPORATION (MPG)

MPG is a wholly-owned subsidiary of Manila Electric Company (Meralco) established to develop, finance, construct, own, operate and maintain power generation assets.

MPG's mission is to develop highly cost-competitive and reliable power plants. As Meralco's vehicle for re-entry into power generation, it will enable Meralco to better assure the provision of adequate, reliable and affordable power to residential, commercial and industrial customers in the Meralco franchise area.

It is currently in the process of developing a portfolio of baseload, mid-merit and peaking generating plants potentially utilizing clean coal, liquefied natural gas (LNG), and/or aeroderivative gas turbine technologies. It intends to build new generating capacity of 1,500 MW, principally in cooperation with strategic partners.

MANUEL V. PANGILINAN, Chairman *(please refer to Board of Directors profile)*

OSCAR S. REYES, President *(please refer to Board of Directors profile)*

AARON A. DOMINGO, 47
Executive Vice President & General Manager
Director
Mr. Domingo holds a Bachelor of Science degree in Business Administration, summa cum laude, from Syracuse University, New York and a Masters in Business Administration from the University of Chicago Graduate School of Business in Illinois, USA. He is a Director of Calamba Aero Power Corporation. He was a Director of GE Capital Structured Finance Group; the Chief Operating Officer of Asian Energy Ventures Group; Managing Director of Moneta Capital Ltd., UPC Renewables Partners BV and Noble Energy Development Ltd. He has 16 years of experience in business development, capital raising, restructuring and energy finance.

CLARK ELECTRIC DISTRIBUTION CORPORATION (CEDC)

CEDC is 65%-owned by Meralco and 35%-owned by Angeles Electric Corporation. It is the exclusive franchised distribution company in the Clark Economic Zone (CEZ). The company distributes power within CEZ through its three substations with a total capacity of 110.5 MVA. Its present distribution network consists of 1,412 distribution transformers, 117 km of primary lines and 31 km of secondary lines. Its system loss has continuously improved from 9.76% in 2002 to 3.81% in 2010 and its supply rates are one of the lowest in Luzon.

PETER G. NEPOMUCENO, 74
Chairman
Mr. Nepomuceno holds a Bachelor of Science degree in Civil Engineering from the Mapua Institute of Technology and a Bachelor's degree in literature from Ateneo de Manila University. He is the Chairman and President of Angeles Power Inc., J Ten Equities, New Move Realty Inc., and Mavwin Properties Inc. He is the Chairman of Angeles Electric Corporation, Mindanao Energy Corporation and Nepomuceno Group of Companies. He is a member of the Board of Directors of Philippine Electric Market Corporation (PEMC) and Holy Angel University.

JESUS P. FRANCISCO, 67
President and Director
Mr. Francisco is a Mechanical and Electrical Engineering graduate of the University of the Philippines. He earned his Master's Degree in Business Management and graduated from the Washington SyCip Graduate School of Business, Asian Institute of Management. He completed the International Senior Managers Program of the Harvard Business School in Vevey, Switzerland (an off-campus management program) and the Strategic Business Economics Program of the University of Asia and the Pacific. He is the President and a Director of Meralco Industrial Engineering Services Corporation (Miescor) and Meralco Energy, Inc.; Chairman and President of Miescorrail Inc. and Landbees Corporation. He is the Chairman of Miescor Builders Inc. He is also Chairman of the Board of Haribon Foundation; Trustee of Preferred Energy, Inc.; member of Philippine Foundation for Science and Technology; and Chairman Emeritus of UP Engineering Research and Development Foundation, Inc. He was President and Chief Operating Officer and a Director of Meralco.

MERALCO INDUSTRIAL ENGINEERING SERVICES CORPORATION (MIESCOR)

Miescor is 99%-owned by Meralco and the remaining 1% by the Miescor Provident Fund. Miescor, a holder of the highest contractor license Category AAA since 1982, 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.

Miescor is Meralco's most reliable service provider in electro-mechanical works, engineering, distribution and technical services. It also handles telecommunication projects for Meralco, e-Meralco Ventures, Inc. and Philippine Long Distance Telephone Company. Among its external clients are the Bangko Sentral ng Pilipinas (BSP), First Gen Corporation, Quezon Power (Philippines) Limited Co. (QPPL), Chevron Philippines, Inc., Maynilad Water Services, Inc. and the Department of Finance.

OSCAR S. REYES, Chairman *(please refer to Board of Directors profile)*

JESUS P. FRANCISCO, President and Director *(please refer to profile under Clark Electric Distribution Corporation)*

Installation of electric poles and overhead contact system at the LRT Line North Extension by Miescorrail, a MIESCOR subsidiary.

CORPORATE INFORMATION SOLUTIONS, INC. (CIS, INC.)

CIS, Inc. is a wholly-owned subsidiary of Meralco, incorporated in 1974 to provide information technology services and integrated business solutions, focusing on the functional areas that are critical to customers' business continuity, growth and profitability. In 1997, CIS engaged in the business of bills payment collection which activity was spun off as CIS Bayad Center, Inc. (Bayad Center), formally incorporated in 2006. Bayad Center is the country's trailblazer and brand leader in the outsourced over-the-counter (OTC) payment collection industry. Trusted by top multinational and local organizations with their payment collection requirements, it accepts payments for over 160 industry-leading partners through its 1,400-strong strategically-located branches nationwide and US-based online payment facility. To complement its bills payment business, Bayad Center now offers electronic wallet services (vehicle insurance), prepaid loading, and applications acceptance. With the vision of becoming a global organization and the undisputed leader in transaction-based services, it is one of the few Philippine companies certified as an "Investors in People" (IiP) by the People Management Association of the Philippines and the UK-based IiP Quality Centre.

OSCAR S. REYES, Chairman *(please refer to Board of Directors profile)*

MANUEL LORENZO L. TUASON, 48
President and Director
Mr. Tuason holds a Bachelor of Science degree in Business Administration and Masters in Business Administration from the University of the Philippines. He is a Fellow of the Institute of Corporate Directors. He is the President and CEO of CIS Bayad Center, Inc. and Outsourced Telleserve Corporation; and a Senior Assistant Vice President of Meralco.

MERALCO ENERGY, INC. (MEI)

MEI is a wholly-owned subsidiary of Meralco established in June 2000 to provide demand-side energy services to Meralco's key accounts. It aims to be the country's premier energy management company by providing innovative energy solutions to industrial, commercial and large residential customers and creating value for these customers through promotion of energy efficiency, renewable energy and innovation.

OSCAR S. REYES, Chairman
(please refer to Board of Directors profile)

JESUS P. FRANCISCO,Vice Chairman and President
(please refer to profile under Clark Electric Distribution Corporation)

MERALCO FINANCIAL SERVICES CORPORATION (FINSERVE)

A wholly-owned subsidiary of Meralco, Finserve was established in 2002 to create shareholder value by enhancing the range of value-adding services provided by Meralco through a portfolio of innovative consumer and customer-based products and multi-services that cater to retail and corporate clients.

For the retail base, Finserve together with Banco de Oro created HOME MasterCard, the first home and family oriented credit card that allows Meralco customers to pay their electricity and other utility bills under convenient charging schemes, including auto charge and payment on demand. Also catering to corporate clients, Finserve provides loyalty/rewards program management to aid companies in their marketing and consumer retention programs.

MONICO V. JACOB, Chairman and President *(please refer to profile under Republic Surety and Insurance Company, Inc.)*

MARY JOCELYN Z. FRANQUELLI, 39
General Manager
Ms. Franquelli holds a Bachelor of Science degree in Electronics and Communications Engineering from De La Salle University. She headed the sales, marketing and operations of a telecommunications company and various local and international BPO companies before joining Finserve. Prior to her appointment as General Manager, she managed the Home MasterCard and Call Center business lines. Ms. Franquelli was appointed General Manager in May 2010.

e-MERALCO VENTURES, INC. (e-MVI)

e-MVI is a 100%-owned subsidiary, operating a telecommunications infrastructure anchored on a 1,500-km fiber optic network within the Meralco franchise area. e-MVI offers data transport and connectivity services to local and international carriers, internet service providers, data centers and other businesses. e-MVI services include leased line connections, Metro Ethernet connections, disaster recovery transport services and packaged internet bandwidth.

e-MVI is a premium data transport provider to the biggest names in the market. It consistently delivers installation lead times that are beyond industry standards and is true to its commitment to operate a future-proof network. e-MVI is also certified as an "Investors in People" (IiP) by the People Management Association of the Philippines and the UK-based IiP Quality Centre.

FELIPE B. ALFONSO , 74
Chairman
Mr. Alfonso holds a Bachelor of Laws degree from Ateneo de Manila University and Masters in Business Administration from New York University. He is the Chairman of the Board of STI Inc. He is a member of the Board of Directors of AIG Global Fund, Inc., Andorra Ventures Corporation, Lopez Holdings Corporation, First Philippine Realty Corporation, Franklin Baker Company of the Philippines, Jollibee Foods Corporation, several PHILAM Funds, Philippine Investment Management, Inc. and Phinma Corporation. He is a Trustee of the Coca-Cola Foundation of the Philippines, First Philippine Conservation, Inc., Knowledge Channel Foundation, Inc., Philippine Foundation for Global Concerns, Inc., and STI Foundation. He is also the Vice Chairman of the Lopez Group Foundation, Inc.

REPUBLIC SURETY AND INSURANCE COMPANY, INC. (RSIC)

RSIC is a professional non-life insurance company and a wholly- owned subsidiary of Meralco. It was acquired in 2007 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.

RSIC is licensed to write the full spectrum of non-life insurance business to include property (fire and allied perils, industrial all risks and commercial all risks) and engineering, casualty, marine and aviation, motor, surety and special packages.

RSIC's objective is to become an acknowledged leader in the field of risk management and to ensure profitability and market share while adhering to the principles of good corporate governance and corporate social responsibility. It envisions itself to be a total risk solutions provider and a major player in the local insurance industry in the near future.

MONICO V. JACOB, 65
Chairman
Atty. Jacob holds a Bachelor of Arts degree major in Liberal Arts from the Ateneo de Naga University and a Bachelor of Laws degree from the Ateneo de Manila University. He is the President and CEO of the STI Education Services Group, PhilPlans First, Inc. and Philhealthcare, Inc. He is the Chairman of Information and Communications Technology Academy (iAcademy), Global Resource for Outsourced Workers, Inc. (GROW, Inc.), Total Consolidated Asset Management, Inc., and Accent/STI Banawe Management, Inc. He is a member of the Board of Directors of Advent Capital and Finance Corporation, Mindanao Energy Corporation and Phoenix Petroleum Philippines. He was President and a director of Petron Corporation. He is Partner in the law firm Jacob & Jacob. He is a member and was President of the Management Association of the Philippines (MAP).

PEDRO P. BENEDICTO, JR., 55
President and Director
Mr. Benedicto holds a Bachelor of Science degree in Electrical Engineering from the Mapua Institute of Technology. He has a PhD in Insurance and Risk Management and is taking up Doctorate in Business Administration at De La Salle Professional Schools, Inc., where he also finished his Masters in Business Administration. He received a certification as a Master of Insurance and Risk Management from Ashwood University, USA (on-line). He is a Fellow of the Georgia State University in International Insurance and Risk Management and the Institute of Corporate Directors (ICD). He is the Chairman of Philippine Insurers and Reinsurers Association, Inc. He was President and CEO of Pioneer Intercontinental Insurance Corporation, Director of the Philippine General Insurers Association; President of the Insurance and Surety Association of the Phils., Member of the Professional Liability Underwriting Society; President of the Philippine Insurance Institute and an ex-officio Member of the PII Council.

LIGHTHOUSE OVERSEAS INSURANCE LIMITED (LOIL)

LOIL, Meralco's wholly-owned subsidiary and captive reinsurer, is registered as a Class 1 insurer under The Bermuda Insurance Act 1978 and Related Regulations. The company was incorporated in Bermuda in 2007 and received its license to operate in the territory in 2008.

Together with RSIC, LOIL plays a major role in Meralco's business risk management model. The company serves as the vehicle to reinsure Meralco's major catastrophic risk exposure.

OSCAR S. REYES, Chairman *(please refer to Board of Directors profile)*

BETTY C. SIY-YAP, President (*please refer to Corporate Officers profile)*

ROCKWELL LAND CORPORATION (ROCKWELL LAND)

Rockwell Land is 51%-owned by Meralco and 49%-owned by First Philippine Holdings Corporation. Formed in 1995, the company is one of the premier real estate developers in the Philippines and its ground-breaking master plan transformed Meralco's former thermal plant site into a high-end residential living and commercial environment now known as the Rockwell Center. Rockwell Center, the company's flagship project, sits on a 15.5-hectare site in Makati City and is strategically located between the three major commercial business districts of Makati City, Bonifacio Global City and Ortigas.

MANUEL M. LOPEZ,
Chairman *(please refer to Board of Directors profile)*

OSCAR M. LOPEZ , 80
Vice Chairman
Mr. Lopez holds a Bachelor of Arts degree, *cum laude*, from Harvard College, USA and a Masters degree in Public Administration from Littauer School of Public Administration, Harvard University. He is the Chairman of First Philippine Industrial Park, Asian Eye Institute, Inc., Griffin Sierra Travel Inc., Inaec Aviation Corp., Securities Transfer Services, Inc. and other companies in the Lopez Group. He is a member of the Board of Directors of ABS-CBN Broadcasting Corp. and Benpres Insurance Agency. He is the Chairman of the Lopez Group Foundation, Inc., Knowledge Channel Foundation, Inc. and the Eugenio Lopez Foundation, Inc. He was Chairman and CEO of Lopez Holdings Corporation, First Philippine Holdings Corporation and First Gen Corporation; and is the Chairman Emeritus of these companies.

Corporate Social Responsibility

Our Company takes on a new strategic direction for its Corporate Social Responsibility thrusts - a blueprint that essentially aligns Meralco's CSR initiatives with the Company's core business of electricity or power distribution, as well as with other business areas of interest moving forward.

With the new framework, CSR initiatives are designed in a way that Meralco's commitments to its 3C's, namely - Customers, Community and Country - are fully supported and fortified as it fulfills its role as a responsible corporate citizen.

Rural/Missionary Electrification

Isolated segments of the Meralco franchise remain still deprived of the benefits and conveniences of legal electricity service. These include (1) informal settlers in certain public lands or private properties; (2) portions of resettlement areas where informal settlers such as families formerly residing along the Pasig River, railroad tracks and privatized government properties; (3) isolated communities; and (4) families unable to meet the minimum legal requirements to apply for and secure legal electricity connections. The thrust of rural/missionary electrification is to develop feasible alternatives to provide these communities with electricity through workable socialized schemes that are suitable to these potential beneficiaries in partnership with Local Government Units (LGUs), Non-Government Organizations (NGOs), and multilateral or bilateral financing institutions.

As the leading electric distribution utility company in the country, Meralco also extends support and assistance to other distribution utilities and cooperatives in restoring electricity service to their customers in urban and rural areas particularly in times of emergencies.

Grassroots Partnership (Local Government/ Barangay)

Meralco recognizes the importance of local government units, government agencies and barangays play in uplifting the lives of the people, improving the environment of their communities and enabling commercial and industrial businesses to operate in a sustainable manner.

Meralco continues its commitment towards strong partnerships with local government and barangays by providing appropriate support for certain local community needs, such as health, sanitation, environmental protection, sports and education. Moreover, through these partnerships, Meralco is able to nurture public safety, promote responsible stewardship among residents and spur growth and development in communities.

Sports and Youth Advocacy

Meralco continues its commitment towards the development of the youth and sports in the country. The Company believes that sports is a highly effective platform where the youth not only enhance their fitness, well-being and health, but also develop leadership, character and discipline that will ultimately make them productive citizens of the country. Through sports-focused outreach programs the Company inspires the youth to make highly-productive activities, such as sports, a vital part of their lives.

The Company also provides exceptionally talented but less privileged youth the opportunity to acquire a good education through sports scholarships. This includes the provision of livelihood training and business opportunities to give out-of-school youth better hope for a brighter future.

Disaster Relief and Emergency Preparedness

Meralco lends its experience and resources in emergency and disaster preparedness to support other utilities and communities. This sharing of expertise and resources aims to further harness response to major emergency situations, natural calamities and disasters.

NEW CSR STRATEGY: The Four CSR Pillars

NEW CSR STRATEGY

- Strongly linked and fully aligned to "Powering Up to Success"
- Focus and maximum social return on capital "critical few advocacies that will make a difference"

Rural/Missionary Electrification

"Providing light to those in darkness"

Grassroots Partnership (LG/Barangay)

"In pursuit of a jumper-free society"

Sports and Youth Advocacy

"Para sa maliwanag na kinabukasan"

- Caritas-Meralco Bolts Partnership
- Basketboys Bolts/ Meralco Basketball Outreach

Disaster Relief & Emergency Preparedness

"Bagyo, baha o ano pa man, nandoon kami"

- Partnership with other disaster relief organizations
- Proactive Environment, Safety and Health Advocacy

Integrated Foundation (Para sa Sambayanan) involving all of our Meralco people.

Meralco is moving forward towards integrating CSR efforts and creating more impact through a One Meralco Foundation

Foundations

MERALCO MILLENNIUM FOUNDATION, INC.

The Meralco Millennium Foundation, Inc. (MMFI) is our corporate foundation registered with the Securities and Exchange Commission on May 8, 2002 as a non-stock, non-profit organization, primarily to initiate, develop, support, finance, undertake or manage programs and projects for socio-economic purposes in any of the areas under corporate social responsibility.

Its vision is to foster CSR programs that address the needs of communities within Meralco's business environment. These programs render a holistic response to society's needs as they are carried out through the dedicated service of Meralco volunteers. On July 31, 2006, the MMFI was granted a five-year accreditation as Donee Institution by the Philippine Council for NGO Certification (PCNC).

MERALCO MANAGEMENT AND LEADERSHIP DEVELOPMENT CENTER FOUNDATION, INC.

The Meralco Management and Leadership Development Center (MMLDC) is our educational foundation that specializes in providing the most effective learning solutions. MMLDC offers Leadership and Management Programs, Technical Excellence for Teachers, Environmental Safety and Health Programs, Technical Development Programs and Education and Training Programs.

The success of MMLDC's business activities enables it to reach more beneficiaries through programs anchored on its advocacies that include environmental safety and health program for public schools, health education reform order (HERO) program, lakbay kalikasan program, quality leadership and management programs and technical excellence program.

MERALCO EMPLOYEES FUND FOR CHARITY, INC.

The Meralco Employees Fund for Charity, Inc. (MEFCI) is an employee-initiated organization formed in 1978 to implement charity projects complementary to those sponsored by the Company. Funding is from the voluntary monthly contributions of Meralco employees.

MEFCI programs include disaster relief, medical and dental missions, assistance to institutions and outreach programs.

CSR Projects

Rural/Missionary Electrification

1. **Dangal Electrification Program.** Provides affordable and safe electric service in organized depressed communities.

2. **Lineman Training for Electric Cooperatives.** Trains linemen from electric cooperatives on safety, basic and advanced lineman skills and supervisory courses, conducted by the Meralco Management and Leadership Development Center (MMLDC).

3. **Electric & Safety Inspection of Public Schools *(Brigada Eskwela)*.** Involves electrical and safety audit or assessment by Meralco and MMLDC in identified public schools. It is an annual activity of the Department of Education with various sectors of society (private sector, education, students, teachers, parents, volunteers) to improve, repair and upgrade public school facilities in time for the opening of classes.

4. **Christmas Lighting Up of Churches *(Lingap Kapwa sa Kapaskuhan).*** Lights up prominent Catholic Churches. Also involves the installation of Christmas lights, donation of church equipment, inspection/ rehabilitation of church electrical facilities and outreach to less privileged parishioners.

- Dangal Electrification Program (Franchise Area): 11 GK Villages lighted
- Lineman Training for Electric Cooperatives: Six batches; 99 linemen trained
- Electric and Safety Inspection of Public Schools (Brigada Eskwela): 4 Public Schools inspected
- Christmas Lighting Up of Churches (Lingap sa Kapwa sa Kapasuhan): 11 Churches lighted

- 3,235 beneficiaries in 6 communities (Medical and Dental Missions)
- 181 children in 4 GK communities (Disease and Prevention Program)
- 2 beneficiaries (Individual Medical Assistance)
- 6 organizations (Institutional Donations)

Grassroots Partnership

1. **Meralco GK Sibol Schools Project.** Involves the construction of a 60 sq. m. school building in Gawad Kalinga (GK) Communities for 3 to 6-year-old children of families residing in GK communities. This project also includes a Feeding Program and a Disease Prevention Program for Sibol School students.

2. **Computer Training Project (for Local Government Units and the Philippine National Police).** Involves the donation of reconditioned Pentium 4 computers to police stations and headquarters and the conduct of a two-day basic computer literacy training.

3. **Delightful Christmas Outreach.** Gift-giving and sharing activity with identified charities for children as beneficiaries.

4. **Community Outreach Projects.** Involves medical and dental missions and gift-giving activities conducted by the Meralco Employees Fund for Charity, Inc. (MEFCI).

5. **Community Livelihood Training.** Implements livelihood training activities for depressed communities.

6. **Employees Day Outreach (FUN-tastic Friendship Fair).** Conducts fun-filled activities for children from different branches of the Department of Social Welfare and Development.

7. **Leadership Program for Public School Heads.** Trains school heads to be better leaders of their schools with continuous improvement initiatives in their annual and strategic plans, conducted by the MMLDC through its School Based Management Development Program (SBMDP).

8. **Educators Summit.** Conducted annually at the Meralco Theater for 1000 educators from the public sector to learn from and be inspired by luminaries in the field of education.

9. **Teacher Education Program.** Equips public high school teachers with skills and concepts (5S, computer literacy and spirituality in the work place).

10. **Project Kasambahay Outreach.** Acknowledges service providers of Meralco i.e., janitors, drivers, security guards, gardeners, through an annual outreach activity.

- Community Livelihood Training: 32 individuals trained
- Community Outreach Activity: 1 institution; 70 individual beneficiaries
- School-Based Management and Development Program: 670 individuals and 147 institutions trained
- Technical Excellence-Educators' Forum-1st MMLDC-PSHSS Science Congress: 2,865 individuals and 195 institutions attended
- Computer Training for Public School Teachers: 118 teachers from 2 public schools trained

Sports & Youth Advocacy

1. **Caritas - Meralco Bolts Partnership Project.** The Meralco Bolts, a team playing in the Philippine Basketball Association, was formed to be a key element in this partnership. This project helps support Caritas Manila, the social arm of the Archdiocese of Manila. A part of the proceeds from the Bolts' game dates is donated to Caritas, also known as the Church of the Poor.

2. **Basketboys Scholarship Project.** Provides scholarships for poor but talented young basketball players.

- Martsa sa Eskwela (improvement of sanitation facilities): 3 sanitary facilities built in 3 public schools
- Bio Intensive Gardening Project: 244 families in 3 GK communities

Disaster Relief & Emergency Preparedness

1. **Martsa sa Eskwela.** Improves sanitation in public schools through a partnership with Hocheng Philippines Corporation (HCG).

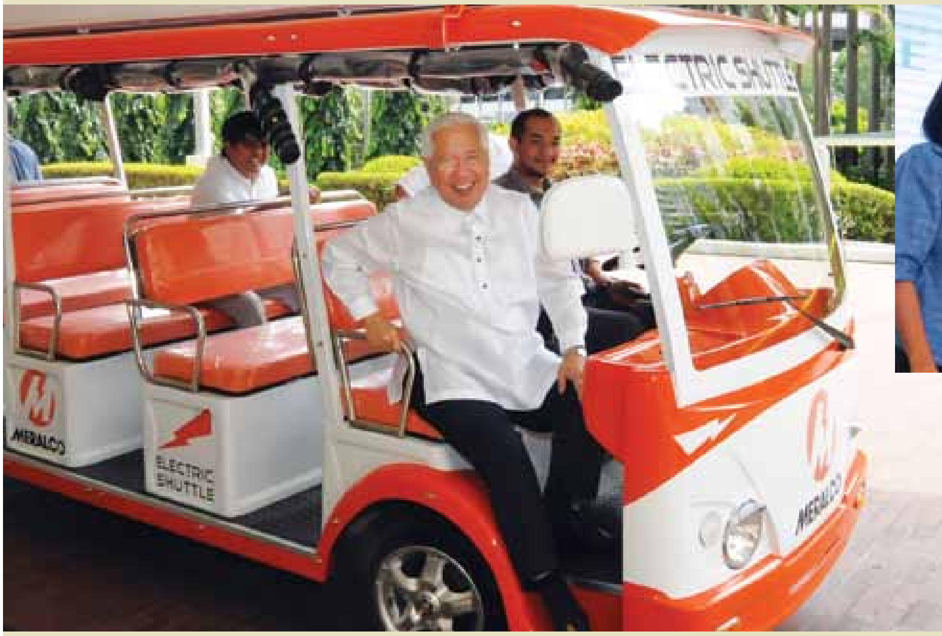
2. **Disaster Preparedness Planning.** Provides training in seven municipalities - Marikina, Pasig, Cainta, Antipolo, San Mateo, Rodriguez and Quezon City – on disaster risk reduction management.

3. **Health Education in Public Schools.** Provides teaching materials for Health Education Reform Order (HERO), being piloted in 10 public schools to prevent 10 top killer diseases in the country.

4. **Bio Intensive Gardening Project.** Trains families in depressed communities on backyard farming using organic fertilizers.

5. **Disaster Relief Operations.** Giving of donations (food and clothing) contributed by Meralco employees to victims of calamities.

For a cleaner future:
Meralco supports electric vehicles



COO Oscar S. Reyes with former Department of Environment and Natural Resources Secretary Elisea Gozun and former Energy Secretary and current World Wildlife Fund Philippines Chairman Vince Perez.

Meralco joins the global vision for a cleaner environment and efficient use of energy and in line with this commitment, it has expressed its support for the development of electric vehicles (EV) considered an environmentally friendlier alternative to existing modes of transportation.

Inside the Company's vast main compound in Pasig City, e-vehicles are used to transport employees and visitors. These e-vehicles are especially built, reprising the design of yesterday's electric streetcar known as the *Tranvia*, which plied the major thoroughfares of Manila in the early 1900s. Meralco, organized in 1903, was tapped to operate the electric streetcar system.

In 2010, Meralco hosted the First Philippine Electric Vehicle Summit which assessed the Philippines' EV sector as well as consumers' readiness for such mode of transport. The summit explored ways to develop the domestic industry. Meralco President and CEO Manuel V. Pangilinan committed to help fund the EV program with the aim of making EVs an affordable option in transportation.

Through the summit, a roadmap was drawn for the EV industry for the next five years. Organized by private organizations of the industry in cooperation with Meralco and the Department of Transportation and Communications, the event was graced by leaders and key players from various sectors led by the Philippine Vice President Jejomar Binay.

Further expressing its full support for clean modes of transport, Meralco sponsored the University of the Philippines' College of Engineering development of the E-Kotse, a one-seater diesel-electric hybrid vehicle using a one-cylinder engine. The E-Kotse is the UP Engineering Team's entry at the 2011 Shell Eco-Marathon. Meralco through President and CEO Manuel V. Pangilinan donated P1.5 million for the development of a fuel-efficient E-Kotse, an integral component of the UP-Meralco academe-industry partnership.

Management's Discussion and Analysis

The following discussion and analysis of financial position and results of operations of Manila Electric Company or *MERALCO* or "*Parent Company",* and its subsidiaries, collectively referred to as the "Company" or "*MERALCO* Group" should be read in conjunction with the audited consolidated financial statements as at December 31, 2010. The audited consolidated financial statements are prepared in accordance with the Philippine Financial Reporting Standards or *PFRS*.

The audited consolidated financial statements are presented in Philippine peso, the *Company*'s functional and presentation currency as defined under *PFRS*. All values are rounded to the nearest million peso, except when otherwise indicated. The exchange rate used to translate U.S. dollars to Philippine peso in this report and in the accompanying audited consolidated financial statements is US$1.00 to ₱43.84, the closing rate on December 30, 2010 (the last trading day in year 2010) quoted through the Philippine Dealing System.

Financial Highlights and Key Performance Indicators

(Amounts in millions, except financial ratios, earnings per share, and operational data)	As at December 31			% Change	
	2010	2009	2008	2010 v 2009	2009 v 2008
Condensed Statements of Financial Position					
Total assets	₱178,968	₱172,129	₱169,885	4.0	1.3
Current assets	55,757	44,685	48,735	24.8	(8.3)
Cash and cash equivalents	24,370	17,068	5,402	42.8	216.0
Equity attributable to equity holders of the	58,969	57,369	52,607	2.8	9.1
Total debt	21,221	21,816	26,187	(2.7)	(16.7)
Current liabilities	44,405	42,123	45,837	5.4	(8.1)
Financial Ratios					
Debt to equity	0.36	0.38	0.50	-	-
Current ratio	1.26	1.06	1.06	-	-
Operational Data					
Number of customers (in thousands)					
Residential	4,412	4,277	4,143	3.2	3.2
Commercial	421	410	414	2.7	(1.0)
Industrial	10	10	10	-	-
Streetlights	4	4	4	-	-

	For the years ended December 31			% Change	
	2010	2009	2008	2010 v 2009	2009 v 2008
Condensed Statements of Income					
Revenues	₱245,461	₱184,550	₱191,775	33.0	(3.8)
Costs and expenses	231,024	175,571	186,575	31.6	(5.9)
Income before income tax	14,437	8,979	5,200	60.8	72.7
Net income	10,117	6,356	3,133	59.2	102.9
Net income attributable to equity holders of the parent	9,685	6,005	2,800	61.3	114.5
Earnings per share					
Basic	8.59	5.42	2.54	58.5	113.4
Diluted	8.59	5.42	2.53	58.5	114.2
Financial Ratios					
Profit margin	4%	3%	2%	-	-
Return on equity	17%	11%	5%	-	-
Asset turnover	1.40	1.08	1.10	-	-
Condensed Statements of Cash Flows					
Cash generated from operating activities	₱20,358	₱29,270	₱14,337	(30.4)	104.2
Cash used in investing activities	(6,292)	(8,770)	(5,119)	(28.3)	71.3
Capital expenditures	*9,053*	*8,890*	*9,175*	1.8	(3.1)
Cash used in financing activities	(6,764)	(8,834)	(8,692)	(23.4)	1.6
Operational Data					
Electricity sales volume (in GWh)	30,247	27,516	27,049	9.9	1.7
System loss[1]					
MERALCO	7.94%	8.61%	9.28%	(7.8)	(7.2)
CEDC	3.81%	3.86%	4.76%	(1.3)	(18.9)

[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. It provides power to 4.8 million customers in 31 cities and 80 municipalities, which include the whole of Metro Manila, the provinces of Rizal, Cavite and Bulacan, and parts of Pampanga, Batangas, Laguna and Quezon. Business establishments in the franchise area account for almost 46% of the country's Gross Domestic Product or *GDP*.

Through Clark Electric Distribution Corporation or *CEDC*, a 65%-subsidiary, it holds the power distribution franchise for Clark Special Economic Zone in Clark, Pampanga. *CEDC* franchise area covers 32 square kilometres and 1,611 customers.

The *Company* is organized into three major operating segments, namely, power distribution, real estate and contracts, services and others. In 2010, *MERALCO* PowerGen Corporation or *MPG* (formerly Asian Center for Energy Management), a wholly owned subsidiary, was reorganized as the *Company*'s vehicle for potential entry into power generation. As at December 31, 2010, *MPG* has just begun development of the proposed power generation plants.

BUSINESS SEGMENTS		
Power	**Real Estate**	**Contracts, Services and Others**
Distribution • *MERALCO* • *CEDC* Generation • *MPG*	• Rockwell Land Corporation or *Rockwell Land*	• *MERALCO* Industrial Engineering Services Corporation or *MIESCOR*, and subsidiaries • *MERALCO* Financial Services Corporation or *Finserve* • Lighthouse Overseas Insurance Limited or *LOIL* • Republic Surety and Insurance Company, Inc. or *RSIC* • Corporate Information Solutions, Inc. or *CIS* and subsidiaries • e-*MERALCO* Ventures, Inc. or *e-MVI* • *MERALCO* Energy, Inc. or *MEI*

RESULTS OF OPERATIONS

The table summarizes the consolidated results of operations and the contribution of each business segment to the *Company*'s revenues, costs and expenses, and net income for the years ended December 31, 2010, 2009 and 2008.

	Power Distribution	Real Estate	Contracts, Services and Others	Inter-segment transactions	Consolidated
			(Amounts in millions)		
For the year ended December 31, 2010					
Revenues	₱239,164	₱3,375	₱4,597	(₱1,675)	₱245,461
Costs and expenses	225,905	2,785	3,193	(859)	231,024
Net income	9,443	444	958	(728)	10,117
Net income attributable to equity holders of the parent	9,405	228	780	(728)	9,685
For the year ended December 31, 2009					
Revenues	178,752	2,877	3,703	(782)	184,550
Costs and expenses	170,694	2,447	2,476	(46)	175,571
Net income	5,881	287	859	(671)	6,356
Net income attributable to equity holders of the parent	5,852	146	678	(671)	6,005
For the year ended December 31, 2008					
Revenues	187,063	2,213	3,056	(557)	191,775
Costs and expenses	182,358	1,896	1,655	666	186,575
Net income	3,181	180	995	(1,223)	3,133
Net income attributable to equity holders of the parent	3,145	92	786	(1,223)	2,800

2010 compared with 2009

On a Consolidated Basis

Revenues

The *Company* registered consolidated revenues for the year ended December 31, 2010 amounted to ₱245,461 million, 33% higher compared with the ₱184,550 million for the same period last year. Sales from all operating segments increased during the year with the highest registered by power distribution. The robust sales were brought about by the increase in electric spending and the delayed implementation of the rate adjustment approved by the Energy Regulatory Commission or *ERC*. The increase in electricity spending is attributable to (i) increased number of customers across all customer classes, (ii) growth in various industries as restocking activities resume after the global economic crisis, (iii) unusually warmer temperature during the first half of the year and, (iv) election spendings. Sales from electricity amounted to ₱239,164 million, an increase of ₱60,412 million, or 34%, from ₱178,752 million for the year ended December 31, 2009.

The following table shows the composition of the *Company*'s consolidated revenues for the years ended December 31, 2010 and 2009 by business segment:

	2010	%	2009	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱239,164	97	₱178,752	97	₱60,412	34
Real estate	3,375	1	2,877	1	498	17
Contracts, services and others	4,597	2	3,703	2	894	24
Inter-segment transactions	(1,675)	-	(782)	-	(893)	114
Consolidated	**₱245,461**	**100**	**₱184,550**	**100**	**₱60,911**	**33**

Costs and Expenses

Consolidated costs and expenses amounted to ₱231,024 million for the year ended December 31, 2010, ₱55,453 million higher than the ₱175,571 million last year, primarily due to higher purchased power costs, increased provision for doubtful accounts, accrual for compensation and employee benefits, including adjustments for current year's costs of the concluded Collective Bargaining Agreement, and adjustments in regulatory expenses due to the *ERC*.

The following table shows the breakdown of the *Company*'s consolidated costs and expenses for the years ended December 31, 2010 and 2009 by business segment:

	2010	%	2009	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱225,905	98	₱170,694	97	₱55,211	32
Real estate	2,785	1	2,447	1	338	14
Contracts, services and others	3,193	1	2,476	2	717	29
Inter-segment transactions	(859)	-	(46)	-	(813)	1,767
Consolidated	**₱231,024**	**100**	**₱175,571**	**100**	**₱55,453**	**32**

Net Income

The 2010 consolidated full year results reflect higher recurring net income compared with 2009 mainly as a result of increased volume of energy sold. The unprecedented 10% growth in demand was the result of unusually high temperatures, higher consumption brought about by election spending in the first half of 2010 and of the upturn in business expansions within the franchise area throughout the year. In addition, the combined effect of the 3% increase in the number of billed customers to 4.8 million albeit delayed implementation of the distribution rate adjustment for the 3rd Regulatory Year (July 1, 2009 – June 30, 2010) of the 2nd Regulatory Period and the notably lower interest charge as a result of the refinancing concluded in 2009 resulted in a record performance for the year.

The following table shows the breakdown of the *Company*'s consolidated net income for the years ended December 31, 2010 and 2009 by business segment:

	2010	%	2009	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱9,443	93	₱5,881	93	₱3,562	61
Real estate	444	4	287	5	157	55
Contracts, services and others	958	10	859	13	99	12
Inter-segment transactions	(728)	(7)	(671)	(11)	(57)	9
Consolidated	**₱10,117**	**100**	**₱6,356**	**100**	**₱3,761**	**59**

Net Income Attributable to Equity Holders of the Parent

Consolidated net income attributable to equity holders of the parent increased to ₱9,685 million for the year ended December 31, 2010 from ₱6,005 million last year. Consolidated core income increased by ₱5,152 million to ₱12,155 million in 2010 from ₱7,003 million in 2009. Consolidated basic and diluted earnings per share as at December 31, 2010 increased to ₱8.59 from ₱5.42 as at December 31, 2009, due to the 61% increase in the consolidated net income attributable to equity holders of the parent. The weighted average number of common shares is 1,127 million and 1,108 million for the years ended December 31, 2010 and 2009, respectively.

On a Business Segment Basis

Power Distribution

Revenues

Revenues generated from power distribution amounted to ₱239,164 million for the year ended December 31, 2010, higher by 34% compared with ₱178,752 million in 2009. The composition of revenues from the power distribution for the years ended December 31, 2010 and 2009 is summarized in the following:

					Change	
	2010	**%**	**2009**	**%**	**Amount**	**%**
			(Amounts in millions)			
Electric revenues						
Pass-through charges						
Generation charge	₱158,439	66	₱107,635	60	₱50,804	47
Transmission charge	25,429	11	23,250	13	2,179	9
System loss charge	11,567	5	16,108	9	(4,541)	(28)
	195,435	82	146,993	82	48,442	33
Wheeling charges						
Distribution charge	29,518	12	21,276	12	8,242	39
Supply charge	8,705	4	6,560	4	2,145	33
Metering charge	5,506	2	3,923	2	1,583	40
	43,729	18	31,759	18	11,970	38
Total	**₱239,164**	**100**	**₱178,752**	**100**	**₱60,412**	**34**

Pass-Through Charges

For the year ended December 31, 2010, pass-through charges increased by ₱48,442 million, or 33% to ₱195,435 million compared with ₱146,993 million in 2009, as a result of higher average generation charge during the year, partially offset by the decrease in the average recoverable system loss charge to ₱11,567 million from ₱16,108 million. System loss rate dropped by 70 basis points from 8.6% for the year ended December 31, 2009 to 7.9% for the year ended December 31, 2010, 0.6 percentage points below the *ERC*-imposed system loss cap of 8.5%.

Wheeling Charges

Wheeling charges, which consists of distribution, supply and metering charges amounted to ₱43,729 million, higher by 38% from ₱31,759 million in 2009, mainly as a result of higher electric spending and the delayed Performance-based Rate or *PBR* adjustment in April 2010. Energy sold went up to 30,247 GWh from 27,516 GWh in 2009, up by a record 10% year-on-year growth, surpassing by multiples the average growth of 2% over the past five years. In addition, the number of customers served increased to 4.8 million, an additional of 146,122 from 4.7 million customers served in 2009.

The following table summarizes the customer count and the corresponding electric consumption per customer class for the years ended December 31, 2010 and 2009:

	No. of Customers (in thousands)		Electricity Sales (in GWh)		% Change	
					No. of	Electricity
Customer Class	**2010**	**2009**	**2010**	**2009**	**Customers**	**Sales**
Residential	4,412	4,277	9,540	8,904	3	7
Commercial	421	410	11,830	10,922	3	8
Industrial	10	10	8,734	7,548	-	16
Streetlights	4	4	143	142	-	1
Total	**4,847**	**4,701**	**30,247**	**27,516**	**3**	**10**

Sales to industrial customers increased by 16% to 8,734 GWh. The turnaround in industrial energy sales from 2009 is attributable to increased consumption, particularly by manufacturers of semiconductors, electronics, food and plastic products. Energy sold to commercial customers registered an increase of 8% to 11,830 GWh in 2010. This growth was driven by the real estate, transport, telecommunications companies and private services consisting of malls, call centers and Business Process Outsourcing or *BPO* services. Sales to residential customers increased by 7% to 9,540 GWh.

In April 2010, *MERALCO* implemented the *ERC*-approved *PBR* adjustment of ₱0.269 per kWh in average distribution rate increasing from ₱1.2227 per kWh to ₱1.4917 per kWh. The unbundled components of the distribution rates are as follows:

	Rate per kWh		
	2010	**2009**	**Increase**
Distribution charge	₱0.9991	₱0.8058	₱0.1933
Supply charge	0.3026	0.2560	0.0466
Metering charge	0.1900	0.1609	0.0291
Total	**₱1.4917**	**₱1.2227**	**₱0.2690**

CEDC's average distribution rate was at ₱0.71 per kWh for the year ended December 31, 2010, slightly higher than the rate in 2009.

Costs and Expenses

Costs and expenses of the power distribution segment increased by ₱55,211 million, or 32%, to ₱225,905 million in 2010 compared with ₱170,694 million in 2009.

Breakdown of costs and expenses is summarized in the following table:

	2010	%	2009	%	Change Amount	Change %
			(Amounts in millions)			
Purchased power	₱200,916	89	₱150,928	88	₱49,988	33
Operations and maintenance	16,068	7	13,592	8	2,476	18
Depreciation and amortization	5,796	3	4,745	3	1,051	22
Taxes, fees and permits	817	-	329	-	488	148
Provision for probable losses from refund - net	4,118	2	2,172	1	1,946	90
Interest and other financial charges	310	-	3,243	2	(2,933)	(90)
Interest and other financial income	(2,017)	(1)	(3,852)	(2)	1,835	(48)
Equity in net earnings of associates and a joint venture	(1,012)	-	(953)	-	(59)	6
Others	909	-	490	-	419	86
Total	**₱225,905**	**100**	**₱170,694**	**100**	**₱55,211**	**32**

Purchased Power

For the year ended December 31, 2010, purchased power costs amounted to ₱200,916 million, an increase of 33% from ₱150,928 million in 2009 brought about by the higher electricity consumption particularly from the industrial customers and increased in average purchased power cost per kWh. The volume of power purchased from the National Power Corporation or *NPC*, Wholesale Electricity Spot Market or *WESM* and Independent Power Producers or *IPPs* increased to 32,925 GWh, 9% higher compared with 30,173 GWh in 2009.

Generation and transmission charges account for 82% of the total electricity sales. The average pass-through generation charge in 2010 amounted to ₱5.43 per kWh. The average purchase price from *WESM* was ₱8.31 per kWh, almost three times the price in 2009 of ₱2.78 per kWh. Charges by the *WESM* peaked at ₱12.16 per kWh in March 2010. Purchase power costs billed by *NPC* ranged from ₱3.68 per kWh to a high of ₱6.60 per kWh in August 2010, for an average price of ₱5.24 per kWh in 2010. *NPC*'s peak price of ₱6.60 per kWh included an unexpected ₱1.20 per kWh increase in its automatic adjustments, which was subsequently reduced by *ERC*. On the other hand, purchases under our long-term bilateral contracts with *IPP*s ranged from ₱3.75 to ₱5.83 per kWh in 2010 or an average of ₱4.55 per kWh. This was largely due to the higher dispatch and lower fuel cost of the Sta. Rita and San Lorenzo natural gas plants.

Operations and Maintenance

Operations and maintenance expense increased by ₱2,476 million, or 18%, to ₱16,068 million for the year ended December 31, 2010 compared with ₱13,592 million for the year ended December 31, 2009 brought about by the increases in salaries and wages and provision for doubtful accounts.

Depreciation and Amortization

Depreciation expense for the year ended December 31, 2010 amounted to ₱5,796 million, 22% higher compared with ₱4,745 million for the year ended December 31, 2009. Increase in the depreciation expense is attributed to the 35 electric projects completed during the year. The major capital projects during the year included, among others, the commissioning of the NAIA-3 and Fort Bonifacio Global City Taguig substations and the construction of the Kaybiga-Novaliches and the Tagaytay-West-Tagaytay 115kV Lines.

Taxes, Fees and Permits

Taxes, fees and permits increased by ₱488 million, or 148%, to ₱817 million for the year ended December 31, 2010 compared with ₱329 million in 2009 brought about by the increase in the *ERC* regulation and supervision fees and permits to ₱653 million in 2010 compared with ₱214 million in 2009.

Provision for Probable Losses from Refund - Net

Provision for probable losses from refund - net amounted to ₱4,118 million for the year ended December 31, 2010 due to additional provisions for legal and regulatory claims during the year.

Interest and Other Financial Charges

Interest and other financial charges dropped by ₱2,933 million to ₱310 million from ₱3,243 million in 2009 as a result of the concluded refinancing of the *Company*'s debt with significantly lower rates, decrease in the applicable interest rate on customers' bill deposits as approved by the *ERC* to 0.75% from the varying rates ranging from 1% to 10% and decrease in carrying charges on *ERC*-approved refunds. In 2010, the *ERC* has not approved any refund of over-recoveries.

Interest and Other Financial Income

Interest and other financial income amounted to ₱2,017 million, ₱1,835 million or 48% lower than the ₱3,852 million earned in 2009. In 2009, the *ERC* approved *MERALCO*'s application to recover under-recoveries in the transmission charges plus carrying costs, which were recognized as part of the "interest and other financial income" account. In 2010, there was no similar approval by the *ERC*.

Equity in Net Earnings of Associates and a Joint Venture

Equity in net earnings of associates and a joint venture amounted to ₱1,012 million, 6% higher compared with ₱953 million in 2009 due to higher earnings posted by the subsidiaries particularly from *Rockwell Land*.

Net Income Attributable to Equity Holders of the Parent

Net income from power distribution attributable to parent for the year ended December 31, 2010 amounted to ₱9,405 million, ₱3,553 million or 61% higher compared with the amount earned in 2009 as a result of higher revenues generated in 2010.

Real Estate

The *Company* is involved in construction and development of several residential condominiums namely, *Number One Rockwell, The Grove* and *Edades Tower and Garden Villas* through its subsidiary, *Rockwell Land*.

Revenues

Revenues from real estate segment increased by ₱498 million or 17% to ₱3,375 million for the year ended December 31, 2010 compared with ₱2,877 million in 2009.

					Change	
	2010	**%**	**2009**	**%**	**Amount**	**%**
			(Amounts in millions)			
Sales of condominium units	**₱3,375**	**100**	**₱2,877**	**100**	**₱498**	**17**

Revenues from real estate are recognized using the percentage-of-completion method, where revenues are recognized based on the proportion of work performed during the accounting period. For the year ended December 31, 2010, *Rockwell Land* is constructing and developing three major residential condominium projects. The following table shows the progress and contribution to revenue of *Rockwell Land*'s projects.

Project	2010			2009		
	% of completion	Revenues		% of completion	Revenues	
		Amount	%		Amount	%
New Developments		(In millions)			(In millions)	
Number One Rockwell	87	₱2,702	80	53	₱2,746	96
The Grove	16	483	14	-	54	2
Edades Tower and Garden Villas	-	138	4	-	6	-
		3,323	98		2,806	98
Completed						
The Manansala	100	1	-	100	13	-
Joya Lofts and Towers	100	51	2	100	58	2
		52	2		71	2
Total		**₱3,375**	**100**		**₱2,877**	**100**

Revenue recognized from the *Number One Rockwell, The Grove and Edades Tower and Garden Villas* projects amounted to ₱3,323 million or 98% of the total revenue from real estate for the year ended December 31, 2010, increasing from ₱2,806 million in 2009. The increase is largely accounted for by the development of *The Grove* in 2010. *The Manansala* and *Joya Lofts and Towers* contributed ₱52 million and ₱71 million in the year ended December 31, 2010 and 2009, respectively, representing sale of units.

Costs and Expenses

Costs and expenses of the real estate business segment increased to ₱2,785 million in 2010, ₱338 million, or 14%, higher compared with ₱2,447 million in 2009 as shown below:

	2010	%	2009	%	Change Amount	Change %
			(Amounts in millions)			
Cost of real estate sold	₱2,640	95	₱2,230	91	₱410	18
Operations and maintenance	330	12	191	8	139	73
Depreciation and amortization	167	6	150	6	17	11
Taxes, fees and permits	54	2	77	3	(23)	(30)
Interest and other financial charges	155	6	117	5	38	32
Interest and other financial income	(580)	(21)	(332)	(14)	(248)	75
Foreign exchange losses	19	1	14	1	5	36
Total	**₱2,785**	**100**	**₱2,447**	**100**	**₱338**	**14**

Cost of Real Estate Sold

Cost of real estate sold amounted to ₱2,640 million for the year ended December 31, 2010, ₱410 million or 18% higher compared with ₱2,230 million for the year ended December 31, 2009. The higher cost of real estate sold is attributed to the progress in the constructions of *The Grove* and *Edades Tower and Garden Villas*.

Operations and Maintenance

For the year ended December 31, 2010, operations and maintenance expense of the real estate segment increased by ₱139 million, or 73% to ₱330 million compared with ₱191 million in 2009. The increase is largely due to higher provision for uncollectible accounts amounting to ₱21 million in 2010 compared with ₱0.3 million in 2009.

Depreciation and Amortization

Depreciation expense increased by ₱17 million or 11% to ₱167 million compared with ₱150 million in 2009 brought about by the depreciation charge of model units for *The Grove* and *Edades Tower and Garden Villas*.

Taxes, Fees and Permits

Taxes, fees and permits decreased by ₱23 million or 30% to ₱54 million for the year ended December 31, 2010 compared with ₱77 million in 2009 due to lower building and construction permits incurred in 2010 because *Rockwell Land* has no new condominium projects after *Edades Tower and Garden Villas*, which started in the later part of 2009.

Interest and Other Financial Charges

Interest and other financial charges increased by ₱38 million, or 32%, to ₱155 million for the year ended December 31, 2010 compared with ₱117 million in 2009 brought about by the increase in interest expense on loans to ₱154 million from ₱79 million for the year ended December 31, 2009.

Interest and Other Financial Income

Interest and other financial income increased to ₱580 million or 75% higher compared with ₱332 million in 2009 due to increase in amortization of unearned interest on trade receivables from ₱293 million to ₱550 million based on collection of installment receivable.

Net Income Attributable to Equity Holders of the Parent

Net income attributable to equity holders of parent from real estate segment for the year ended December 31, 2010 amounted to ₱228 million, ₱82 million higher or 56% compared with ₱146 million in 2009. The higher net income was brought about by the progress in the construction of the residential condominium projects.

Contracts, Services and Others

Revenues

Revenues recognized from contracts, services and other business segment increased to ₱4,597 million, or 24% higher compared with the ₱3,703 million for the year ended December 31, 2009:

The table below shows the breakdown of the revenues from contracts, services and other business segment for the years ended December 31, 2010 and 2009:

					Change	
	2010	**%**	**2009**	**%**	**Amount**	**%**
			(Amounts in millions)			
Contracts	₱1,914	42	₱1,499	40	₱415	28
Services and others	2,683	58	2,204	60	479	22
	₱4,597	**100**	**₱3,703**	**100**	**₱894**	**24**

Contracts

Revenues from contracts amounted to ₱1,914 million, ₱415 million or 28% higher compared with ₱1,499 million registered in 2009. The *Company*'s contracts business is led by *MIESCOR*. Contract revenue of *MIESCOR* was from electro-mechanical engineering contracts with the government and private sector customers, which increased by 27% in 2010 largely attributable to the Andritz Vatech Hydro-Pantabangan project.

Services and Others

Revenues from services and others increased to ₱2,683 million, 22% higher compared with ₱2,204 million generated in 2009. Higher revenues from services largely came from CIS Bayad Center, Inc. or *Bayad Center* brought about by the growth in the number of billers served and higher number of transactions handled.

Costs and Expenses

	2010	%	2009	%	Change Amount	%
			(Amounts in millions)			
Cost of contracts and services	₱1,997	63	₱1,803	73	₱194	11
Operations and maintenance	901	28	545	22	356	65
Depreciation and amortization	291	9	169	7	122	72
Taxes, fees and permits	103	3	15	-	88	587
Interest and other financial charges	29	1	21	1	8	38
Interest and other financial income	(128)	(4)	(77)	(3)	(51)	66
Total	**₱3,193**	**100**	**₱2,476**	**100**	**₱717**	**29**

Cost of Contracts and Services

Cost of contracts and services amounted to ₱1,997 million for the year ended December 31, 2010, ₱194 million or 11% higher compared with ₱1,803 million for the year ended December 31, 2009. The higher cost of contracts and services is attributed to the increase in the maintenance contracts rendered by *MIESCOR*.

Operations and Maintenance

For the year ended December 31, 2010, operations and maintenance expense of the contracts, services and other business segment increased by ₱356 million or 65% to ₱901 million compared with ₱545 million for the year ended December 31, 2009. The increase is due to higher labor costs, provision for doubtful accounts and professional fees.

Depreciation and Amortization

Depreciation expense increased by ₱122 million or 72% to ₱291 million compared with ₱169 million in 2009 brought about by the full-year recognition of depreciation expense of *RBC* towers amounting to ₱124 million in 2010 compared with ₱49 million representing depreciation expense from July to December 2009.

Taxes, Fees and Permits

Taxes, fees and permits amounted to ₱103 million for the year ended December 31, 2010, an increase of ₱88 million from ₱15 million in 2009. The increase pertains to the business permits and licenses incurred for the operation of the *RBC* towers and *Power Plant Mall* for a total of ₱76 million.

Interest and Other Financial Charges

Interest and other financial charges increased by ₱8 million or 38% to ₱29 million for the year ended December 31, 2010 compared with ₱21 million in 2009 due to the ₱188 million notes obtained by *MIESCOR* in 2010.

Interest and Other Financial Income

Interest and other financial income increased to ₱128 million, or 66% higher compared with ₱77 million in 2009. The increase came from *RBC* generating other income amounting to ₱120 million representing reimbursable charges from leases such as common use and service areas or *CUSA* and utility charges (water, electricity, *LPG* and air conditioner).

Net Income Attributable to Equity Holders of the Parent

Net income from contracts, services and other business segment attributable to the shareholder of the parent is ₱780 million, 15% higher compared with ₱678 million in 2009 due to higher revenues generated particularly from *MIESCOR*.

2009 compared with 2008

On a Consolidated Basis

Revenues

For the year ended December 31, 2009, the *Company* registered consolidated revenues of ₱184,550 million, 4% lower compared with ₱191,775 million in 2008. Revenues from sale of electricity was lower by 4% while revenues from sales of real estate, contracts and services increased by 25%.

The following table shows the composition of the *Company*'s consolidated revenues for the years ended December 31, 2009 and 2008 by business segment:

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱178,752	97	₱187,063	98	(₱8,311)	(4)
Real estate	2,877	1	2,213	1	664	30
Contracts, services and others	3,703	2	3,056	1	647	21
Inter-segment transactions	(782)	-	(557)	-	(225)	40
Consolidated	**₱184,550**	**100**	**₱191,775**	**100**	**(₱7,225)**	**(4)**

Consolidated revenues, in which electricity sales account 98%, decreased by 4% due to the ₱0.69 per kWh decrease in average generation and transmission charges as well as adjustment on estimated amount of electricity distributed but unbilled after scheduled meter readings of the various bill groups. The impact of this reduction was partially offset by the modest increase in kWh consumption of 1.7% for the year despite the effect of Typhoon Ondoy. The impact of Typhoon Ondoy is 66 GWh of foregone energy sales as a result of submerged facilities, which include substations, distribution circuits and customer connections. *MERALCO* also implemented its first distribution rate adjustment equivalent to ₱0.257 per kWh starting May 2009 under the *PBR*. The last rate adjustment of *MERALCO* was in January 2004.

Costs and Expenses

For the year ended December 31, 2009, costs and expenses amounted to ₱175,571 million, 6% or ₱11,004 million lower compared with ₱186,575 million in 2008 mainly due to lower purchased power cost in 2009.

The following table shows the breakdown of the *Company*'s consolidated costs and expenses for the years ended December 31, 2009 and 2008 by business segment:

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱170,694	97	₱182,358	98	(₱11,664)	(6)
Real estate	2,447	1	1,896	1	559	30
Contracts, services and others	2,476	2	1,655	1	813	49
Inter-segment transactions	(46)	-	666	-	(712)	(107)
Consolidated	**₱175,571**	**100**	**₱186,575**	**100**	**(₱11,004)**	**(6)**

Net Income

Consolidated net income for the year ended December 31, 2009 increased to ₱6,356 million, 103% higher compared with the net income in 2008. Despite the decrease in revenues during the year, the *Company* managed its costs and expenses resulting in a net income higher than in 2008.

The following table shows the breakdown of the *Company*'s consolidated net income for the years ended December 31, 2009 and 2008 by business segment:

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Power distribution	₱5,881	93	₱3,181	102	₱2,700	85
Real estate	287	5	180	14	107	59
Contracts, services and others	859	13	995	23	(136)	(14)
Inter-segment transactions	(671)	(11)	(1,223)	(39)	552	(45)
Consolidated	**₱6,356**	**100**	**₱3,133**	**100**	**₱3,223**	**103**

Net Income Attributable to Equity Holders of the Parent

Consolidated net income attributable to equity holders of the parent increased to ₱6,005 million for the year ended December 31, 2009 from ₱2,800 million last year. Consolidated core income increased by ₱4,398 million to ₱7,003 million from ₱2,605 million for the year ended December 31, 2008. Consolidated basic and diluted earnings per share or *EPS* as at December 31, 2009 both amounted to ₱5.42, 113% and 114% higher than the consolidated basic and diluted *EPS* as at December 31, 2008 of ₱2.54 and ₱2.53, respectively.

On a Business Segment Basis

<u>Power Distribution</u>

Revenues

The power distribution segment registered revenues of ₱178,752 million for the year ended December 31, 2009, lower by ₱8,311 million or 4% compared with ₱187,063 in 2008. The following table shows the composition of revenues from the power distribution segment for the years ended December 31, 2009 and 2008.

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Electric revenues						
Pass-through charges						
Generation charge	₱107,635	60	₱119,143	64	(₱11,508)	(10)
Transmission charge	23,250	13	25,512	14	(2,262)	(9)
System loss charge	16,108	9	16,139	9	(31)	-
	146,993	82	160,794	86	(13,801)	(9)
Wheeling charges						
Distribution charge	21,276	12	17,593	9	3,683	21
Supply charge	6,560	4	5,753	3	807	14
Metering charge	3,923	2	2,923	2	1,000	34
	31,759	18	26,269	14	5,490	21
Total	**₱178,752**	**100**	**₱187,063**	**100**	**(₱8,311)**	**4**

Pass-Through Charges

Pass-through charges decreased by ₱13,801 million, or 9%, to ₱146,993 million for the year ended December 31, 2009 as compared with ₱160,794 million in 2009 due to a decrease in average generation and transmission charges in 2009 to ₱5.28 per kWh from ₱5.97 per kWh in 2008. In addition, a net adjustment of ₱4,856 million against electricity revenues was recognized mainly for the estimated amount of electricity distributed but unbilled after scheduled meter readings. The impact of this reduction was partially offset by the increase in electricity sales of the additional kWh consumption for the year from 27,049 GWh in 2008 to of 27,516 GWh in 2009. The 2% growth in volume sales came mainly from the residential and commercial customer segments, which accounted for 72% of the total electricity sales.

Wheeling Charges

Wheeling charges, which includes distribution, supply and metering charges amounted to ₱31,759 million, higher by 21% from ₱26,269 million in 2008, mainly due to increase in average distribution rate from ₱0.97 to ₱1.15 per kWh. In May 2009, the *ERC* approved the *Parent Company*'s much delayed implementation of rate adjustments under the *PBR* scheme. Energy sold in 2009 went up by 2% to 27,516 GWh from 27,049 GWh in 2008. In addition, number of customers served increased to 4.7 million, an additional of 128,996 new customers from the 4.6 million customers served in 2008.

The following table summarizes the number of customers and the electricity consumption per customer class for the years ended December 31, 2009 and 2008:

	No. of Customers *(in thousands)*		Electricity Sales *(in GWh)*		% Change	
Customer Class	**2009**	**2008**	**2009**	**2008**	**No. of Customers**	**Electricity Sales**
Residential	4,277	4,144	8,904	8,620	3	3
Commercial	410	414	10,922	10,606	(1)	3
Industrial	10	10	7,548	7,683	-	(2)
Streetlights	4	4	142	140	-	1
Total	**4,701**	**4,572**	**27,516**	**27,049**	**3**	**2**

The residential and commercial sectors led growth during the year. While the industrial sector showed negative growth, the volume sold was a significant improvement from that at the beginning of the year. The growth in residential consumption was propelled by sustained remittances, lower inflation and lower electricity prices. The commercial service sector showed robust performance with retail trade and telecommunications accounting for 9% and 18% of the growth. The year also saw self-generating customers returning to the grid to take advantage of the lower ecozone rates, which contributed 237 GWh to the 2009 volume as well as the integration of Carmelray Industrial Park 2 or *CIP2*, to the *MERALCO* distribution system. *CIP2* contributed 47 GWh.

On the other hand, *CEDC*'s average distribution rate was ₱0.70 per kWh in 2009 and 2008.

Costs and Expenses

Costs and expenses for the year ended December 31, 2009 decreased by ₱11,664 million to ₱170,694 million compared with ₱182,358 million in 2008.

Breakdown of costs and expenses for the years ended December 31, 2009 and 2008 is summarized in the following table:

					Change	
	2009	**%**	**2008**	**%**	**Amount**	**%**
			(Amounts in millions)			
Purchased power	₱150,928	88	₱156,872	86	(₱5,944)	(4)
Operations and maintenance	13,592	8	13,122	7	470	4
Depreciation and amortization	4,745	3	4,294	2	451	10
Taxes, fees and permits	329	-	284	-	45	16
Provision for probable losses from refund - net	2,172	1	6,935	4	(4,763)	(69)
Interest and other financial charges	3,243	2	3,825	3	(582)	(15)
Interest and other financial income	(3,852)	(2)	(2,476)	(2)	(1,376)	56
Equity in net earnings of associates and a joint venture	(953)	(1)	(910)	-	(43)	5
Others	490	-	412	-	78	19
Total	**₱170,694**	**100**	**₱182,358**	**100**	**(₱11,664)**	**(6)**

Purchased Power

Purchased power cost, which accounted for 88% of the total costs and expenses in 2009, decreased by ₱5,944 million. Total volume of power purchased for the year ended December 31, 2009 was 30,173 GWh at an average cost of ₱5.01 per kWh compared with 29,886 GWh at an average cost of ₱5.27 per kWh in 2008.

Operations and Maintenance

Operations and maintenance expense increased from ₱13,122 million for the year ended December 31, 2008 to ₱13,592 million for the year ended December 31, 2009 largely due to increase in salaries and employees benefits. In 2009, the *Parent Company* fully amortized the cost related to the 13th Employees' Stock Purchase Plan or *ESPP* with the approval of the offering's accelerated vesting.

Depreciation and Amortization

Depreciation expense for the year ended December 31, 2009 amounted to ₱4,745 million, 10% higher compared with ₱4,294 million for the year ended December 31, 2008 brought about by the completion of several electric projects in 2009.

Taxes, Fees and Permits

Taxes, fees and permits amounted to ₱329 million for the year ended December 31, 2009, higher compared with ₱284 million for the year ended December 31, 2008. The increase is due to increase regulatory fees and permits.

Provision for Probable Losses from Refund - Net

Provision for probable losses from refund - net amounted to ₱2,172 million for the year ended December 31, 2008, 69% lower compared with ₱6,935 million in 2008. In 2009, net provision for probable refund of ₱1,179 million was reversed as a result of the approval by the *ERC* of *MERALCO*'s application to collect transmission cost under-recoveries incurred between June 2003 and July 2007. Meanwhile, from April 2008 through April 2009, *MERALCO* accumulated ₱4,528 million net over-recoveries of transmission costs for which a provision for probable refund was set-up. On October 12, 2009, the *ERC* authorized *MERALCO* to collect ₱5,348 million of transmission cost under-recoveries inclusive of carrying costs from its customers, net of disallowances amounting to ₱1,222 million.

Interest and Other Financial Charges

Interest and other financial charges decreased by ₱582 million or 15% to ₱3,243 million from ₱3,825 million in 2008 due to lower interest rates on notes payable and lower carrying charges on approved over-recoveries. Carrying charges recognized for transmission over-recoveries amounted to ₱543 million in 2009 compared with ₱934 million in 2008 for the Currency Exchange Rate Adjustment or *CERA,* refund.

Interest and Other Financial Income

Interest and other financial income amounted to ₱3,852 million, higher by ₱1,376 million, or 56%, compared with ₱2,476 million for the year ended December 31, 2008. Interest and other financial income represents interest income from bank placements, dividend income from available-for-sale investments and investments accounted for at equity, and recognition of carrying charge related to the *ERC*-approved collection of transmission cost under-recoveries. Total carrying charge on transmission under-recoveries amounted to ₱2,782 million in 2009 compared with ₱813 million in 2008 for generation under-recoveries approved by the *ERC*.

Equity in Net Earnings of Associates and a Joint Venture

Equity in net earnings of associates and a joint venture amounted to ₱953 million, 5% higher compared with ₱910 million in 2008 due to higher earnings posted by the subsidiaries for the year ended December 31, 2009.

Net Income Attributable to Equity Holders of the Parent

Net income attributable to equity holders of the parent for the year ended December 31, 2009 is ₱5,852 million, ₱2,707 million or 86% higher compared with ₱3,145 million in 2008. The higher net income was brought about by the decrease in costs and expenses of ₱11,664 million, partially offset by the decrease in revenues of ₱8,311 million.

<u>Real Estate</u>

Revenues

The real estate segment registered revenues of ₱2,877 million for the year ended December 31, 2009, 30% higher compared with ₱2,213 million in 2009 due to progress in the construction of *Number One Rockwell*, a two-tower residential building at the Rockwell Center, scheduled to be completed by the end of 2011. As at December 31, 2009, the estimated percentage of completion of the said project was 53% compared with the 19% as at December 31, 2008.

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Sales of condominium units	**₱2,877**	**100**	**₱2,213**	**100**	**₱664**	**30**

The following table shows the progress and contribution to revenue of *Rockwell Land*'s projects for the year ended December 31, 2009 and 2008.

Project	2009 % of completion	2009 Revenues Amount	2009 Revenues %	2008 % of completion	2008 Revenues Amount	2008 Revenues %
		(in millions)			(in millions)	
New Developments						
Number One Rockwell	53	₱2,746	96	19	₱1,418	64
The Grove	-	54	2	-	-	-
Edades Tower and Garden Villas	-	6	-	-	-	-
		2,806	98		1,418	64
Completed						
Joya Lofts and Towers	100	13	-	100	789	36
The Manansala	100	58	2	100	6	-
		71	2		795	-
Total		**₱2,877**	**100**		**₱2,213**	**100**

As at December 31, 2009, *Rockwell Land* has three new developments namely, *Number One Rockwell*, *The Grove* and *Edades Tower and Garden Villas*. Revenues from these projects totalled to ₱2,806 million, accounting for 98% of the total revenues from real estate in 2009. *Number One Rockwell* progressed to 53% as at December 31, 2009. The remaining 2% of ₱2,877 million came from sales of condominium units in *The Manansala* and *Joya Lofts and Towers*.

Costs and Expenses

The real estate business segment's costs and expenses increased to ₱2,447 million for the year ended December 31, 2009, ₱551 million or 29% higher compared with ₱1,896 million for the year ended December 31, 2008.

The following table shows the breakdown of the costs and expenses:

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Cost of real estate sold	₱2,230	91	₱1,646	87	₱584	35
Operations and maintenance	191	8	500	26	(309)	(62)
Depreciation and amortization	150	6	88	5	62	70
Taxes, fees and permits	77	3	63	3	14	22
Interest and other financial charges	117	5	53	3	64	121
Interest and other financial income	(332)	(14)	(429)	(22)	97	(23)
Foreign exchange losses (gains)	14	1	(25)	(2)	39	(156)
Total	**₱2,447**	**100**	**₱1,896**	**100**	**₱551**	**29**

Cost of Real Estate Sold

Cost of real estate sold increased by 35% from ₱1,646 million for the year ended December 31, 2008 to ₱2,230 million for the year ended December 31, 2009, 95% of which pertains to percentage cost of completion of *Number One Rockwell*. The accretion rate of the *Number One Rockwell* residential buildings was 34% from December 31, 2008 to December 31, 2009.

Operations and Maintenance

Operations and maintenance expense of the real estate segment decreased by ₱309 million or 62% to ₱191 million compared with ₱500 million in 2008 due to reductions in marketing and promotion expense, professional fees, commissions and amortization of pre-selling costs.

Depreciation and Amortization

Depreciation expense increased to ₱150 million, 70% higher compared with ₱88 million in 2008. The increase is attributed to the depreciation expense of model units of *The Grove* and depreciation of the completed function room at *The Grove*.

Taxes, Fees and Permits

Taxes, fees and permits increased to ₱77 million compared with ₱63 million in 2008 due to additional permits and licenses associated with the development and construction of *The Grove* and *Edades Tower and Garden Villas*.

Interest and Other Financial Charges

Interest and other financial charges increased by ₱64 million or 121% to ₱117 million for the year ended December 31, 2009 compared with ₱53 million in 2008 brought about by the increase in interest expense on loans to ₱77 million from ₱51 million for the year ended December 31, 2008.

Interest and Other Financial Income

Interest and other financial income decreased to ₱332 million, 23% lower compared with ₱429 million in 2008 due to decrease in amortization of unearned interest on trade receivables from ₱450 million to ₱293 million based on collections of instalments receivable.

Net Income Attributable to Equity Holders of the Parent

Net income attributable to equity holders of parent from real estate segment for the year ended December 31, 2009 is ₱146 million, 59% or ₱54 million higher compared with ₱92 million in 2008 as a result of the progress in the construction of *Number One Rockwell*.

Contracts, Services and Others

Revenues

Revenues recognized from contracts, services and other business segment increased to ₱3,703 million, or 21% higher compared with the ₱3,056 million for the year ended December 31, 2008.

The table below shows the breakdown of the revenues from contracts, services and other business segment for the years ended December 31, 2009 and 2008.

					Change	
	2009	**%**	**2008**	**%**	**Amount**	**%**
			(Amounts in millions)			
Contracts	₱1,499	40	₱1,230	40	₱269	22
Services and others	2,204	60	1,826	60	378	21
	₱3,703	**100**	**₱3,056**	**100**	**₱647**	**21**

Contracts

Revenues from contracts amounted to ₱1,499 million, ₱269 million or 22% higher compared with ₱1,230 million registered in 2008. The increase is attributed to the improvement in the revenues of *MIESCOR* by 22% from ₱1,229 million in 2008. *MIESCOR* won a contract with the Department of Finance or *DoF* for the upgrade/rehabilitation of the latter's electro-mechanical system, a major project in 2009.

Services and Others

Services and other business segment registered revenues for the year ended December 31, 2009 of ₱2,204 million, ₱378 million or 21% higher compared with ₱1,826 million in 2008. The increase is attributed to higher revenues generated by *Rockwell Land* from the *Power Plant Mall* due to increase in commercial rental rate and foot traffic.

Costs and Expenses

	2009	%	2008	%	Change Amount	Change %
			(Amounts in millions)			
Cost of contracts and services	₱1,803	73	₱1,456	88	₱347	24
Operations and maintenance	545	22	382	23	163	43
Depreciation and amortization	169	7	44	3	125	284
Taxes, fees and permits	15	-	42	3	(27)	(64)
Interest and other financial charges	21	1	37	2	(16)	(43)
Interest and other financial income	(77)	(3)	(306)	(19)	229	(75)
Total	**₱2,476**	**100**	**₱1,655**	**100**	**₱821**	**50**

Cost of Contracts and Services

Cost of contracts and services amounted to ₱1,803 million for the year ended December 31, 2009, 24% higher compared with ₱1,456 million for the year ended December 31, 2008. The increase in the cost of contracts of *MIESCOR* in 2009 to ₱1,268 million from ₱1,056 million in 2008 was brought about by the costs related to the construction and maintenance contracts with Chevron's Tiwi and MakBan Geothermal Plants and the upgrade/rehabilitation of electro-mechanical system of the *DoF*.

Operations and Maintenance

For the year ended December 31, 2009, operations and maintenance expenses increased by ₱163 million, or 43%, to ₱545 million compared with ₱382 million for the year ended December 31, 2008 mainly due to costs related to the operation of *RBC* Towers in 2009 and the increase in employees' compensation and benefit costs.

Depreciation and Amortization

Depreciation expense increased by ₱125 million, or 284%, to ₱169 million compared with ₱44 million in 2008. The increase pertained to the depreciation expense of the *RBC* Towers.

Taxes, Fees and Permits

Taxes, fees and permits amounted to ₱15 million for the year ended December 31, 2009, a decrease of ₱27 million, or 64%, from ₱42 million in 2008. The decrease is attributable to *MIESCOR* whose taxes other than income tax dropped to ₱4 million in 2009 from ₱17 million in 2008. In 2008, a capital gains tax was recognized related to sale of the 65% stake in *CEDC* by *MIESCOR* to the *Parent Company*.

Interest and Other Financial Charges

Interest and other financial charges decreased by ₱16 million or 43% to ₱21 million compared with ₱37 million in 2008. The decrease is consistent with the reduction in the balance of long-term loans of *MIESCOR* to ₱3 million in 2009 from ₱9 million in 2008.

Interest and Other Financial Income

Interest and other financial income decreased to ₱77 million, 75% lower compared with ₱306 million in 2008 when *MIESCOR* realized a gain from sale of *CEDC* to the *Parent Company*.

Net Income Attributable to Equity Holders of the Parent

Net income attributable to equity holders of parent from contracts, services and other business segment for the year ended December 31, 2008 amounted to ₱678 million, ₱108 million or 14% lower compared with ₱786 million in 2008. The decrease in net income attributable to the equity holders of the parent is due to lower net income registered by *MIESCOR* from ₱130 million in 2008 to ₱101 million in 2009 as a result of higher costs of contracts and services. In addition, the *Company* incurred losses of ₱54 million from *RBC*, which started business operation in the second semester of 2009 with an occupancy rate of 19%.

Liquidity and Capital Resources

The following table shows the *Company*'s consolidated cash flows for the years ended December 31, 2010, 2009 and 2008 as well as the *Company*'s capitalization as at December 31, 2010, 2009 and 2008.

	2010	2009	2008
	(Amounts in millions)		
Cash Flows			
Net cash provided by operating activities	₱20,358	₱29,270	₱14,337
Net cash used in investing activities	(6,292)	(8,770)	(5,119)
Capital Expenditures	*9,053*	*8,890*	*9,175*
Net cash used in financing activities	(6,764)	(8,834)	(8,692)
Net increase in cash and cash equivalents	7,302	11,666	526
Capitalization			
Interest-bearing long-term financial liabilities			
Current portion	₱5,574	₱4,069	₱3,131
Noncurrent portion	15,498	17,234	13,228
Notes payable	149	513	9,828
Equity	63,196	61,146	56,159

As at December 31, 2010, the *Company*'s consolidated cash and cash equivalents totalled ₱24,370 million, ₱7,302 million higher compared with the balance of ₱17,068 million as at December 31, 2009. Sources of consolidated cash and cash equivalents in 2010 were cash flows from operating activities of ₱20,358 million, proceeds from long-term loans of ₱10,528 million and interest and other financial income received amounting to ₱1,058 million. Cash dividends paid amounted to ₱6,187 million, settlement of debt principal and interest totalled ₱13,536 million and, capital expenditures amounted to ₱9,053 million, of which ₱8,990 million were paid.

Operating Activities

Consolidated net cash provided by operating activities for the year ended December 31, 2010 decreased to ₱20,358 million, ₱8,912 million lower compared with ₱29,270 million in 2009. The decrease is brought about by the decrease net cash generated from operations from ₱33,067 million in 2009 to ₱25,311 million in 2010 due to increase in trade and other receivables. As at December 31, 2010, trade and other receivables – net amounted to ₱25,609 million, 19% higher compared with ₱21,600 million as at December 31, 2009. In 2010, *ERC* approved the *Company*'s application to recover under-recoveries in generation and transmission charges and began billing the approved under-recoveries thereon.

For the year ended December 31, 2009, net cash provided by operating activities increased to ₱29,270 million from ₱14,337 million in 2008. The improved operating results was partly attributable to the much delayed implementation of the approved rate adjustment under the *PBR* beginning May 2009 and improved collections.

Investing Activities

Consolidated net cash flows used in investing activities for the year ended December 31, 2010 totalled ₱6,292 million. *MERALCO* completed 35 major and residual electric capital projects in 2010 to serve new customers and to enhance the reliability and efficiency of its electric distribution system. Among the projects completed were the construction of the 115kV sub-transmission lines in Amadeo, Tagaytay and NAIA-3, and the commissioning of the substations at the Fort Bonifacio Global City or *FBGC*, Marilao and Veinte Reales.

Net cash used in investing activities for the year ended December 31, 2009 was ₱8,770 million compared with ₱5,119 million in 2008. Primary investing activity of the *Company* was the construction of distribution facilities of *MERALCO*, which totalled ₱7,914 million in 2009.

Financing Activities

Consolidated net cash used in financing activities decreased to ₱6,764 million compared with ₱8,834 million in 2009. In the last quarter of 2010, *MERALCO* prepaid the outstanding balance of its ₱6,000 million floating rate corporate notes amounting to ₱4,680 million and the ₱3,900 floating rate notes from its ₱5,500 million note facility agreement. Simultaneously, *MERALCO* obtained the ₱5,000 million and the 4,800 million fixed rate notes. Total dividends paid in 2010 totalled ₱6,187 million, 219% more than the dividends paid in 2009. *MERALCO* pays regular cash dividends equivalent to 50% of the core net income.

Net cash used in financing activities amounted to ₱8,834 million for the year ended December 31, 2009 as against ₱8,692 million for the year ended December 31, 2008. Aside from the refinancing activities done in 2009 (see related discussion under Debt Financing), *MERALCO* also paid higher dividends in 2009 totalling ₱2,820 million compared with ₱1,960 million in 2008.

Debt Financing

Consolidated debt, including notes payable, decreased by ₱595 million or 3% to ₱21,221 million as at December 31, 2010. The decrease is mainly due to payments of principal of ₱10,748 million, partially offset by additional drawings on note facility of ₱10,528 million. The new loans were used to support the capital expenditure requirements of *MERALCO* and to finance maturing debt obligations. Debt maturities of the *Company* are spread through 2020.

In 2010, Standard & Poor's re-rated and upgraded *MERALCO* to 'B+' with 'stable' outlook to reflect the significant and sustained improvement in the *Company*'s financial risk profile arising from higher tariffs and stronger electricity sales.

In 2009, *MERALCO* refinanced a total of ₱10,160 million of maturing debts. Refinancing was provided by consortia of local banks and financial institution in January 2009 (₱5,000 million) and another local bank in December (₱5,500 million). In addition, the *Company* drew new loans totalling ₱4,834 million, ₱1,183 million of which was drawn by *Rockwell Land*. Consolidated debt as at December 31, 2009 decreased by ₱4,371 million to ₱21,816 million compared with ₱26,187 million in 2008.

For further details on long-term debt, see *Note 21 – Interest-bearing Long-term Financial Liabilities* to the accompanying audited consolidated financial statements.

Equity Financing

Consistent with the provisions of PAS 32, "Financial Instruments: Disclosure and Presentation", the *Company*'s preferred shares were reclassified 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 for 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.

As at December 31, the *Company*'s capital stock consists of:

(Amounts in millions except par value)	**2010**	2009
Common stock – ₱10 par value		
Authorized – 1,250,000,000 shares	₱12,500	₱12,500
Issued and outstanding	11,273	11,273

Of the total authorized common shares of 1,250 million, 1,127 million shares are issued and outstanding as at December 31, 2010 and 2009. This included the 7.2 million fully vested and paid shares under the 13th *ESPP* offering and subscriptions under the 13thA and 14th *ESPP* offerings.

Consolidated cash dividends declared to shareholders in 2010, 2009 and 2008 amounted to ₱7,834 million, ₱2,695 million and ₱1,116 million, respectively.

The table below summarizes the cash dividends declared in 2010, 2009, and 2008:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
				(In millions)
March 22, 2010	April 21, 2010	May 11, 2010	₱3.15	₱3,551
July 26, 2010	August 23, 2010	September 16, 2010	2.50	2,818
December 13, 2010	December 29, 2010	January 17, 2011	1.30	1,465
				₱7,834
October 29, 2009	November 13, 2009	December 11, 2009	₱1.50	₱1,617
May 26, 2009	June 9, 2009	June 30, 2009	1.00	1,078
				₱2,695
August 26, 2008	September 25, 2008	October 21,2008	₱0.50	₱559
March 17, 2008	April 16, 2008	May 13, 2008	0.50	557
				₱1,116

RISK FACTORS

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

a. Regulated rates and cost recoveries
b. Volume sales and Philippine economic conditions
c. Electricity supply
d. Currency exchange rates
e. Industry restructuring

Regulated Rates and Cost Recoveries

- The most significant determinants of *MERALCO*'s rate structure vis-à-vis operating results are "allowable returns" and "permitted cost recoveries". Rates billed by the Company are approved by the Energy Regulatory Commission or *ERC* and are set to allow a reasonable rate of return on investments. The *Company*'s rate structure also allows pass-through of certain purchased power costs, system loss up to an annual cap enforced by the *ERC*, and taxes.

  In accordance with the provisions of the Electric Power Industry Reform Act or *EPIRA* of 2001, the *ERC* approved the Distribution Wheeling Rate Guidelines or *DWRG*, later renamed, Rules for Setting Distribution Wheeling Rates or *RDWR*, which took effect on January 29, 2005. The Performance-Based Regulation or *PBR* is embodied in the *DWRG*.

  Under *PBR*, tariffs are set according to forecasts of performance and capital and operating expenditures. The *RDWR* also employs a penalty/reward mechanism that adjust tariffs upwards and downwards depending on the utility's actual performance. The *Company* filed its first rate adjustment application based on the new rate-making scheme on September 1, 2006. After a series of hearings and regulatory evaluations, the new *PBR*-based tariff was to have been implemented by July 2007.

  On August 31, 2007, the *ERC* issued its Final Determination, which set forth its evaluation of *MERALCO*'s annual revenue requirement and approved the performance incentive scheme and price control arrangements that will apply to *MERALCO* during the second Regulatory Period (from July 1, 2007 to June 30, 2011). The approved Maximum Average Prices or *MAP* were ₱1.167 per kWh, ₱1.260 per kWh, ₱1.361 per kWh, and ₱1.471 per kWh for the Regulatory Years or *RY*s 2008, 2009, 2010 and 2011, respectively.

  The *ERC* mandated the shift from Return on Rate Base or *RORB* to *PBR* for all investor-owned distribution utilities or *DU*s. The shift would be done in batches, with all investor-owned DUs expected to have shifted by 2011. *MERALCO*, along with Cagayan Electric Power and Light Company or *CEPALCO* and Dagupan Electric Corporation or *DECORP*, are the first three *DU* entrants to *PBR*. *DECORP* and *CEPALCO* began implementing *PBR* tariffs in October 2008, while *MERALCO* started implementing *PBR* tariffs in May 2009.

  Similarly, the rate-setting mechanism of Clark Electric Distribution Corporation or *CEDC*, a 65% owned subsidiary, is likewise in compliance with *ERC* regulations. After the unbundling of its rates in accordance with the *ERC* guidelines, *CEDC* shall also become an entrant to the *PBR*. *CEDC* filed its *PBR* reset application on September 24, 2010 covering the regulatory period October 1, 2011 to September 30, 2015. To date, *CEDC* is awaiting for the release of Draft Determination on its application for public comments.

- The pass-through of allowable costs or costs that do not entail a revision of the rate base and/or rate of return of the *Company* 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. The guidelines prescribe a semi-annual verification process. 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 or *SC*, 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 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 *DU*s, 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 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 *DU*s, 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 *DU*s.

  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 period of the *DU*s and their suppliers in the confirmation of the system loss. However, the Commission 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 *DU*s' consolidated applications, and set 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 *DU*s in Luzon to file their respective applications. Subsequent filings shall likewise be every three years thereafter.

  On March 31, 2011, *MERALCO* filed its consolidated application to confirm its under- or over-recoveries accumulated from June 2003 to December 2010, docketed as *ERC* Case No. 2011-010 CF.

- *MERALCO*'s recovery of costs through the system loss charge was limited to 9.5% of the total power purchased by *MERALCO* in accordance with Republic Act or *RA* No. 7832, or the Anti-Electricity Pilferage Act. System loss is comprised of technical losses, or the electrical energy lost in the process of distributing power to its customers, and non-technical losses, mainly due to pilferage. Up to 2007, *MERALCO*'s system loss levels were in excess of the 9.5% cap.

On August 6, 2008, the *ERC* released a draft Resolution that: (i) will reduce the system loss cap for private *DU*s to 8% effective January 2008 and (ii) will change the treatment of company use, from a component of the system loss charge to being part of operations and maintenance expenses. The draft Resolution further stated that the treatment of company use of electricity as part of operations and maintenance expenses shall commence on the next reset for utilities under the *PBR* and that the manner by which the utility will be rewarded for its efforts in system loss reduction shall be addressed in the Performance Incentive Scheme or *PIS* under the *PBR*. After receiving written comments and conducting public consultations, the *ERC* eventually released on December 8, 2008 a Resolution setting the recoverable rate of system loss for private *DU*s at 8.5% effective January 2010.

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 system loss 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 level of system loss cap to not less than 9%. On November 18, 2010, the first and only hearing on the Petition was conducted by the *ERC*. Thereafter, *MERALCO* was directed to submit its Formal Offer of Evidence. The Petition is awaiting the resolution by the Commission.

For the year ended December 31, 2010, *MERALCO*'s system loss improved by 67 basis points from the 8.61% registered in December 31, 2009 to 7.94%. *CEDC*'s system loss also improved by 5 basis points from 3.86% for the year ended December 31, 2009 to 3.81% for the year ended December 31, 2010.

Volume Sales and Philippine Economic Conditions

The sale of electric energy is driven mainly by prevailing economic conditions and the number of customers being served by the *Company*. The *Company*'s franchise area accounts for almost 46% of the Philippines' *GDP*, with 33% from Metro Manila.

In 2010, Philippine's *GDP* posted at 7.3%, the highest performance in more than 20 years brought about by strong foreign trade performance, global economic recovery and election-related spending. From 2006 to 2010, Philippine *GDP* grew at a compounded annual rate of approximately 6.2%, compared with 3.4% during the period from 2005 to 2009.

With the Philippine *GDP* growth of 7.3% in 2010, the *Company*'s energy sales volume grew by 10% from 27,516 GWh in 2009 to 30,247 GWh in 2010. All customer classes registered increases in their electric spending with sales to industrial customers the highest at 16% brought about by increased economic activities.

Billed customers grew steadily over the last five years, with 146,122 new customers representing an increase of 3%, in 2010. As at December 31, 2010, total customer count was 4.8 million. Residential customers, while consuming 32% of the total energy sold, account for 91% of the total 4.8 million customers. Commercial customers totalling 0.4 million accounts for 39% of the total energy sold. Approximately, 0.1 million industrial customers account for 29% of energy sold.

Electricity Supply

The *Company* does not operate its own generation capacity yet and purchases all of the power that it distributes from the National Power Corporation or *NPC* and Independent Power Producers or *IPP*s. For the year ended December 31, 2010, *MERALCO* purchased 40.6% of its requirements from *NPC*, 14.1% from the Wholesale Electricity Spot Market or *WESM*, a venue where suppliers and buyers trade electricity as a commodity, and the balance from its *IPP*s.

On November 22, 2006, the *NPC* and the C*ompany* signed a Transition Supply Contract or *TSC*, which expires at the earlier of the end of five years from effectivity date or, if open access is introduced within the 5-year period, at the end of one year from the introduction of open access. On July 20, 2007, *MERALCO* and *NPC* signed an Addendum to its *TSC* increasing the annual contracted quantities. The amended schedule of contracted energy is 7,156 GWh in 2007, 7,624 GWh in 2008, and 7,666 GWh for each of 2009 to 2011.

In relation to a Petition filed by the Bureau of Trade Regulation and Consumer Protection of the Department of Trade and Industry against the *Company*, the *ERC* directed *MERALCO* to negotiate and contract with the *NPC* for an increase in the *TSC* contracted volume to match this with the updated demand forecast, net of the quantities under its *IPP* contracts. To date, discussion between *MERALCO* and *NPC* has not yet concluded.

With respect to *CEDC*, its supply contract with the *NPC* for the purchase of electricity was renewed for the period March 26, 2008 to March 25, 2013, with minimum contract energy per annum as follows:

Year	GWh
March 26, 2008 to March 25, 2008	250
March 26, 2008 to March 25, 2010	256
March 26, 2010 to March 25, 2011	263
March 26, 2011 to March 25, 2012	269
March 26, 2012 to March 25, 2013	276

Currency Exchange Rates

Changes in the value of the peso against other currencies, particularly the U.S. dollar, may affect the *Company*'s operating results and financial condition in a number of respects. As at December 31, 2010, while substantially all the *Company*'s revenues are denominated in Philippine peso, less than 1% of the principal amount of the *Company*'s indebtedness, most of the *Company*'s capital expenditures, a substantial portion of the *Company*'s power purchased costs and interest expense and a small portion of the *Company*'s operations and maintenance expenses are denominated in, or indexed to, the U.S. dollars, and may increase significantly in peso terms as a result of any substantial depreciation of the peso. The peso has appreciated vis-à-vis the U.S. dollar, from ₱46.20:US$1.00 as at December 31, 2009 to ₱43.84:US$1.00 as at December 31, 2010.

On October 22, 2008, the *ERC* released an order directing *MERALCO* to refund over a period of 12 months over-recoveries in the Currency Exchange Rate Adjustment or *CERA* mechanism incurred from June 2003 to December 2006. The Commission directed *MERALCO* to refund the *CERA* over-recoveries, along with carrying charges estimated at ₱833 million, over a period of 12 months, equivalent to ₱0.1461 per kWh.

On December 4, 2008, *MERALCO* filed a Motion, that asked the *ERC* to defer the *CERA* refund and to implement it no earlier than the February 2008 billing cycle. *MERALCO*'s motion for the deferral of the *CERA* refund was granted by the *ERC* and *MERALCO* was authorized to implement a *CERA* refund "equivalent to ₱0.0400 per kWh starting the March 2009 billing cycle until such time that the full amount shall have been refunded.

On April 25, 2009, the *ERC* released an Order reinstating its directive for *MERALCO* to refund the *CERA* over-recovery at a rate of ₱0.1461 per kWh. The acceleration of the *CERA* refund would cushion the impact on the consumers of the implementation of *MERALCO*'s approved *MAP* for *RY* 2008, both of which were implemented beginning May 2008. The refund of the *CERA* over-recoveries was completed in April 2010.

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 distribution utilities, 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

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. The *ESCA* amends certain provisions of *RA* No. 9257, which mandates the grant of benefits to senior citizens and to institutions catering to senior citizens.

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

The *ESCA* took effect on April 22, 2010 and its Implementing Rules and Regulations or *IRR* were promulgated by the Department of Social Welfare and Development or *DSWD* last June 18, 2010. The *IRR* provides that utility-regulatory agencies (such as the *ERC*) shall, within six months after the *IRR* takes effect, "formulate supplemental guidelines to cover recovery rate mechanisms and/or sharing of burden, among other concerns of the distribution utilities," in the implementation of the discounts provided under the law.

On August 25, 2010, the *ERC* released for comments the "Draft Rules for the Calculation of Senior Citizen Discounts and Subsidy on Electricity Consumption under Section 4 and 5 of *RA* No. 9994". Public consultations were held last September 22, 29, and October 6, 2010. The *ERC* has yet to finalize and promulgate the said rules. After the conduct of consultations, the *ERC* released the second draft on November 15, 2010 for comments.

On January 5, 2011, the *ERC* released Resolution No. 23, Series of 2010 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". The Resolution was published in Daily Tribune on January 6, 2011, and in Manila Times on January 7, 2011. It became effective on January 22, 2011. *MERALCO* implemented the discount starting the February 2011 billing.

OTHER QUANTITATIVE AND QUALITATIVE DISCLOSURES

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

For further details on contingencies, see *Note 33 – Contingencies* to the accompanying audited consolidated financial statements.

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

Not Applicable.

(iii) Any material commitments for capital expenditures, the general purpose of such commitments, and the expected sources of funds for such expenditures should be described;

2011 Capital Expenditure Requirements (*In millions)*

Electric capital projects	₱8,299
Non-electric projects and other capitalized items	2,603
Total Capital Expenditures	**₱10,902**

As at December 31, 2010, the *Company* has met, and expects that it will continue to meet its capital expenditure requirements primarily from cash flow from operations, and working capital.

The *Company* 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.

The *Company* has an approved capital expenditure budget of ₱10,902 million for the year ending December 31, 2011, of which about 76% 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 2011 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 ₱10,902 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 company facilities, and initiate practical and cost-effective projects to correct system deficiencies.

(iv) 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**

On February 18, 2011, the *ERC* pursuant to its mandate under Section 3, Rule 12 of the *EPIRA* Implementing Rules and Regulations issued an Order setting public hearings for the purpose of determining whether or not Open Access and Retail Competition may already be declared. The *DOE*, *NPC, PEMC* and *PSALM* were directed to appear at the hearings and present evidence on the matter. *MERALCO* is an intervenor in said case. Hearings commenced on March 7, 2011 and the involved parties have been directed to submit a legal memorandum on this matter. The latest hearing was conducted on April 6, 2011 and all parties were given until April 16, 2011 to file their comments on the submitted legal memoranda, after which, the case will be deemed submitted for resolution by the Commission.

(v) Any significant elements of income or loss that did not arise from the registrant's continuing operations;

None

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

Seasonality of Operations and Growth Drivers

Approximately 97% of the Company'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 1st 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 2nd 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. Despite the onset of the rainy season which tapers cooling requirements of commercial establishments, kWh sales typically peaks on the 3rd Quarter of the year. 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 4th 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 the *Company*'s quarterly sales in GWh.

Period	2010	2009	2008
First Quarter	6,996	6,124	6,214
Second Quarter	7,954	6,993	6,976
Third Quarter	7,710	7,275	6,983
Fourth Quarter	7,587	7,124	6,876
Total	30,247	27,516	27,049

The businesses of all other subsidiaries are not highly seasonal.

Report of the Audit and Risk Management Committee to the Board of Directors

The Audit and Risk Management Committee's primary role and responsibility, as embodied in its Charter, is to assist the Board of Directors in fulfilling its oversight responsibilities to provide shareholders with timely, meaningful and reliable financial reports and to protect the interests of the shareholders, customers, employees and the public through effective identification of assessment, monitoring and management risks.

To fulfill its responsibilities, the Audit and Risk Management Committee has focused on the following tasks in 2010:

- An independent director chaired the Committee.
- Held nine meetings during the year.
- Reviewed and discussed the quarterly unaudited consolidated financial statements and the audited consolidated annual financial statements of the Company, including management's significant judgments and estimates that formed part of the financial statements, with the management, the internal auditors and the independent auditors of the Company. Responsibilities on the financial reporting are further defined as follows:
    - Management has the primary responsibility for preparing the financial statements and the financial reporting process; and
    - The independent external auditors are responsible for expressing an opinion on whether the Company's consolidated audited financial statements conform with Philippine Financial Reporting Standards.
- Endorsed the nomination of SGV & Co. as the independent auditors for 2010 to the Board of Directors.
- Discussed and approved the overall scope and respective audit plans of the internal auditors and the independent auditors.
- Discussed and reviewed the results of the audit findings and recommendations of the internal and independent auditors and their assessment of the Company's internal controls and the overall quality of the financial reporting process.
- Reviewed and approved all services provided by independent auditors to the Company and the related fees for such services.
- Reviewed the reports of the internal auditors and regulatory agencies, where applicable, ensuring that management is taking timely and appropriate corrective actions, including those addressing internal control and compliance issues.

Based on the reviews and discussions undertaken, and subject to the limitations on the roles and responsibilities referred to above, the Audit and Risk Management Committee recommended to the Board of Directors the approval of the audited consolidated financial statements for the year ended December 31, 2010 and their filing with the Securities and Exchange Commission and other regulatory bodies.

On behalf of the Audit and Risk Management Committee,

Former Chief Justice ARTEMIO V. PANGANIBAN
Chairman, Audit and Risk Management Committee

February 21, 2011

Statement of Management's Responsibility for Financial Statements

The management of Manila Electric Company is responsible for all information and representations contained in the consolidated statements of financial position as at December 31, 2010 and 2009 and the consolidated statements of income, consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for each of the three years in the period ended December 31, 2010, and the summary of significant accounting policies and other explanatory notes. The consolidated financial statements have been prepared in accordance with Philippine Financial Reporting Standards and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration of materiality.

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

The Board of Directors reviews the consolidated financial statements before such statements are approved and submitted to the stockholders of the Company.

SyCip Gorres Velayo & Co., the independent auditors appointed by the Board of Directors and stockholders, have audited the consolidated financial statements of the Company and the major subsidiaries in accordance with auditing standards generally accepted in the Philippines and have expressed their opinion on the fairness of presentation upon completion of such audit, in their report to the Board of Directors and stockholders.

MANUEL M. LOPEZ
Chairman of the Board

MANUEL V. PANGILINAN
President & Chief Executive Officer

RAFAEL L. ANDRADA
Treasurer

OSCAR S. REYES
Chief Operating Officer

Independent Auditors' Report

The Stockholders and the Board of Directors
Manila Electric Company

We have audited the accompanying consolidated financial statements of Manila Electric Company and Subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2010 and 2009, and the consolidated statements of income, statements of comprehensive income, statements of changes in equity and statements of cash flows for each of the three years in the period ended December 31, 2010, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 principles used and reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated 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 of December 31, 2010 and 2009, and their financial performance and their cash flows for each of the three years in the period ended December 31, 2010 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.

Gemilo J. San Pedro
Partner
CPA Certificate No. 32614
SEC Accreditation No. 0094-AR-2
Tax Identification No. 102-096-610
BIR Accreditation No. 08-001998-34-2009,
June 1, 2009, Valid until May 31, 2012
PTR No. 2641562, January 3, 2011, Makati City

February 28, 2011

Consolidated Statements of Financial Position

	Notes	December 31 2010	2009
		(Amounts in Millions)	
ASSETS			
Noncurrent Assets			
Utility plant and others - net	8, 9, 11 and 19	**₱101,009**	₱98,231
Construction in progress	8, 9 and 11	**2,241**	3,627
Investments in associates and a joint venture	10	**321**	1,203
Investment properties - net	8, 9, 11, 19, 21 and 27	**8,037**	8,021
Deferred pass-through fuel costs	12 and 26	**1,222**	3,161
Deferred tax assets - net	3 and 32	**42**	17
Other noncurrent assets - net	13, 15, 18, 26, 30, 31 and 33	**10,339**	13,184
Total Noncurrent Assets		**123,211**	127,444
Current Assets			
Cash and cash equivalents	14 and 31	**24,370**	17,068
Trade and other receivables - net	2, 13, 15 ,21, 22, 27, 29 and 31	**25,609**	21,600
Inventories - at lower of cost or net realizable value	16	**2,043**	1,857
Land and development costs - at lower of cost or net realizable value	11 and 17	**1,708**	1,191
Other current assets	18 and 31	**2,027**	2,969
Total Current Assets		**55,757**	44,685
		₱178,968	₱172,129
EQUITY AND LIABILITIES			
Equity Attributable to Equity Holders of the Parent			
Common stock	19	**₱11,273**	₱11,273
Subscriptions receivable		**(738)**	(960)
Additional paid-in capital		**4,111**	4,112
Excess of acquisition cost over carrying value of non-controlling interest acquired		**(328)**	(328)
Employee share-based payment plan	20	**743**	569
Unrealized fair value gains on available-for-sale investments	13	**96**	71
Share in cumulative translation adjustment of a subsidiary and an associate	10	**12**	684
Retained earnings:	5 and 19		
Appropriated		**6,000**	4,198
Unappropriated		**37,800**	37,750
Equity Attributable to Equity Holders of the Parent		**58,969**	57,369
Non-controlling Interests		**4,227**	3,777
Total Equity		**63,196**	61,146
Noncurrent Liabilities			
Interest-bearing long-term financial liabilities - net of current portion	11, 15, 21, 29 and 31	**15,498**	17,234
Customers' deposits - net of current portion	15, 22, 26, 29 and 31	**23,761**	25,063
Deposits from pre-selling of condominium units	17	**741**	343
Deferred tax liabilities - net	3 and 32	**3,322**	4,230
Long-term employee benefits	30	**9,547**	10,987
Provisions	23 and 33	**12,875**	7,492
Advances for construction - net of current portion	26 and 31	**3,271**	2,989
Other noncurrent liabilities	26 and 31	**2,352**	522
Total Noncurrent Liabilities		**71,367**	68,860
Current Liabilities			
Notes payable	25, 29 and 31	**149**	513
Trade payables and accrued expenses	2, 12, 21, 22, 26, 27 and 31	**31,138**	28,261
Income tax payable		**413**	133
Customers' refund	2, 24 and 31	**7,131**	9,147
Current portion of interest-bearing long-term financial liabilities	11, 15, 21, 29 and 31	**5,574**	4,069
Total Current Liabilities		**44,405**	42,123
Total Liabilities		**115,772**	110,983
		₱178,968	₱172,129

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Income

	Notes	2010	2009	2008
		Years Ended December 31		
		(Amounts in Millions, Except Per Share Data)		
REVENUES				
Sale of electricity	*2, 5, 12, 26, 27, 28 and 34*	**₱239,077**	₱178,686	₱186,999
Sale of real estate	*5*	**3,375**	2,877	2,213
Sale of contracts, services and others	*5 and 11*	**3,009**	2,987	2,563
		245,461	184,550	191,775
EXPENSES (INCOME)				
Purchased power	*27, 28 and 34*	**200,916**	150,928	156,872
Operations and maintenance	*15, 20, 27, 29 and 30*	**15,711**	13,611	13,351
Depreciation and amortization	*8, 11 and 13*	**6,219**	5,064	4,426
Provision for probable charges and expenses from claims	*23 and 33*	**5,750**	3,351	318
Cost of real estate sold	*5*	**2,640**	2,230	1,646
Interest and other financial income	*29 and 31*	**(2,690)**	(4,246)	(2,919)
Cost of services	*29*	**1,996**	1,803	1,456
Provision (reversal of provision) for probable losses from refund - net	*23 and 33*	**(1,632)**	(1,179)	6,617
Interest and other financial charges	*21, 22, 25 and 29*	**493**	3,328	4,135
Equity in net earnings of associates and a joint venture	*10*	**(283)**	(245)	(199)
Accretion of present value impact on customers' refund	*24*	**225**	555	846
Foreign exchange losses (gains) - net		**51**	(266)	(467)
Taxes, fees and permits		**974**	421	493
Others		**654**	216	–
		231,024	175,571	186,575
INCOME BEFORE INCOME TAX		**14,437**	8,979	5,200
PROVISION FOR (BENEFIT FROM) INCOME TAX	*32*			
Current		**5,233**	3,218	5,122
Deferred		**(913)**	(595)	(3,055)
		4,320	2,623	2,067
NET INCOME		**₱10,117**	₱6,356	₱3,133
Attributable To				
Equity holders of the parent	*35*	**₱9,685**	₱6,005	₱2,800
Non-controlling interests		**432**	351	333
		₱10,117	₱6,356	₱3,133
Earnings Per Share Attributable to the Equity Holders of the Parent	*35*			
Basic		**₱8.59**	₱5.42	₱2.54
Diluted		**8.59**	5.42	2.53

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income

	Notes	2010	2009	2008
		Years Ended December 31		
		(Amounts in Millions)		
NET INCOME FOR THE YEAR		**₱10,117**	₱6,356	₱3,133
OTHER COMPREHENSIVE INCOME				
Unrealized fair value gains (losses) on available-for-sale investments	*13*	**44**	27	(23)
Income tax effect		**(4)**	(3)	2
		40	24	(21)
Share in cumulative translation adjustment of a subsidiary and an associate	*10*	**(672)**	682	–
OTHER COMPREHENSIVE INCOME (LOSS) FOR THE YEAR, NET OF TAX		**(632)**	706	(21)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX		**₱9,485**	₱7,062	₱3,112
Attributable To				
Equity holders of the parent		**₱9,038**	₱6,711	₱2,779
Non-controlling interests		**447**	351	333
		₱9,485	₱7,062	₱3,112

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Changes in Equity

	Equity Attributable to Equity Holders of the Parent												
	Common Stock (Note 19)	Subscriptions Receivable	Additional Paid-in Capital	Excess of Acquisition Cost Over Carrying Value of Non-controlling Interest Acquired	Employee Share-based Payment Plan (Note 20)	Unrealized Fair Value Gains on Available-for-Sale Investments (Note 13)	Share in Revaluation Increment of an Associate (Note 10)	Share in Cumulative Translation Adjustment of a Subsidiary and an Associate (Note 10)	Appropriated Retained Earnings (Note 19)	Unappropriated Retained Earnings (Notes 5 and 19)	Equity Attributable to Equity Holders of the Parent	Non-controlling Interests	Total Equity
						(Amounts in Millions)							
At January 1, 2010	**₱11,273**	**(₱960)**	**₱4,112**	**(₱328)**	**₱569**	**₱71**	**₱–**	**₱684**	**₱4,198**	**₱37,750**	**₱57,369**	**₱3,777**	**₱61,146**
Net income	–	–	–	–	–	–	–	–	–	**9,685**	**9,685**	**432**	**10,117**
Other comprehensive income	–	–	–	–	–	**25**	–	**(672)**	–	–	**(647)**	**15**	**(632)**
Total comprehensive income	–	–	–	–	–	**25**	–	**(672)**	–	**9,685**	**9,038**	**447**	**9,485**
Appropriations - net of reversal	–	–	–	–	–	–	–	–	**1,802**	**(1,802)**	–	–	–
Collection of subscriptions receivable	–	**222**	**(1)**	–	–	–	–	–	–	–	**221**	–	**221**
Share-based payments	–	–	–	–	**174**	–	–	–	–	–	**174**	–	**174**
Dividends	–	–	–	–	–	–	–	–	–	**(7,833)**	**(7,833)**	**3**	**(7,830)**
	–	**222**	**(1)**	–	**174**	–	–	–	**1,802**	**(9,635)**	**(7,438)**	**3**	**(7,435)**
At December 31, 2010	**₱11,273**	**(₱738)**	**₱4,111**	**(₱328)**	**₱743**	**₱96**	**₱–**	**₱12**	**₱6,000**	**₱37,800**	**₱58,969**	**₱4,227**	**₱63,196**
At January 1, 2009	₱11,038	₱–	₱2,932	(₱328)	₱268	₱47	₱129	₱2	₱4,198	₱34,321	₱52,607	₱3,552	₱56,159
Net income	–	–	–	–	–	–	–	–	–	6,005	6,005	351	6,356
Other comprehensive income	–	–	–	–	–	24	–	682	–	–	706	–	706
Total comprehensive income	–	–	–	–	–	24	–	682	–	6,005	6,711	351	7,062
Share on depreciation of revaluation increment of an associate transferred to unappropriated retained earnings	–	–	–	–	–	–	(129)	–	–	129	–	–	–
Issuance of shares	235	(960)	1,481	–	–	–	–	–	–	–	756	–	756
Share-based payments	–	–	(301)	–	301	–	–	–	–	–	–	–	–
Dividends	–	–	–	–	–	–	–	–	–	(2,705)	(2,705)	(126)	(2,831)
	235	(960)	1,180	–	301	–	(129)	–	–	(2,576)	(1,949)	(126)	(2,075)
At December 31, 2009	₱11,273	(₱960)	₱4,112	(₱328)	₱569	₱71	₱–	₱684	₱4,198	₱37,750	₱57,369	₱3,777	₱61,146
At January 1, 2008	₱11,033	₱–	₱2,931	(₱328)	₱152	₱68	₱298	₱2	₱200	₱37,324	₱51,680	₱3,341	₱55,021
Net income	–	–	–	–	–	–	–	–	–	2,800	2,800	333	3,133
Other comprehensive income	–	–	–	–	–	(21)	–	–	–	–	(21)	–	(21)
Total comprehensive income	–	–	–	–	–	(21)	–	–	–	2,800	2,779	333	3,112
Share on depreciation of revaluation increment of an associate transferred to unappropriated retained earnings	–	–	–	–	–	–	(169)	–	–	169	–	–	–
Issuance of shares	5	–	1	–	–	–	–	–	–	–	6	–	6
Share-based payments	–	–	–	–	116	–	–	–	–	–	116	–	116
Appropriations - net of reversal	–	–	–	–	–	–	–	–	3,998	(3,998)	–	–	–
Dividends	–	–	–	–	–	–	–	–	–	(1,974)	(1,974)	(122)	(2,096)
	5	–	1	–	116	–	(169)	–	3,998	(5,803)	(1,852)	(122)	(1,974)
At December 31, 2008	₱11,038	₱–	₱2,932	(₱328)	₱268	₱47	₱129	₱2	₱4,198	₱34,321	₱52,607	₱3,552	₱56,159

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

	Notes	2010	2009	2008
		Years Ended December 31		
		(Amounts in Millions)		
CASH FLOWS FROM OPERATING ACTIVITIES				
Income before income tax		**₱14,437**	₱8,979	₱5,200
Adjustments for:				
Depreciation and amortization	*8, 11 and 13*	**6,219**	5,064	4,426
Provision for probable charges and expenses from claims	*23*	**5,750**	3,351	5,729
Interest and other financial income	*29*	**(2,690)**	(4,246)	(2,919)
Interest and other financial charges	*29*	**493**	3,328	4,135
Provision (reversal of provision) for probable losses from refund - net	*23*	**(1,632)**	(1,179)	6,617
Loss on disposal of utility plant and others - net		**1,033**	–	–
Provision for doubtful accounts, net of recoveries	*15 and 29*	**982**	886	1,563
Cost of guaranteed service levels payout		**388**	216	–
Loss from disposal of investment		**–**	46	–
Equity in net earnings of associates and a joint venture	*10*	**(283)**	(245)	(199)
Present value impact on customers' refund	*24*	**225**	555	846
Employee share-based payments	*20*	**174**	301	116
Reversal of write-down of inventory to net realizable value	*16*	**(3)**	(41)	(53)
Gain on disposal of investment property		**(4)**	–	–
Donation of investment property		**2**	–	–
Foreign exchange loss (gain)		**51**	(266)	(467)
Operating income before working capital changes		**25,142**	16,749	24,994
Decrease (increase) in:				
Trade and other receivables		**(10)**	15,601	(685)
Inventories		**(130)**	(168)	(57)
Land and development costs		**(517)**	(531)	421
Deferred pass-through fuel costs		**1,939**	631	1,104
Other current assets		**955**	(1,854)	(314)
Increase (decrease) in:				
Trade payables and accrued expenses		**41**	8,798	(13,952)
Customers' refund		**(2,241)**	(2,889)	(1,713)
Customers' deposits		**1,298**	2,913	4,468
Deposits from pre-selling of condominium units		**398**	307	2,375
Long-term employee benefits		**(1,424)**	(1,555)	653
Provisions		**(140)**	(4,935)	(69)
Net cash generated from operations		**25,311**	33,067	17,225
Income tax paid		**(4,953)**	(3,797)	(2,888)
Net cash flows generated from operating activities		**20,358**	29,270	14,337
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to:				
Construction in progress	*9*	**(5,769)**	(7,914)	(8,351)
Utility plant and others	*8*	**(2,741)**	(187)	(629)
Intangibles	*13*	**(300)**	(127)	(147)
Investment properties	*11*	**(110)**	(662)	(48)
Interest and other financial income received		**1,058**	1,332	2,472
Proceeds from:				
Return of investment		**752**	–	–
Disposal of utility plant and others		**82**	–	–
Disposal of investment property		**28**	–	–
Settlement of deliverable currency forwards		**5**	–	–
Dividends received from associates	*10*	**96**	445	456
Dividends paid by subsidiaries attributable to non-controlling interests		**(15)**	–	–
Decrease (increase) in:				
Other noncurrent assets		**622**	(1,657)	1,731
Other receivables		**–**	–	(603)
Net cash used in investing activities		**(6,292)**	(8,770)	(5,119)
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from:				
Interest-bearing long-term financial liabilities, net of issue costs		**10,528**	12,398	1,235
Notes payable		**380**	2,936	9,650
Collection of subscriptions receivable		**222**	445	5
Payments of:				
Interest-bearing long-term financial liabilities		**(10,748)**	(8,295)	(1,751)
Dividends		**(6,187)**	(2,820)	(1,960)
Interest and other financial charges		**(2,044)**	(1,524)	(2,689)
Notes payable		**(744)**	(12,251)	(10,570)
Stock transaction costs		**(1)**	–	–
Increase (decrease) in other noncurrent liabilities		**1,830**	277	(2,612)
Net cash flows used in financing activities		**(6,764)**	(8,834)	(8,692)
NET INCREASE IN CASH AND CASH EQUIVALENTS		**7,302**	11,666	526
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		**17,068**	5,402	4,876
CASH AND CASH EQUIVALENTS AT END OF YEAR	*14*	**₱24,370**	₱17,068	₱5,402

See accompanying Notes to Consolidated Financial Statements.

1. Corporate Information

Manila Electric Company or *MERALCO or Parent Company,* holds a congressional franchise under Republic Act or *RA* No. 9209 effective June 28, 2003. *RA* No. 9209 grants the *Parent Company* a 25-year franchise to construct, operate, and maintain an 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 the *Parent Company* a consolidated Certificate of Public Convenience and Necessity for the operation of electric service within its franchise coverage, effective until June 28, 2028, to coincide with the *Parent Company*'s congressional franchise.

MERALCO is the largest distribution utility or *DU,* in the Philippines. The power segment, primarily power distribution, consists of operations of the *Parent Company* and its subsidiary, Clark Electric Distribution Corporation or *CEDC*. In 2010, the *Parent Company* organized a segment for potential entry into power generation with the new subsidiary commencing development of proposed power generation plants. Through its other operating segments, it develops and sells real estate properties and provides engineering, construction and consulting services, bill payments, collection services, energy systems management and information systems and technology services. *MERALCO* and its subsidiaries are collectively referred to as the *Company* or *MERALCO* Group.

MERALCO is owned by three major shareholder groups. Beacon Electric Asset Holdings, Inc. or *Beacon Electric,* and PLDT Communications and Energy Ventures, Inc. or *PCEV*, formerly Pilipino Telephone Company, together own 40.92% of the common shares. *Beacon Electric* is jointly owned by Metro Pacific Investments Corporation or *Metro Pacific* and *PCEV,* which are both domestic corporations, and are affiliates of First Pacific Company Limited, a Hong Kong-based investment and management company. In 2009, San Miguel Corporation or SMC entered into a Share Purchase Agreement or *SPA* with Government Service Insurance Corporation or *GSIS* and Social Security System or *SSS* to acquire a pre-agreed number of shares. The nominees of SMC represent and vote on the shares covered by the *SPA*. As at December 31, 2010, the collective ownership of *GSIS* and *SSS* based on the Stock and Transfer Books of *MERALCO*, inclusive of the shares covered by the *SPA* represents 35.05% of the outstanding shares of *MERALCO*. First Philippine Holdings Corporation and First Philippine Utilities Corp. (formerly First Philippine Union Fenosa, Inc.), own 6.61% of *MERALCO.*

The common shares of the *Parent Company* are listed and traded on the Philippine Stock Exchange, or *PSE*.

As at December 31, 2010, the *Company* has 7,193 employees, 6,203 of which are employees of the *Parent Company.*

The registered office address of the *Parent Company* is Lopez Building, Ortigas Avenue, Pasig City, Philippines.

The accompanying consolidated financial statements as at December 31, 2010 and 2009, and for each of the three years ended December 31, 2010, 2009 and 2008 were reviewed and recommended for approval by the Audit and Risk Management Committee on February 21, 2011. The same consolidated financial statements were approved and authorized for issue by the Board of Directors or *BOD,* on February 28, 2011.

2. Rate Regulations

As *DU*s, *MERALCO* and *CEDC* are subject to the rate-making regulations and regulatory policies of the *ERC.* Billings to customers of the *Parent Company* 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) local franchise and (f) business taxes; 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 the *Parent Company’s* distribution, supply, and metering charges.

The rate-setting mechanism of *CEDC* is likewise in accordance with *ERC* regulations. After the unbundling of its rates based on *ERC* guidelines, *CEDC* became an entrant to the Performance-Based Regulation, or *PBR* under Group D. *CEDC* is currently undergoing regulatory reset.

The following is a discussion of matters related to rate-setting of the *Parent Company*:

Rate Applications

PBR

The *Parent Company* was among the first entrants to the *PBR*, together with Dagupan Electric Corporation and Cagayan Electric and Power Company.

Rate-setting under *PBR* is governed by the *RDWR*. Unlike the Return on Rate Base methodology, which was in place up to June 2007, where utility tariffs were determined based on historical costs plus a reasonable rate of return, the *PBR* scheme sets tariffs based on the *DU*'*s* asset base, and the required operating and capital expenditures once every regulatory period or *RP* to meet a level of operational performance determined or 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 setting are done on an *RP* basis where one *RP* consists of four regulatory years. A regulatory year or *RY*, begins on July 1 and ends on June 30 of the following year. As at December 31, 2010, the *Parent Company* is operating in the first half of the fourth *RY* of the second *RP.* The second *RP* is from July 1, 2007 to June 30, 2011.

Maximum Average Price or MAP for RY 2008 and RY 2009

On January 11 and April 1, 2008, the *Parent Company* filed separate applications for the approval of its proposed translation of the *MAP* for *RY* 2008 and *RY* 2009 into different rate schedules for the *Parent Company*'s 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* of ₱1.3607 per kWh for the *RY* 2009.

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

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 the *Parent Company*'s rate translation application for *RY* 2009 which the *ERC* set at ₱1.2227 per kWh. In a decision dated January 27, 2010, the *CA* denied the Petition. Consequently, the consumer groups brought the case to the Supreme Court or *SC*. The *Parent Company* already filed its Comment on the Petition before the *SC* while the Petitioners filed their Reply thereto. As at February 28, 2011, the *Parent Company* is awaiting further action of the *SC* on the petition.

As part of the *PBR*, the *Parent Company* implemented payouts to customers where the *Parent Company's* performance was beyond the guaranteed service levels or *GSL* established by the *ERC*. See *Note 26 – Trade Payables and Accrued Expenses.*

MAP for RY 2010

On August 7, 2009, the *Parent Company* filed a petition for the verification of the *MAP* for *RY* 2010 and its translation into tariffs by customer category. In accordance with the *ERC*'s Guidelines for *RY* 2010 Rate Reset for First Entrant Distribution Utilities, the constrained *MAP* for *RY* 2010 was computed to be ₱1.4917 per kWh.

On December 14, 2009, the *ERC* approved the *Parent Company*'s application for approval of: a) *MAP* for *RY* 2010; and b) translation of *MAP* for *RY* 2010 into a distribution rate structure for its various customer classes. A Motion for Reconsideration and Clarification was filed by a consumer against the said *ERC* decision. On January 26, 2010, the *Parent Company* filed a manifestation with the *ERC* voluntarily suspending the implementation of the *ERC*'s December 14, 2009 Decision, until such time the regulator resolves and addresses all other issues raised by the intervenors. On March 10, 2010, the *ERC* resolved the Motion for Reconsideration and approved a new rate schedule that ensures there will be no rate distortion or no cross-subsidies, other than the lifeline subsidy, in the *Parent Company's* rates. Consequently, the *Parent Company* implemented the new rate schedule effective its April 2010 billing cycle.

Certain electricity consumer groups likewise filed a Petition for Certiorari with the *SC* questioning the Decision rendered by the *ERC*. The *Parent Company* has filed its comment thereto and has likewise commented on the new issues raised by petitioners in their reply. The *Parent Company* is now awaiting further action by the *SC* on the Petition.

MAP for RY 2011

On December 6, 2010, the *ERC* approved the *Parent Company's* application for constrained *MAP* for *RY* 2011 of ₱1.6464 per kWh, limited by the side constraints and S Factor of ₱0.008 per kWh; and ordered the *Parent Company* to implement, starting the next billing cycle from receipt thereof, its approved distribution, supply and metering charges. The 2011 *MAP* rates were implemented starting the January 2011 billing cycle.

Third RP Reset Application

On June 18, 2010, *the Parent Company* filed its application for the approval of its proposed Annual Revenue Requirement or *ARR* and Performance Incentive Scheme or *PIS,* for the third *RP* (July 1, 2011–June 30, 2015). The case is docketed as *ERC* Case No. 2010-069-RC.

The hearings for the case have been completed and *ERC* has released its Draft Determination, which contains its initial position on the *Parent Company's* application. On February 7, 2011, the *ERC* conducted a public consultation on the *Parent Company's* Draft Determination. Comments submitted by the intervenors shall be reviewed by the *ERC* in connection with its Final Determination.

Upon approval, *the Parent Company*'s *ARR* will then be translated into a distribution rate structure to be implemented across the various customer classes of the *Parent Company* for the third *RP*. The *PIS*, on the other hand will provide the performance measures and targets that will apply to the *Parent Company* throughout the third *RP.*

SC Decision on Unbundling Rate Case

On May 30, 2003, the *ERC* issued an Order approving the *Parent Company*'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 the *Parent Company*'s 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 the *Parent Company*. The *ERC* and the *Parent Company* 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 the *Parent Company* elevated the case to the *SC* of the Philippines.

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 the *ERC* to request the *COA* to undertake a complete audit of the books, records and accounts of the *Parent Company*. On January 15, 2007, in compliance with the directive of the *SC*, the *ERC* requested the *COA* to conduct an audit of the books, records and accounts of the *Parent Company*.

The status of the *COA* audit is discussed in *Note 33 – Contingencies*.

Applications for Recoveries

The *Parent Company* filed with the *ERC* its applications for recoveries of advances for pass-through costs. These advances consist mainly of unrecovered or differential generation and transmission charges technically referred to as under-recoveries, which are recoverable from the customers, as allowed by law.

Applications for the Recovery of Generation Costs and System Loss Charges

The *Parent Company* filed separate applications (*ERC* Case Nos. 2006-52RC, 2006-062RC, 2006-076RC, 2007-001RC, 2007-038RC, 2007-078RC, 2007-101RC, 2007-120RC, 2007-123RC and 2007-135RC) 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 system loss, or *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, 2010 the remaining balance of ₱2,607 million of such unrecovered generation costs will be billed in 2011 at the rate of ₱0.0314 per *kWh* until completed and is shown as part of "Trade and other receivables - Unbilled" account. See *Note 15 – Trade and Other Receivables*.

With respect to the ₱1,295 million *SL* charge under-recoveries, the *ERC* ordered the *Parent Company* 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. As at February 28, 2011, the *Parent Company* has yet to file the application for recovery of the ₱1,295 million *SL* charge under-recoveries with the *ERC*.

Application for Recovery of Transmission Costs

Consistent with the rules on Transmission Rate Adjustment Mechanism, the *Parent Company* filed an application to recover transmission costs advances, net of transmission over-recoveries. The final Order from *ERC* dated December 14, 2009 updated the net amount recoverable of the *Parent Company* to ₱1,480 million, inclusive of carrying charges. As at December 31, 2010, the balance of ₱88 million, which will be billed in 2011 is included in "Trade and other receivables" account in the consolidated statement of financial position.

Applications for Recovery of Advances for Other Pass-Through Costs

Inter-Class Cross Subsidy and Lifeline Subsidy

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

In December 2009, the *Parent Company* implemented the decisions of *ERC* on the inter-class cross and lifeline subsidies. As at December 31, 2010, the total amount of billed inter-class cross subsidy and lifeline subsidy amounted to ₱334 million and ₱220 million, respectively. The unbilled balance of inter-class cross subsidy is ₱715 million and is expected to be recovered within the next 28 months. The balance of lifeline subsidy is ₱636 million and will be billed within the 38 months. The amount recoverable within twelve months is included in the "Trade and other receivables" while the long-term portion is included in the "Other noncurrent assets" account.

Rules Governing the Automatic Cost Adjustment and True-up Mechanisms and Corresponding Confirmation Process for Distribution Utilities

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 in the following bill components: generation charge, transmission charge, system loss charge, lifeline rate subsidies, local franchise and business taxes.

The rules synchronize the various confirmation and verification processes by the *ERC* for the foregoing charges. In its Decision, the *ERC* required *DU*s in Luzon to which the *Parent Company* belongs, to file their consolidated applications to resolve under- or over-recoveries accumulated from the start of their rate unbundling until December 2008, not later than October 30, 2009. Subsequent filings will be every three years thereafter. However, under *ERC* Resolution No. 23 Series of 2009, dated October 12, 2009, such application was deferred. 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 *DU*s in Luzon to file their respective applications. Subsequent filings shall likewise be every three years thereafter.

See *Note 13 – Other Noncurrent Assets*.

Petition to Implement a Lower Generation Charge for the February 2010 Supply Month

The *Parent Company's* generation cost abruptly increased to ₱15.9 billion for the supply month of February 2010. This translates to a generation charge of ₱6.76 per kWh to its customers for the March 2010 billing. The sharp increase in generation cost was mainly due to the high prices in the Wholesale Electricity Spot Market or *WESM*, brought about by the tight supply of electricity, as several plants were either out on preventive or emergency maintenance, or with de-rated capacity because of the "El Nino" phenomenon and unusually higher temperature. A Petition was filed by the *Parent Company* to mitigate the effects of the abrupt increase in generation cost through a voluntary deferral of a portion of generation costs, with the differential to be recovered over a period, which shall be approved by the *ERC*. In an Order dated March 10, 2010, the *ERC* provisionally approved a lower generation charge of ₱5.8417 per kWh representing ₱13.8 billion generation cost for the subject period. The *Parent Company* was also provisionally allowed to charge over a six month period starting April 2010 the generation charge at the rate of ₱0.07 per kWh, corresponding to the incremental costs of the condensate fuel used by the *First Gas* plants during the said period. The balance of the generation costs, which the *Parent Company* is seeking to recover in the same petition, is now undergoing evaluation by the *ERC*. All hearings have been completed with the case pending decision by the *ERC.*

Others

SC Decision on the ₱0.167 per kWh Refund

Following the *SC*'s final ruling that directed the *Parent Company* to refund affected customers ₱0.167 per kWh covering the billing period from February 1994 to April 30, 2003, the *ERC* approved the release of the refund in four phases. The refund is still ongoing. See *Note 24 – 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 the *Parent Company*'s utility plant and others, and investment properties, which are carried at deemed cost and for derivative financial instruments and available-for-sale, or *AFS* financial assets. *AFS* financial assets are measured at fair value. Derivative financial instruments are shown as part of "Other current assets," "Other noncurrent assets," "Trade payables and accrued expenses" and "Other noncurrent liabilities" accounts 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 accompanying consolidated financial statements are presented in Philippine peso, the *Company*'s functional and presentation currency, and all values are rounded to the nearest million peso (₱000,000), except when otherwise indicated.

Statement of Compliance

The consolidated financial statements of the *Parent Company* and subsidiaries have been prepared in compliance with 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 *PFRSC*.

Basis of Consolidation

The consolidated financial statements comprise the financial statements of *MERALCO* and its subsidiaries as at December 31 of each year, except for *MIESCOR* and its subsidiaries, whose financial reporting date ends at September 30. Adjustments and disclosures are made for the effects of significant transactions or events that occurred between the date of *MIESCOR* and its subsidiaries' financial statements and the date of the consolidated financial statements.

The consolidated financial statements include the financial statements of the *Parent Company* and the following directly and indirectly-owned subsidiaries as at December 31, 2010 and 2009:

Subsidiaries	Place of Incorporation	Principal Business Activity	Percentage of Ownership Direct	Indirect
Corporate Information Solutions, Inc. or *CIS*	Philippines	e-Transactions	100	–
CIS Bayad Center, Inc.	Philippines	Bills payment collection	–	100
Outsourced Telleserve Corporation or OTC	Philippines	Tellering services	–	100
Meralco Energy, Inc. or *MEI*	Philippines	Energy systems management	100	–
eMERALCO Ventures, Inc. or *e-MVI*	Philippines	e-Business development	100	–
Meralco PowerGen Corporation or *MPG* (formerly Asian Center for Energy Management or *ACEM*)	Philippines	Building and operation of plants and related facilities	100	–
Meralco Financial Services Corporation or *Finserve*	Philippines	Financial services provider	100	–
Republic Surety and Insurance Company, Inc. or *RSIC*	Philippines	Insurance	100	–
Lighthouse Overseas Insurance Limited or *LOIL*	Bermuda	Insurance	100	–
MIESCOR	Philippines	Engineering, construction and consulting services	99	–
MIESCOR Builders Inc. or MBI	Philippines	Electric transmission and distribution operation and maintenance	–	100
Landbees Corporation or Landbees	Philippines	General services, manpower/maintenance	–	100
Miescorrail, Inc. or Miescorrail	Philippines	Engineering and construction of mass transit system	–	60
CEDC	Philippines	Power distribution	65	–
Rockwell Land Corporation or *Rockwell Land*	Philippines	Real estate	51	–

MPG was originally incorporated as *ACEM*. On August 19, 2010, the *BOD* and the stockholders of *ACEM* (now *MPG*) approved a resolution to reactivate *ACEM* which was previously resolved to cease operations in September 2005. On November 12, 2010, the *SEC* approved the following resolutions of *ACEM*: (i) resumption of operations; (ii) change in corporate name to "Meralco PowerGen Corporation"; (iii) change in principal place of business; and (iv) change in primary and secondary purposes of the business.

Subsidiaries are fully consolidated from the date of acquisition, being the date at which the *MERALCO Group* obtains control, and continue to be consolidated until the date that such control ceases.

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, Rockwell Land*, and *MIESCOR* and its subsidiaries not held by the *Parent Company* 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.

Losses within a subsidiary are attributed to the non-controlling interest even if that 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 control over a subsidiary is lost, the *Company*: (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 differences recorded 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 the *Parent Company's* share of components previously recognized in the consolidated statement of comprehensive income to the consolidated statement of income.

4. Changes in Accounting Policies and Disclosures

The accounting policies adopted are consistent with those of the previous financial year except with respect to the adoption of the following amendments and improvements to existing *PFRS* and a new interpretation as at January 1, 2010:

Amendments to PFRS

Amendment to PFRS 2, Share-based Payment

The amendments clarify how an individual subsidiary in a group should account for share-based payment arrangements in its own financial statements. It further states that an entity that receives goods or services in a share-based payment arrangement must account for these goods or services no matter which entity in the group settles the transaction, and regardless of whether the transaction is equity-settled or cash-settled.

Improvements to PFRS 5, Noncurrent Assets Held-for-Sale and Discontinued Operations

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

Amendment to PAS 39, Financial Instruments: Recognition and Measurement – Eligible Hedged Items

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

New Interpretation

Philippine Interpretation International Financial Reporting Interpretations Committee (IFRIC) 17, Distributions of Non-Cash Assets to Owners

This interpretation provides guidance on non-reciprocal distribution of assets by an entity to its owners acting in their capacity as owners, including distributions of non-cash assets and those giving the shareholders a choice of receiving non-cash assets or cash, provided that: (a) all owners of the same class of equity instruments are treated equally; and (b) the non-cash assets distributed are not ultimately controlled by the same party or parties both before and after the distribution, and as such, excluding transactions under common control.

Improvements to PFRS

The *PFRSC* approved in May 2009 the adoption of the Improvements to International Financial Reporting Standards or *IFRS*, issued in April 2009 by the International Accounting Standards Board or *IASB*. There are separate transitional provisions for the improvements in each standard, which are all effective beginning January 1, 2010.

PFRS 2, Share-based Payment

The amendment clarifies that the contribution of a business on formation of a joint venture and combinations under common control are not within the scope of *PFRS 2* regardless of its exclusion from the Revised *PFRS 3*.

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

The amendment clarifies the disclosures required in respect of noncurrent assets or disposal groups classified as held for sale or discontinued operations. The disclosure requirements of other *PFRS* only apply if specifically required for such noncurrent assets or discontinued operations.

It also clarifies that the general requirements of *PAS 1, Presentation of Financial Statements,* still apply, particularly paragraphs 15 (to achieve fair presentation) and 125 (sources of estimation and uncertainty) of *PAS 1*.

PFRS 8, Operating Segments

The amendment clarifies that segment assets and liabilities need only be reported when those assets and liabilities are included in measures that are used by the chief operating decision maker.

PAS 1, Presentation of Financial Statements

The terms of a liability that could result, at anytime, in its settlement by the issuance of equity instruments at the option of the counterparty do not affect its classification.

PAS 7, Statement of Cash Flows

The amendment explicitly states that only expenditure that results in a recognized asset can be classified as a cash flow from investing activities.

PAS 17, Leases

The amendment removes the specific guidance on classifying land as lease so that only the general guidance remains.

PAS 36, Impairment of Assets

The amendment clarifies that the largest unit permitted for allocating goodwill acquired in a business combination is the operating segment, as defined in *PFRS 8*, before aggregation for reporting purposes.

PAS 38, Intangible Assets

The amendment clarifies that if an intangible asset acquired in a business combination is identifiable only with another intangible asset, the acquirer may recognize the group of intangible assets as a single asset, provided the individual assets have similar useful lives. It also clarifies that the valuation techniques presented for determining the fair value of intangible assets acquired in a business combination that are not traded in active markets are only examples and are not restrictive on the methods that can be used.

PAS 39, Financial Instruments: Recognition and Measurement

The amendment clarifies that a prepayment option is considered closely related to the host contract when the exercise price of a prepayment option reimburses the lender up to the approximate present value of lost interest for the remaining term of the host contract. The amendment also clarifies that the scope exemption for contracts between an acquirer and a vendor in a business combination to buy or sell an acquiree at a future date, applies only to binding forward contracts, and not derivative contracts where further actions by either party are still to be taken. It also clarifies that gains or losses on cash flow hedges of a forecast transaction that subsequently results in the recognition of a financial instrument or on cash flow hedges of recognized financial instruments should be reclassified in the period that the hedged forecast cash flows affect profit or loss.

Philippine Interpretation IFRIC 9, Reassessment of Embedded Derivatives

The improvement clarifies that it does not apply to possible reassessment, at the date of acquisition, to embedded derivatives in contracts acquired in a combination between entities or businesses under common control or the formation of a joint venture.

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

The improvement states that in a hedge of a net investment in a foreign operation, qualifying hedging instruments may be held by any entity or entities within the group, including the foreign operation itself, as long as the designation, documentation and effectiveness requirements of *PAS 39* that relate to a net investment hedge, are satisfied.

The adoption of the foregoing amendments and improvements to existing *PFRS* and new interpretation did not have any effect on the *Company's* financial position and performance.

New Accounting Standards and Interpretations to Existing Standards Effective Subsequent to December 31, 2010

The *Company* will adopt the following revised standards and interpretations enumerated below when these become effective. Except as otherwise indicated, the *Company* does not expect the adoption of these revised standards and amendments to *PFRS* to have a significant impact on the *Company's* consolidated financial statements.

Effective 2011

Revised PAS 24, Related Party Disclosures

The standard has been revised to simplify the identification of related party relationships and re-balance the extent of disclosures of transactions between related parties based on the costs to preparers and the benefits to users in having this information available in the financial statements. Also, the revised standard provides a partial exemption from the disclosure requirements for government-related entities. This revision is applicable retrospectively and for annual periods beginning on or after January 1, 2011.

Amendment to PAS 32, Financial Instruments: Presentation - Classification of Rights Issues

The definition of a financial liability in the standard has been amended to classify rights issues (and certain options or warrants) as equity instruments if: (a) the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, and (b) the instruments are used to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. This amendment is applicable retrospectively and for annual periods beginning on or after February 1, 2010.

Amendment to IFRIC 14, Prepayments of a Minimum Funding Requirement

The interpretation has been amended to permit an entity to treat the prepayment of a minimum funding requirement as an asset. The amendment should be applied to the beginning of the earliest period presented in the first financial statements in which the entity applied the original interpretation. This amendment is applicable retrospectively and for annual periods beginning on or after January 1, 2011.

Philippine Interpretation IFRIC 19, Extinguishing Financial Liabilities with Equity Instrument

The interpretation clarifies that equity instruments issued to a creditor to extinguish a financial liability are consideration paid. As a result, the financial liability is derecognized and the equity instruments issued are treated as consideration paid to extinguish that financial liability. The interpretation states that equity instruments issued in a debt for equity swap should be measured at the fair value of the equity instruments issued, if this can be determined reliably. If the fair value of the equity instruments issued is not reliably determinable, the equity instruments should be measured by reference to the fair value of the financial liability extinguished as of the date of extinguishment. Any difference between the carrying amount of the financial liability that is extinguished and the fair value of the equity instruments issued is recognized immediately in profit or loss. This interpretation is applicable retrospectively and for annual periods beginning on or after July 1, 2010.

Improvements to PFRS

The *PFRSC* approved in its meeting in July 2010 the adoption of Improvements to *IFRS* issued by the *IASB* in May 2010. There are separate transitional provisions for the improvements in each standard, which are all effective beginning January 1, 2011.

PFRS 3, Business Combinations

The improvements include: (a) clarification that the amendments to *PFRS 7, Financial Instruments: Disclosures, PAS 32, Financial Instruments: Presentation,* and *PAS 39,Financial Instruments: Recognition and Measurement,* that eliminate the exemption for contingent consideration, do not apply to contingent consideration that arose from business combinations whose acquisition dates precede the application of *PFRS 3* (as revised in 2008); (b) guidance that the choice of measuring non-controlling interest at fair value or at the proportionate share of the acquiree's net assets applies only to instruments that represent present ownership interests and entitle their holders to a proportionate share of the net assets in the event of liquidation. All other components of non-controlling interest are measured at fair value unless another measurement basis is required by *PFRS*; and (c) clarification that the application guidance in *PFRS 3* applies to all share-based payment transactions that are part of a business combination, including un-replaced and voluntarily replaced share-based payment awards.

PFRS 7, Financial Instruments

The amendment emphasizes the interaction between quantitative and qualitative disclosures about the nature and extent of risks associated with financial instruments.

PAS 1, Presentation of Financial Instruments

The amendment clarifies that an entity shall present an analysis of other comprehensive income for each component of equity, either in the statement of changes in equity or in the notes to the financial statements.

PAS 27, Consolidated and Separate Financial Statements

The improvement clarifies that the consequential amendments from *PAS 27* made to *PAS 21, The Effect of Changes in Foreign Exchange Rates, PAS 28, Investments in Associates,* and *PAS 31, Interests in Joint Ventures,* apply prospectively for annual periods beginning on or after July 1, 2009, or earlier when *PAS 27* is applied earlier.

PAS 34, Interim Financial Reporting

The amendment provides guidance how to apply disclosure principles in *PAS 34* and additional disclosure requirements around (a) the circumstances likely to affect fair values of financial instruments and their classification; (b) transfers of financial instruments between different levels of the fair value hierarchy; (c) changes in classification of financial assets; and (d) changes in contingent liabilities and assets.

Philippine Interpretation IFRIC 13, Customer Loyalty Programmes

The amendment clarifies the meaning of fair value in the context of measuring award credits under customer loyalty programmes.

The improvements to *PFRS* 3 will be applied prospectively while those for *PFRS* 7, *PAS* 1, *PAS* 27 and *PAS* 34 will be applied retrospectively. *IFRIC* 13 is not applicable to the *Company.*

Effective 2012

Philippine Interpretation IFRIC 15, Agreements for Construction of Real Estate

This interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. This interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as a construction contract to be accounted for under *PAS 11*, *Construction Contracts*, or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and reward of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The *Company* will apply this interpretation in 2012. Adoption of this interpretation will result in a change in the *Company*'s revenue recognition on sale of condominium units and will result in decrease in retained earnings and non-controlling interests and increase in assets and liabilities.

Effective 2013

PFRS 9, Financial Instruments: Classification and Measurement (Phase I)

Phase I introduces new requirements for classifying and measuring financial assets. Other phases are currently being deliberated to expand *PFRS* 9 to include classifications and measurement of financial liabilities, derecognition of financial instruments, impairment, and hedge accounting. The objective is to replace *PAS 39* in its entirety in the middle of 2011.

PFRS 9 (Phase I) is applicable to all financial assets within the scope of *PAS 39*. At initial recognition, all financial assets (including hybrid contracts with a financial asset host) are measured at fair value plus, in the case of a financial asset not classified as at fair value through profit or loss or *FVPL*, transaction costs.

Subsequent to initial recognition, financial assets that are debt instruments are measured at amortized cost or fair value on the basis of both: (a) the entity's business model for managing the financial assets; and (b) the contractual cash flow characteristic of the financial asset. Debt instrument may be subsequently measured at amortized cost if: (a) the asset is held within a business model whose objective is to hold the assets to collect the contractual cash flows; and (b) the contractual terms of the financial asset 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.

All financial assets that are equity investments are measured at fair value either through other comprehensive income or profit or loss. This is an irrevocable choice on the part of the entity unless the equity investments are held for trading, in which case, they must be measured at *FVPL*.

This standard is applicable retrospectively and for annual periods beginning on or after January 1, 2013 with certain exceptions. Earlier application is permitted.

5. **Summary of Significant Accounting Policies**

The principal accounting policies adopted in preparing the consolidated financial statements of the *Company* are as follows:

Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value. Acquisition-related costs in a business combination are expensed.

As at the acquisition date, the *Company* recognizes, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. Identifiable assets acquired and liabilities assumed are measured at acquisition-date fair values. For each business combination, the *Company* has the option to measure the non-controlling interest in the acquiree at fair value or the non-controlling interest's proportionate share of the acquiree's identifiable net assets.

When a business is acquired, an assessment 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 to fair value as at acquisition date.

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 *Company's* 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.

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.

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 of and the portion of the cash-generating unit retained.

Business combinations involving entities under common control are accounted for similar to 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 year, 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.

Prior to January 1, 2010, business combinations were accounted for using the purchase method. Transaction costs directly attributable to the acquisition formed part of the acquisition cost. Non-controlling interests were measured at the proportionate share of the acquiree's identifiable net assets.

Utility Plant and Others

Utility plant and others, except land, are stated at cost, net of accumulated depreciation and amortization and any accumulated impairment loss. Costs include the cost of replacing part of such utility plant and other properties when that 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.

The *Parent Company'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 19 – Equity* for the related discussion.

Depreciation and amortization of utility plant and others of the *Company* is 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
Others:	
Buildings and improvements	15–40 years
Communication equipment	10 years
Office furniture, fixtures and other equipment	5 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 year 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 financial year-end 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 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 or sale.

Borrowing costs includes 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 is carried at cost less any impairment in value.

The *Parent Company*'s investment properties are stated at deemed cost. See *Note 19 – 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 the investment properties are permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss on the derecognition of the investment properties are recognized in the consolidated 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, the *Company* 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 *Company*'s lease contracts, the *Company* 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 *Company* 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 5 years using the straight-line method of accounting 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 least 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 to determine whether such indefinite useful life continues to exist. If not, 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 in profit or loss in the year in which these are incurred.

Investments in Associates

An associate is an entity over which the *Company* has significant influence and which is neither a subsidiary nor a joint venture. Investments in associates are accounted for using the equity method of accounting and are initially recognized at cost.

Under the equity method, an investment in an associate is carried in the consolidated statement of financial position at cost plus post-acquisition changes in the *Company*'s share of net assets of the associate, less any impairment in value. Any goodwill relating to an associate is included in the carrying amount of the investment and is not amortized nor individually tested for impairment. The consolidated statement of income reflects the *Company*'s share of the results of operations of the associates. Where there has been a change recognized directly in the equity of the associate, the *Company* recognizes its share in any changes and discloses this, when applicable, in the consolidated statements of comprehensive income and changes in equity. Unrealized gains and losses resulting from transactions between and among the *Company* and the associates are eliminated to the extent of the interest in those associates.

The share in profits and losses of associates is shown on the face of the consolidated statement of income. This is the profit or loss attributable to equity holders of the associate and is therefore profit or loss after tax and net of non-controlling interest in the subsidiaries of the associates.

The reporting dates of the associates and the *Company* are identical and the associates' accounting policies conform with those used by the *Company* for like transactions and events in similar circumstances.

After application of the equity method, the *Company* determines whether it is necessary to recognize an impairment loss on the investments in associates. At the end of each reporting date, the *Company* determines whether there is any objective evidence that each of the investments in associates is impaired. If this is the case, the *Company* calculates the amount of impairment as the difference between the recoverable amount of the investment in associate and its carrying value and recognize the amount in the consolidated statement of income.

Upon loss of significant influence over the associate, the *Company* measures and recognizes any remaining investment at its fair value. Any difference between the carrying amount of the investment in associate upon loss of significant influence, and the aggregate of the fair value of the remaining investment and proceeds from disposal, is recognized in the consolidated statement of income.

Interest in a Joint Venture

The *Company*'s interest in Indra Philippines, Inc. or *Indra Philippines,* a jointly controlled entity, is accounted for using the equity method of accounting in the consolidated financial statements. The interest in a joint venture is carried at cost plus post-acquisition changes in the *Company*'s share of the net assets of the joint venture, less any impairment in value. The *Company*'s share of the results of operations of the joint venture is recognized in the consolidated statement of income.

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. A jointly controlled entity is a joint venture that involves the establishment of a separate entity in which each venturer has an interest. The financial statements of the joint venture are prepared for the same reporting year as the *Company*, using consistent accounting policies.

Adjustments are made in the consolidated financial statements to eliminate the *Company's* share of unrealized gains and losses on transactions between the *Company* and the jointly controlled entity. The joint venture is carried at equity method until the date on which the *Company* ceases to have joint control over the jointly controlled entity.

Upon loss of control and provided the jointly controlled entity does not become a subsidiary or associate, the *Company* measures and recognizes the remaining investment at fair value. Any difference between the carrying amount of the jointly controlled entity upon loss of joint control, and the aggregate of the fair value of the remaining investment and proceeds from disposal, is recognized in the consolidated statement of income. When the remaining investment constitutes significant influence, it is accounted for as investment in an associate.

Deferred Pass-through Fuel Costs

Deferred pass-through fuel costs are accounted as prepayments for gas purchases and are initially recorded based on the billings received. The account is reduced for fuel consumption above the required annual volume based on historical costs and is tested for impairment at each reporting date. Key factors in the impairment test of the deferred pass-through costs are the ability of the First Gas Power Corporation or *FGPC* and FGP Corp. or *FGP*'s power plants to burn the banked gas within the contractually-agreed period and the *Parent Company's* ability to bill its customers for the power generated from the banked gas burnt on the basis of the amounts paid for such gas.

Impairment of Nonfinancial Assets

The *Company* assesses at each reporting date whether there is an indication that a nonfinancial asset, other than goodwill and intangible assets with indefinite useful life, may be impaired. If any such indication exists the *Company* makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an individual asset's or, if the individual asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, 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 multipliers, 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 *Company* 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 is 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 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 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.

Inventories

Materials and supplies 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.

Condominium units for sale are stated at the lower of cost or net realizable value. Cost includes the cost of the land, expenditures for the construction of the condominium units and borrowing costs incurred during construction. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

Land and Development Costs

Real estate properties for development, subdivided or otherwise, are stated at the lower of cost or net realizable value. Expenditures for development are capitalized as part of the cost of the land. Borrowing costs are capitalized while development is in progress. Net realizable value is the estimated selling price in the ordinary course of business less estimated costs to complete and to sell.

Financial Assets

Initial Recognition

Financial assets are classified as at *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 that the *Company* commits to purchase or sell the asset.

The *Company*'s financial assets include cash and cash equivalents, trade and other receivables (including *SC GRAM* refund), 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 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 recognized in the consolidated statement of income under "Interest and other financial income" account.

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.

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 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.

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 in the current assets except for assets with maturities beyond 12 months from the reporting date, which are classified as noncurrent assets.

HTM Investments

Nonderivative financial assets with fixed or determinable payments and fixed maturities are classified as *HTM* when the *Company* has the positive intention and ability to hold 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. The *Company* has no *HTM* investments as at December 31, 2010 and 2009.

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 *Company*'s financial liabilities include notes payable, interest-bearing long-term financial liabilities, trade payables and accrued expenses (excluding output *VAT*, accrued taxes and leases), customers' deposits, customers' refund, other noncurrent liabilities and derivatives that are not accounted for as effective accounting hedges.

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 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 *Company* does not have financial liabilities designated as at *FVPL* as at December 31, 2010 and 2009.

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 either under "Interest and other financial charges" or "Interest and other financial income" account in the consolidated statement of income.

Derivative Financial Instruments

Initial Recognition and Subsequent Measurement

The *Parent Company* has separated embedded foreign currency forwards and currency options while *Rockwell Land* has foreign currency contracts, 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.

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.

The fair values of freestanding currency forward transactions of *Rockwell Land* are calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

See *Note 31 – Financial Assets and Liabilities.*

Offsetting of Financial Instruments

Financial assets and 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.

Fair Value of Financial Instruments

The fair value of financial instruments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business at the transaction or reporting date. When current bid and asking prices are not available, the price of the most recent transaction provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction.

For financial instruments where there is no active market, fair value is determined using valuation techniques. Such techniques include use of recent arm's-length market transactions, reference to the current market value of another instrument which is substantially the same, discounted cash flow analysis and other pricing models.

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 *Company* 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 *Company* determines the appropriate method of recognizing the 'Day 1' profit or loss amount.

Impairment of Financial Assets

The *Company* 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 *Company* 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. The *Parent Company* 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 *Rockwell Land*, consideration is given to breach of contract, such as default or delinquency in interest or principal payments 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 are 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 *Company*.

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 investments 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 an investment in an equity instrument 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 *Company* 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 *Company* (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 *Company* 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 *Company*’s continuing involvement in the asset.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that the *Company* could be required to repay.

Financial Liabilities

A financial liability is derecognized when the obligation under the liability is discharged 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

The *Company*'s peso-denominated redeemable preferred stock exhibits 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.

Provisions

Provisions are recognized when the *Company* 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 *Company* 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. Where discounting is used, the increase in the provision due to the passage of time is recognized as part of "Interest and other financial charges" account.

Pension and Other Post-Employment Benefits

MERALCO and substantially all of its subsidiaries have distinct, funded, noncontributory defined benefit retirement plans covering all permanent employees. *MERALCO* has a pension plan covering employees hired up to 2003, which provides for post-retirement benefits. For employees hired in 2004 and onwards, *MERALCO* maintains a Provident Plan. Also, *MIESCOR* has a defined contribution retirement plan in addition to its noncontributory defined benefit plan.

The costs of providing benefits under the distinct defined benefit plans are determined using the projected unit credit actuarial valuation method. This method reflects services rendered by employees to the date of valuation and incorporates assumptions concerning employees' projected salaries. Retirement costs include current service cost, interest costs, return on plan assets plus amortizations of past service cost, experience adjustments and changes in actuarial assumptions. Past service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested. If the benefits vest immediately following the introduction of, or changes to a pension plan, past service cost is recognized immediately. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting year exceeded 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plan.

The defined benefit liability (or asset) is the aggregate of the present value of the defined benefit obligation and any actuarial gains not yet recognized reduced by past service cost and actuarial losses not yet recognized and the fair value of plan assets out of which the obligations are to be settled directly. Plan assets are assets that are held by a long-term employee benefit fund. Fair value is based on market price information, and the published bid price in the case of quoted securities. The amount of any defined benefit asset recognized is restricted to the sum of any past service cost and actuarial gains or losses not yet recognized and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

MIESCOR records expenses based on its contribution to the defined contribution plan as the employee renders service to *MIESCOR*.

Share-based Payment Transactions

MERALCO has an employee share-based payment plan covering its employees, active and retired, to purchase fixed number of shares of stock at a stated price. The plan features include vesting requirements and payment terms.

The cost of equity-settled transactions with employees is measured by reference to the fair value on the date at which the options are granted. The fair value is determined using the Black-Scholes Option Pricing Model. 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 year represents the movement in cumulative expense recognized as at the beginning and end of the reporting year.

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 due 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.

Long-term Incentive Plan

Liability arising from the long-term incentive plan is determined using the projected unit credit actuarial valuation method.

The liability relating to the long-term incentive plan comprises the present value of the defined benefit obligation at the end of the reporting date.

Revenue Recognition

Revenues are stated at amounts invoiced to customers, net of discounts, rebates, *VAT* and duty, where applicable. Revenue is recognized to the extent that it is probable that the economic benefits will flow to the *Company*, the revenue can be reliably measured. In addition, collectibility is reasonably assured and the delivery of the goods or rendering of the service has occurred. The *Company* assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent, The *Company* 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) system loss charge, (d) distribution charge, (e) supply charge, (f) metering charge, (g) Currency Exchange Rate Adjustment or *CERA* I and II and (h) inter-class and lifeline subsidies. Value added and local franchise taxes, the Power Act Reduction (for residential customers) and the universal charges are also separately presented in the customer's billing statement. Value added and local franchise taxes and universal charges, which are billed and merely collected on behalf of the national and local governments, do not form part of the *Company*'s revenues.

Sale of Real Estate

Sale of real estate, which includes the sale of the land and condominium units, is generally accounted for using the full accrual method. The percentage-of-completion method is used to recognize income from sale of projects including condominium units where the *Company* has material obligations under the sales contract to complete the projects after the properties are sold. Under this method, revenue is recognized as the related obligations are fulfilled, measured principally on the basis of the estimated completion of a physical proportion of the contract work.

The *Company* accounts for cash received as "Deposits from condominium units pre-sold" when the construction is not beyond a preliminary stage. Construction is not beyond a preliminary stage if engineering and design work, execution of construction contracts, site clearance and preparation, excavation, and completion of the building foundation are incomplete. Proceeds shall be accounted for as deposits until the criteria for revenue recognition under percentage-of-completion method are met. Collections received in excess of receivables recognized under the percentage-of-completion method are shown separately as part of "Trade payables and accrued expenses" account in the consolidated statement of financial position.

Cost of condominium units sold before completion of the project is determined based on actual costs and project estimates of building contractors and technical staff.

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 from contract penalty provisions, and final contract settlements, which may result in revisions to estimated costs and gross margins are recognized in the year in which the changes are determined.

Service fees are recognized when the services are rendered.

Consulting fees are recognized when services are rendered.

Interest Income

Revenue is recognized as interest accrues, using the effective interest rate, which is the rate that discounts estimated future cash receipts through the expected life of the financial instrument.

Dividends

Revenue is recognized when the *Company*'s right to receive the payment is established.

Lease Income

Lease income is generated from investment properties, poles, condominium units held for lease and retail outlets as part of the *Company*'s mall operations. Lease contracts are with third parties and are accounted for on a straight-line basis over the lease terms.

Lease income is included under “Revenues – Sale of services and others” in the consolidated statement of income.

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 *Company* does not transfer substantially all the risk and benefits of ownership of the asset are classified as operating lease. Initial direct cost 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 the *Parent Company*'s functional and presentation currency. The Philippine peso is the currency of the primary economic environment in which the *Parent Company* operates. This is also the currency that mainly influences the revenue from and cost of rendering services. Each entity in the *Company* determines it own functional currency and items included in the financial statements of each entity are measured using that functional currency.

The functional and presentation currency of the entities under the Company (except *LOIL*) is the Philippine peso.

The functional currency of *LOIL* 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 at the functional closing rate of exchange prevailing at the end of the reporting date. 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 an associate, 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 periods are measured at the amount expected to be recovered from or paid to the taxation authority. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted as at the 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 rate 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 have been 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 deferred income tax assets against deferred 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 attributable to equity holders of the *Parent Company* 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 attributable to equity holders of the parent by the weighted average number of shares outstanding, adjusted for the effects of all 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 year-end events that provide additional information about the *Company*'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 benefit. Amount of proceeds and/or fair value of consideration received in excess of par value are/is recognized as additional paid-in capital.

Employee share-based payment plan represents the cumulative compensation expense recognized based on the *Company*'s share-based payment plan.

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, including reclassification adjustments, that are not recognized in profit or loss as required or permitted by *PFRS*.

Non-controlling interests represent the equity interests in *Rockwell Land, CEDC* and *MIESCOR and its subsidiaries*, which are not held by the *Parent Company*.

6. Management's Use of Judgments, Estimates and Assumptions

The preparation of the *Company*'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 *Company*'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*, is the Philippine peso. The functional and presentation currency of *LOIL* is the U.S. dollar.

Operating Lease Commitments

As Lessor

As a lessor, the *Company* has several lease arrangements. Based on the terms and conditions of the arrangements, the *Company* has evaluated that the significant risks and rewards of ownership of such properties are retained by the *Company*. 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, the *Company* has commercial lease arrangements covering certain office spaces, payment offices, substation sites and towers, and transmission lines. The *Company* 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 *Company* the ownership over the assets at the end of the lease term and do not provide the *Company* with a bargain purchase option over the leased assets. Consequently, the lease agreements are accounted for as operating leases.

Arrangement that Contains a Lease

The *Company*'s purchased power agreements or *PPA*s and transmission line agreements or *TLA*s, with Independent Power Producers, or *IPP*s, qualify as leases on the basis that the *Company* and the *IPP*s have take or pay arrangements where payments for purchased power are made on the basis of the availability of the power plant and not on actual consumption. In determining the lease classification, it is judged that substantially all the risks and rewards incident to the ownership of the *IPP*s' power plants are with the *IPPs*. Thus, the *PPAs* and *TLAs* are classified as operating leases. Accordingly, capacity fees, fixed operating fees 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 ₱19,960 million, ₱20,900 million and ₱21,592 million in 2010, 2009 and 2008, respectively. This is recognized as "Purchased power" in the consolidated statements of income.

See *Note 28 – Revenues and Purchased Power*.

Contingencies

The *Company* 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 the control of the *Company*. 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 33 – Contingencies*.

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 and Investment Properties

The *Company* estimates the useful lives of utility plant and others as well as 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 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 of the utility plant and others as well as investment properties 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 the *Company*'s utility plant and others and investment properties would increase recorded operating expenses and decrease noncurrent assets.

The total depreciation and amortization of utility plant and others amounted to ₱5,958 million, ₱4,882 million and ₱4,305 million for the years ended December 31, 2010, 2009 and 2008, respectively. Total carrying values of utility plant and others, net of accumulated depreciation and amortization amounted to ₱101,009 million and ₱98,231 million as at December 31, 2010 and 2009, respectively.

Total depreciation for investment properties amounted to ₱219 million, ₱163 million, and ₱121 million for the years ended December 31, 2010, 2009 and 2008, respectively. Total carrying value of investment properties, net of accumulated depreciation amounted to ₱8,037 million and ₱8,021 million as at December 31, 2010 and 2009, respectively.

See *Note 8 – Utility Plant and Others* and *Note 11 – Investment Properties*.

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 a suitable discount rate in order to calculate the present value of those cash flows.

Determining the recoverable amount of utility plant and others, construction in progress, investment properties, investments in associates and a joint venture, deferred pass-through fuel costs, 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 could cause management to conclude that utility plant and others, construction in progress, investment properties, investments in associates and a joint venture, deferred pass-through fuel costs and other noncurrent assets are impaired. Any resulting impairment loss could have a material adverse impact on the *Company*'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 noncurrent assets subject to impairment review are as follows:

	2010	2009
	(Amounts in Millions)	
Utility plant and others - net	**₱101,009**	₱98,231
Construction in progress	**2,241**	3,627
Investment properties - net	**8,037**	8,021
Deferred pass-through fuel costs	**1,222**	3,161
Investments in associates and a joint venture	**321**	1,203
Pass through *VAT* - net	**3,024**	3,651
Deferred input *VAT*	**1,006**	816
Receivable from the Bureau of Internal Revenue, or *BIR*	**577**	577
Intangible assets	**513**	255
Goodwill	**36**	36

See *Note 8 – Utility Plant and Others*, *Note 9 – Construction in Progress*, *Note 10 – Investments in Associates and a Joint Venture*, *Note 11 – Investment Properties*, *Note 12 – Deferred Pass-Through Fuel Costs* and *Note 13 – Other Noncurrent Assets*.

Goodwill

The *Company*'s consolidated financial statements and results of operations reflect acquired businesses after the completion of the respective acquisition. The *Company* 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 *Company*'s 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 *Company*'s results of operations.

Realizability of Deferred Tax Assets

The *Company* 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 income 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:

	2010	2009
	(Amounts in Millions)	
Recognized deferred tax assets	**₱7,991**	₱7,531
Unrecognized deferred tax assets	**12**	12

See *Note 32 – Income and Franchise Taxes*.

Determination of Fair Values of Financial Assets and 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.

Total fair values of financial assets and liabilities as at December 31, 2010 amounted to ₱54,630 million and ₱81,075 million, respectively, while the total fair values of financial assets and liabilities as at December 31, 2009 amounted to ₱45,673 million and ₱82,304 million, respectively.

See *Note 31 – Financial Assets and Liabilities*.

Estimating Allowance for Doubtful Accounts

If there is objective evidence that an impairment loss has been incurred in the *Company's* trade and other receivables, 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 collectibility of the accounts. In these cases, use of judgment based on the best available facts and circumstances, including but not limited to, the length of *the Company*'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 Company*'s receivables to amounts that the *Company* expect 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 characteristic, 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 recognized in the consolidated statement of income amounted to ₱982 million, ₱886 million and ₱1,566 million for the years ended December 31, 2010, 2009 and 2008, respectively. Trade and other receivables, net of asset impairment, amounted to ₱25,609 million and ₱21,600 million as at December 31, 2010 and 2009, respectively.

See *Note 15 – Trade and Other Receivables* and *Note 29 – Expenses and Income*.

Estimating Net Realizable Value of Inventories and Materials and Supplies

Inventories consist of condominium units for sale and, materials and supplies used in the power distribution and services segments of the *Company*. 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 ₱2,043 million and ₱1,857 million as at December 31, 2010 and 2009, respectively.

See *Note 16 – Inventories*.

Estimation of Pension Benefit Costs and Other Retirement Benefits

The cost of defined benefit plans and present value of the pension obligation are actuarially determined. Actuarial valuation includes making various assumptions, which includes discount rates, expected rates of return on plan assets, rates of compensation increases and mortality rates. Actual results that differ from the *Company's* assumptions are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceed 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. Due to complexity of valuation, the underlying assumptions and its long-term nature, a defined benefit obligation is highly sensitive to changes in assumptions. While management believes that the assumptions are reasonable and appropriate, significant differences in the actual experience or significant changes in the assumptions may materially affect cost for pension and other retirement obligations. All assumptions are reviewed at each reporting date.

Total consolidated defined pension benefit costs amounted to ₱1,766 million, ₱1,886 million and ₱1,889 million for the years ended December 31, 2010, 2009 and 2008, respectively. Unrecognized net actuarial losses as at December 31, 2010 amounted to ₱1,521 million while net actuarial gains as at December 31, 2009 amounted to ₱1,362 million. Except for *Rockwell Land*, consolidated net pension liability as at December 31, 2010 and 2009 amounted to ₱8,227 million and ₱10,301 million, respectively. The net pension asset of *Rockwell Land* as at December 31, 2010 and 2009 amounted to ₱50 million and ₱66 million, respectively.

See *Note 29 – Expenses and Income* and *Note 30 – Long-term Employee Benefits*.

Share-based Payment Transactions

The *Company*'s Employee Stock Purchase Plan, or *ESPP*, grants qualified participants the right to purchase common shares of the *Company* at a grant price. The *ESPP* recognizes the services received from the eligible employees and an equivalent adjustment to the equity account over the vesting period. The *Company* measures the cost of equity-settled transactions with the participants by reference to the fair value of the equity instrument at the date when such right to purchase is granted. Estimating the fair value requires the determination of the most appropriate valuation model for a grant of equity instrument depending on the terms and conditions of the grant. This also requires determining the most appropriate inputs to the valuation model and making certain assumptions. The estimates and assumptions are described in *Note 20 – Share-based Payment Plan* and include, among other things, annual stock volatility, risk-free interest rate, dividends yield, and the remaining life of options. While management believes that the estimates and assumptions used are reasonable and appropriate, significant differences in *the Company's* actual experience or significant changes in the estimates and assumptions may materially affect the stock compensation costs charged to operations.

The amounts recognized as stock compensation for the years ended December 31, 2010, 2009 and 2008, with a corresponding charge to the equity account are ₱174 million, ₱301 million and ₱116 million, respectively. As at December 31, 2010 and 2009, the balances of employee share-based payment plan in the equity section of the consolidated statements of financial position amounted to ₱743 million and ₱569 million, respectively.

See *Note 20 – Share-based Payment Plan* and *Note 29 – Expenses and Income.*

Insurance Liabilities Arising from Insurance Contracts

RSIC makes estimates of 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, prior year claims estimates 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, 2010 and 2009, gross carrying values of insurance liabilities arising from insurance contracts (included in "Other noncurrent liabilities" account) amounted to ₱293 million and ₱409 million, respectively.

Provision for Asset Retirement Obligations

Provision for asset retirement obligations are 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 square meter 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.

Revenue Recognition

The *Company*'s revenue recognition policies require the use of estimates and assumptions that may affect the reported amounts of the *Company*'s revenues and receivables.

Revenues from sale of electricity by the *Parent Company* and *CEDC* are billed based on different billing cycles with different cycle cut-off dates, while take-up of related power purchase cost in the accounts is based on calendar month. The recognition of unbilled revenues for billing cycles that have earlier than month-end cut-off dates requires the use of estimates.

The difference between the amount initially recognized and the actual settlement or actual billing is taken up in the subsequent period. Management believes that such use of estimates will not result in material adjustments in future periods.

Revenues from real estate transactions of *Rockwell Land* and 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. There is no assurance that such use of estimates may not result in material adjustments in future periods.

7. Segment Information

Each operating segment of the *Company* 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 *Company*). The operating results of each of the operating segments are regularly reviewed by the *Company*'s chief operating decision-maker to make decisions about how resources are to be allocated to the operating segments and to assess their performances, and for which discrete financial information is available.

For management purposes, the *Company*'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 is involved in the distribution and supply of electricity covering franchise areas in the Luzon islands representing 54% of the requirements of the country. This is primarily provided by *MERALCO* and *CEDC*, the latter covering the Clark Economic Zone.

- Real Estate — This segment, which is provided by *Rockwell Land*, is involved in luxury residential and commercial real estate development and leasing.

- Services and others — The services segment is involved principally in engineering, construction and consulting services, e-transaction services, insurance and power generation. These services are provided by *MIESCOR*, *MBI*, *Landbees* and *Miescorrail* (collectively known as "*MIESCOR Group*"), *MEI*, *e-MVI*, *RSIC*, *LOIL*, *Finserve*, *CIS*, *CIS Bayad Center* and *OTC* (collectively known as "*CIS Group*") and *MPG.*

The chief operating decision-maker or management monitors the operating results of each business unit separately for the purpose of making decisions about resource allocation and performance assessment. Performance is evaluated based on net income for the year, earnings before interest, taxes and depreciation and amortization, or *EBITDA*; *EBITDA* margin; and core net income. Net income for the year is measured consistent with consolidated net income in the consolidated financial statements.

EBITDA is measured as net income excluding depreciation and amortization, impairment of noncurrent assets, financing costs, carrying charges, interest and other financial income, equity in net earnings of associates and a joint venture, foreign exchange gains (losses) - net, gains (losses) on derivative financial instruments - net, provision for (benefit from) income tax and other non-recurring gains (losses) - net, if any.

Core net income for the year is measured as net income attributable to equity holders of the *Parent Company* adjusted for foreign exchange gains or losses, gains or losses on derivative financial instruments, asset impairment on noncurrent assets, one time approvals of carrying charges of *ERC*-approved under or over-recoveries, and other non-recurring gains or losses, net of tax effect of the foregoing adjustments.

Transfer prices between operating segments are set 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 in the consolidation.

The *Company* mainly operates and generates substantially its revenues from the Philippines (i.e., one geographical location). Thus, geographical segment information is not presented. The *Company* has no revenues from transactions with a single external customer accounting for 10% or more of the *Company*'s revenues from external customers.

		Power			Real Estate			Services and Others			Inter-segment Transactions			Total		
	Notes	**2010**	2009	2008	**2010**	2009	2008	**2010**	2009	2008	**2010**	2009	2008	**2010**	2009	2008
								(Amounts in Millions)								
Revenues		**₱239,164**	₱178,752	₱187,063	**₱3,375**	₱2,877	₱2,213	**₱4,597**	₱3,703	₱3,056	**(₱1,675)**	(₱782)	(₱557)	**₱245,461**	₱184,550	₱191,775
Segment results		**20,367**	13,347	16,375	**331**	365	36	**1,596**	1,340	1,167	**–**	–	–	**22,294**	15,052	17,578
Depreciation and amortization		**(5,796)**	(4,745)	(4,294)	**(167)**	(150)	(88)	**(291)**	(169)	(44)	**35**	–	–	**(6,219)**	(5,064)	(4,426)
Provisions		**(4,118)**	(2,172)	(6,935)	**–**	–	–	**–**	–	–	**–**	–	–	**(4,118)**	(2,172)	(6,935)
Interest and other financial income	*29*	**2,017**	3,852	2,476	**580**	332	429	**128**	77	306	**(35)**	(15)	(292)	**2,690**	4,246	2,919
Equity in net earnings of associates and a joint venture	*10*	**1,012**	953	910	**–**	–	–	**–**	–	–	**(729)**	(708)	(711)	**283**	245	199
Interest and other financial charges	*29*	**(310)**	(3,243)	(3,825)	**(155)**	(117)	(53)	**(29)**	(21)	(37)	**1**	53	(220)	**(493)**	(3,328)	(4,135)
Provision for income tax - net		**(3,729)**	(2,111)	(1,526)	**(145)**	(143)	(144)	**(446)**	(368)	(397)	**–**	–	–	**(4,320)**	(2,623)	(2,067)
Non-controlling interests		**–**	–	–	**–**	–	–	**–**	–	–	**(432)**	(351)	(333)	**(432)**	(351)	(333)
Net income attributable to equity holders of the Parent		**₱9,443**	₱5,881	₱3,181	**₱444**	₱287	₱180	**₱958**	₱859	₱995				**₱9,685**	₱6,005	₱2,800

The following table shows the reconciliation of the consolidated EBITDA to consolidated net income:

	2010	2009
	(Amounts in Millions)	
Consolidated EBITDA	**₱18,452**	₱13,169
Depreciation and amortization	**(6,219)**	(5,064)
Interest and other financial expenses	**(493)**	(3,328)
Equity in net earnings of associates and a joint venture	**283**	245
Present value impact on customers' refund	**(225)**	(555)
Foreign exchange gains - net	**(51)**	266
Interest and other income	**2,690**	4,246
Consolidated income before income tax	**14,437**	8,979
Provision for income tax	**(4,320)**	(2,623)
Consolidated net income for the year	**₱10,117**	₱6,356

The following table shows the reconciliation of the consolidated core net income to the consolidated net income:

	2010	2009
	(Amounts in Millions)	
Consolidated core net income for the year	**₱12,155**	₱7,003
Add (deduct) non-core items, net of tax:		
Approved pass-through charges and related costs	**(3,903)**	(1,241)
Reversal of interest on bill deposits	**1,219**	–
Gain on return of an investment	**248**	–
Foreign exchange gain (loss) - net	**(36)**	186
Mark-to market gain	**2**	57
Net income for the year attributable to equity holders of the Parent	**9,685**	6,005
Net income for the year attributable to non-controlling interest	**432**	351
Consolidated net income for the year	**₱10,117**	₱6,356

8. Utility Plant and Others

The movements of utility plant and others as at December 31, 2010 and 2009 are as follows:

	Notes	Subtransmission and Distribution	Land	Buildings and Improvements	Communication Equipment	Office Furniture, Fixtures and Other Equipment	Transportation Equipment	Others	Total
					2010				
					(Amounts in Millions)				
Cost									
Balance at beginning of year		₱117,752	₱15,001	₱4,727	₱5,647	₱4,974	₱1,922	₱2,336	₱152,359
Transfers from construction in progress	9	6,594	–	239	398	–	–	27	7,258
Additions		1,556	20	34	34	545	453	129	2,771
Disposals/retirements		(4,747)	–	–	(1)	(1,182)	(65)	(1)	(5,996)
Transfer to investment properties	11	–	(151)	–	–	–	–	–	(151)
Reclassification and others		57	–	(39)	(185)	(26)	15	177	(1)
Balance at end of year		121,212	14,870	4,961	5,893	4,311	2,325	2,668	156,240
Less Accumulated Depreciation and Amortization									
Balance at beginning of year		42,244	–	1,802	3,882	3,758	1,105	1,337	54,128
Charge for the year		4,649	–	121	426	482	157	123	5,958
Disposals/retirements		(3,645)	–	–	(1)	(1,182)	(52)	(1)	(4,881)
Reclassification and others		105	–	(9)	(212)	17	216	(91)	26
Balance at end of year		43,353	–	1,914	4,095	3,075	1,426	1,368	55,231
Net book value		₱77,859	₱14,870	₱3,047	₱1,798	₱1,236	₱899	₱1,300	₱101,009

	Notes	Subtransmission and Distribution	Land	Buildings and Improvements	Communication Equipment	Office Furniture, Fixtures and Other Equipment	Transportation Equipment	Others	Total
					2009				
					(Amounts in Millions)				
Cost									
Balance at beginning of year		₱112,102	₱15,622	₱4,511	₱5,334	₱4,669	₱1,956	₱2,119	₱146,313
Transfers from construction in progress	9	6,597	–	145	417	316	126	243	7,844
Additions		35	–	2	12	56	44	38	187
Disposals/retirements		(1,766)	–	–	(132)	(53)	(199)	(24)	(2,174)
Transfer to investment properties	11	–	(621)	–	–	–	–	–	(621)
Transfer from investment properties	11	17	–	27	–	–	–	–	44
Reclassification and others		767	–	42	16	(14)	(5)	(40)	766
Balance at end of year		117,752	15,001	4,727	5,647	4,974	1,922	2,336	152,359
Less Accumulated Depreciation and Amortization									
Balance at beginning of year		40,044	–	1,695	3,280	3,498	1,087	1,005	50,609
Charge for the year		3,746	–	112	457	347	42	178	4,882
Disposals/retirements		(1,466)	–	–	(132)	(52)	(99)	(23)	(1,772)
Reclassification and others		(80)	–	(5)	277	(35)	75	177	409
Balance at end of year		42,244	–	1,802	3,882	3,758	1,105	1,337	54,128
Net book value		₱75,508	₱15,001	₱2,925	₱1,765	₱1,216	₱817	₱999	₱98,231

A significant portion of the *Company*'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. The *Company* records the 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. See *Note 26 – Trade Payables and Accrued Expenses* and *Note 31 – Financial Assets and Liabilities*.

9. Construction in Progress

The movements of construction in progress are as follows:

	Notes	2010	2009
		(Amounts in Millions)	
Balance at beginning of year		**₱3,627**	₱5,002
Net additions		**5,872**	7,914
Transfers to utility plant and others	8	**(7,258)**	(7,844)
Transfer to investment properties	11	**–**	(1,445)
Balance at end of year		**₱2,241**	₱3,627

The construction in progress pertains to electric capital projects, or *ECP*s and non-electric capital projects, or *NEPs*. *ECPs* are capital projects involving construction of new facilities and the upgrade and major rehabilitation of existing electrical facilities. In 2010, major *ECP*s under construction in progress consist of 115kV subtransmission lines (Zapote-Legaspi-Kamagong and Balintawak-Sta. Mesa) and one 34.5kV distribution line (Ternate-TMC2 Tie-line). *NEPs* relate to construction of non-network structures and/or major renovation of existing non-network facilities.

Total interest capitalized and included in the "Construction in progress" account amounted to ₱119 million and ₱98 million as of December 31, 2010 and 2009, respectively.

The average annual range of interest rates of interest used for capitalization in 2010 and 2009 ranged from 7.6% to 8.6% and 8.6% to 8.8%, respectively.

10. Investments in Associates and a Joint Venture

This account consists of:

	Country of Incorporation	Principal Activities	Percentage of Ownership 2010 Direct	2010 Indirect	2009 Direct	2009 Indirect
Associates						
Bauang Private Power Corporation or *BPPC*	Philippines	Power Generation	**38**	**–**	–	–
General Electric Philippines Meter and Instrument Company, Inc. or *GEPMICI*	Philippines	Sale of metering products and services	**35**	**–**	35	–
First Private Power Corporation or *FPPC*	Philippines	Power Generation	**–**	**–**	40	–
Joint Venture						
Indra Philippines	Philippines	Management and information technology, or *IT*, consultancy	**50**	**–**	50	–

The movements in the investments in associates and a joint venture account follow:

	2010	2009
	(Amounts in Millions)	
Acquisition costs:		
Balance at beginning of year	**₱459**	₱465
Return of capital	**(397)**	(6)
Balance at end of year	**62**	459
Accumulated equity in net earnings:		
Balance at beginning of year	**60**	782
Equity in net earnings for the year	**283**	245
Dividends received	**(96)**	(445)
Adjustments	**–**	(657)
Depreciation on share in revaluation increment	**–**	129
Return of capital	**–**	6
Balance at end of year	**247**	60
Share in cumulative translation adjustment of an associate:		
Balance at beginning of year	**684**	2
Movements	**(672)**	682
Balance at end of year	**12**	684
	₱321	₱1,203

Investment in FPPC

FPPC was organized in October 1992 to engage in the power generation business. In response to the Philippine Government's then program to fast track stabilization of the power industry, FPPC incorporated *BPPC* and constructed the 195-*MW* Bauang generating plant, or Bauang plant, under a Build-Operate-Transfer, or *BOT* Agreement, sponsored by the *NPC.*

In accordance with the *BOT* Agreement signed in 1993, *FPPC* constructed the 215 *MW* Bauang plant and operated the same under a 15-year Cooperation Period up to July 25, 2010.

On July 26, 2010, *FPPC/BPPC* turned-over the *Bauang Plant* to *NPC* without any compensation and free of any liens. Hence, *FPPC/BPPC* has been winding down operations.

Consistent with its limited administrative activities, the *BODs* of *FPPC* and *BPPC* approved the merger of the two entities with *BPPC* as the surviving entity. The merger resulted in a 2% dilution of the *Parent Company's* interest in *BPPC.*

Investment in GEPMICI

GEPMICI was established in 1979, with the General Electric Company or *GE Company* of U.S.A., to serve the Philippine market for ANSI-type Watt-hour meters.

Investment in 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.

See *Note 27 – Related Party Transactions* for details of transactions.

The carrying values of investments in associates and a joint venture follow:

	2010	2009
	(Amounts in Millions)	
Indra Philippines	**₱174**	₱151
BPPC	**89**	–
GEPMICI	**58**	63
FPPC	**–**	989
	₱321	₱1,203

The condensed financial information of *BPPC* (for 2010), *FPPC* (for 2009*), GEPMICI* and *Indra Philippines* follow:

	2010			2009		
	BPPC	**GEPMICI**	**Indra Philippines**	BPPC	GEPMICI	Indra Philippines
			(Amounts in Millions)			
Current assets	**₱251**	**₱205**	**₱554**	₱2,686	₱199	₱472
Noncurrent assets	**–**	**22**	**128**	2,242	13	134
Current liabilities	**(15)**	**(61)**	**(324)**	(193)	(31)	(284)
Noncurrent liabilities	**–**	**–**	**(10)**	(2,264)	–	(20)
Net assets	**₱236**	**₱166**	**₱348**	₱2,471	₱181	₱302

	2010			2009			2008		
	BPPC	**GEPMICI**	**Indra Philippines**	FPPC	GEPMICI	Indra Philippines	FPPC	GEPMICI	Indra Philippines
					(Amounts in Millions)				
Revenues	**₱442**	**₱115**	**₱948**	₱973	₱377	₱922	₱1,210	₱396	₱832
Costs and expenses	**(451)**	**(100)**	**(888)**	(436)	(335)	(834)	(786)	(359)	(778)
Net income (loss)	**(₱9)**	**₱15**	**₱60**	₱537	₱42	₱88	₱424	₱37	₱54

11. Investment Properties

The movements in investment properties are as follows:

			2010	
	Note	**Land**	**Buildings and Improvements**	**Total**
			(Amounts in Millions)	
Cost:				
Balance at beginning of year		**₱3,155**	**₱6,018**	**₱9,173**
Additions during the year		**–**	**110**	**110**
Transfer from utility plant and others	*8*	**151**	**–**	**151**
Disposal of investment properties		**(26)**	**–**	**(26)**
Balance at end of year		**3,280**	**6,128**	**9,408**
Accumulated depreciation:				
Balance at beginning of year		**–**	**1,152**	**1,152**
Charge for the year		**–**	**219**	**219**
Balance at end of year		**–**	**1,371**	**1,371**
Net book value		**₱3,280**	**₱4,757**	**₱8,037**

			2009	
	Note	Land	Buildings and Improvements	Total
			(Amounts in Millions)	
Cost:				
Balance at beginning of year		₱2,551	₱3,943	₱6,494
Additions during the year		–	662	662
Transfer from utility plant and others	*8*	621	–	621
Transfer to utility plant and others	*8*	(17)	(27)	(44)
Transfer from construction in progress	*9*	–	1,445	1,445
Transfer to land and development costs		–	(5)	(5)
Balance at end of year		3,155	6,018	9,173
Accumulated depreciation:				
Balance at beginning of year		–	989	989
Charge for the year		–	163	163
Balance at end of year		–	1,152	1,152
Net book value		₱3,155	₱4,866	₱8,021

Investment properties are stated at cost. These consist of real properties held for capital appreciation, future or previous substation sites, and real properties, mainly the Rockwell Power Plant Mall at Rockwell Center, Makati City and *BPO* buildings at the *MERALCO* compound, which are being leased to related and third parties.

Charges for leases to related and third parties are made at market rates. Lease income (included as part of "Revenues - sale of contracts, services and others") earned from investment properties amounted to ₱633 million, ₱566 million and ₱542 million in 2010, 2009 and 2008, respectively. Direct operating expenses incurred for investment properties that generated income amounted to ₱267 million, ₱231 million and ₱357 million in 2010, 2009 and 2008, respectively.

As at December 31, 2010 and 2009, unamortized borrowing costs capitalized as part of investments properties amounted to ₱261 million and ₱270 million, respectively.

The aggregate fair value of the *Company's* investment properties are as follows:

	2010	2009
	(Amounts in Millions)	
Rockwell Power Plant Mall	**₱5,947**	₱5,159
BPO building	**2,408**	2,247
Land where *Rockwell-Meralco* BPO Venture and "The Strip" are located	**2,026**	1,689
Other investment properties held for lease	**2,073**	1,797

As at December 31, 2010 and 2009, the Rockwell Power Plant Mall was partially used as collateral for *Rockwell Land's* long-term interest bearing financial liabilities.

The fair values of investment properties as at December 31, 2010 were determined by independent professionally qualified appraisers, namely, Asian Appraisal Company, Inc. for the *Parent Company* and Vitale Valuation Services, Inc. for *Rockwell Land*. The fair values represent the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's-length transaction at the date of valuation.

12. Deferred Pass-through Fuel Costs

Deferred pass-through fuel costs represent amounts paid for the quantity and the cost of natural gas that was contracted for but not yet consumed by the *Parent Company*'s major *IPP*s, namely, *FGPC* and *FGP* collectively referred to as "*First Gas.*" See *Notes 26 – Trade Payables and Accrued Expenses, Note 27 – Related Party Transactions* and *Note 33 – Contingencies*. Any unconsumed gas is the result of lower dispatch of the *First Gas* plants vis-a-vis their stipulated capacity factors.

In 2005, *First Gas* billed the *Parent Company* for 44 million giga-joules in gross calorific value representing unconsumed gas for the years 2002 to 2004. The *Parent Company's* obligations to pay for unconsumed gas were deferred until the resolution of the dispute between *First Gas* and the *Gas Sellers* (Shell Philippines Exploration B.V., Shell Philippines LLC, Texaco Philippines, Inc., and PNOC Exploration Corporation) under the Gas Sale and Purchase Agreements or *GSPA*. *FGP* and *FGPC* each have a distinct *GSPA* with the *Gas Sellers* for the supply of natural gas in connection with the operations of the power plants. The *GSPAs* with *FGPC* and *FGC* expire on August 25, 2025 and September 25, 2007, respectively.

Under the *GSPAs*, *FGP* and *FGPC* are each obligated to consume (or pay for, if not consumed) a minimum quantity of gas for each contract year (which runs from December 26 of a particular year up to December 25 of the immediately succeeding year), called the *Take-or-Pay Quantity* or *TOPQ*. Thus, if the *TOPQ* is not consumed within a particular contract year, *FGP* and *FGPC* will incur an "annual deficiency" for that contract year equivalent to the total volume of unused gas. *FGP* and *FGPC* are required to make payments to the *Gas Sellers* for such annual deficiency after the end of the contract year. After paying for annual deficiency, *First Gas* can, subject to the terms of the *GSPA*, "make-up" such annual deficiency by consuming the unused-but-paid-for gas (without further charge) within 10-contract years after the contract year for which the annual deficiency was incurred, in the order that it arose.

On December 29, 2006, the *Gas Sellers* issued the Annual Reconciliation Statements or *ARS*, of *FGP* and *FGPC* for contract year 2006. The *Gas Sellers* then claimed annual deficiency payments amounting to $3.9 million for *FGP* and $5.4 million for *FGPC*. Both *FGP* and *FGPC* disagreed that such Annual Deficiency payments are due and each claimed for among others, relief due to events of force majeure or *EFM* that affected the San Lorenzo and Santa Rita plants, respectively. *FGP's* and *FGPC*'s position is that the power plants actually consumed more than their respective *TOPQs* and are entitled to make-up its outstanding balance of annual deficiency.

Pursuant to the terms of the *GSPAs*, the dispute on the foregoing matter was subjected to arbitration in Hong Kong, SAR under the *International Chamber of Commerce* or *ICC* Rules of Arbitration, whereby a Partial Final Award was rendered on August 11, 2009. The Tribunal determined that the transmission-related events claimed by *FGP* and

FGPC constitute *EFM* under the *GSPA*s. The *Tribunal* was not persuaded, however, that the government-related events claimed by *FGP* and *FGPC* for contract year 2006 constitute *EFM* under the *GSPA*s based on the evidence presented. Any settlement to *FGP* and *FGPC* shall be billed *MERALCO*.

On June 9, 2010, *FGP*, *FGPC*, and the *Gas Sellers* executed a Settlement Agreement or *SA* to settle the *GSPA* dispute for Contract Year 2006. On July 29, 2010, *MERALCO* fully settled the amount of ₱104 million ($2.2 million) billed by *First Gen*.

On September 15, 2010, *FGP* and *FGPC* received the Final Award by Consent rendered by the Tribunal on September 13, 2010, incorporating by reference the June 9, 2010 *SA*, including all exhibits thereto, and forming an inseparable part of the Final Award by Consent, as per *FGP*, *FGPC*, and the *Gas Sellers*, written request dated June 16, 2010 to the Tribunal and *ICC*.

The liability for unconsumed gas amounting to ₱433 million as at December 31, 2009 was already reduced to zero as of December 31, 2010.

See *Note 26 – Trade Payables and Accrued Expenses*.

13. Other Noncurrent Assets

This account consists of:

	Note	**2010**	2009
		(Amounts in Millions)	
Unbilled receivables - net of current portion	*15*	**₱3,063**	₱5,406
Pass-through *VAT* - net		**3,024**	3,651
Deferred input *VAT*		**1,006**	816
SC GRAM case refund	*2*	**780**	780
Receivable from *BIR*	*33*	**577**	577
Intangible assets		**513**	255
AFS investments	*31*	**403**	361
Advance payments to suppliers		**253**	135
Deferred reinsurance premium		**214**	165
Pension asset	*30*	**50**	66
Installment contracts receivable - net of current portion	*15*	**39**	54
Goodwill		**36**	36
Derivative assets - net of current portion of ₱11 million in 2009	*18 and 31*	**–**	172
Others - net		**381**	710
		₱10,339	₱13,184

Unbilled Receivables

Unbilled receivables represent unbilled generation and other pass-through costs incurred by the *Company*. It includes unbilled charges covered by an approved recovery mechanism but is expected to be collected beyond one year. These also include other unbilled generation and pass-through charges of prior years, which are the subject of applications for recovery with the *ERC*.

Pass-through VAT

Pass-through *VAT* pertains to *VAT* on pass-through generation and transmission costs. Remittance of such deferred *VAT* is based on collection of billed receivables from the customers. The balance represents *VAT* on unpaid billed receivables, net of amount paid to the Independent Power Producers or *IPP*s under existing terms and conditions of the contract.

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 life of the related capital assets or 60 months, whichever is shorter, against the output *VAT* due.

SC GRAM Case Refund

The balance represents amount of refund made by the *Parent Company* to its customers as directed by the *SC* in response to the Petition of an electricity consumer group that the *IRR* for the collection by *MERALCO* of the rate adjustment under the second *GRAM* that was not published nor was subjected to a public hearing. On

November 12, 2010, *MERALCO* filed an application to recover the amount previously refunded including any additional amount still to be refunded and corresponding carrying charges.

See *Note 2 – Rate Regulations* for the related discussions.

Intangible Assets

The movements of intangible assets are as follows:

	2010		
	Software	**Franchise**	**Total**
		(Amounts in Millions)	
Cost:			
Balance at beginning of year	**₱274**	**₱–**	**₱274**
Additions during the year	**251**	**49**	**300**
Balance at end of year	**525**	**49**	**574**
Less accumulated amortization:			
Balance at beginning of year	**19**	**–**	**19**
Amortization for the year	**42**	**–**	**42**
Balance at end of year	**61**	**–**	**61**
Net book value	**₱464**	**₱49**	**₱513**

	2009		
	Software	Franchise	Total
		(Amounts in Millions)	
Cost:			
Balance at beginning of year	₱147	₱–	₱147
Additions during the year	127	–	127
Balance at end of year	274	–	274
Less accumulated amortization:			
Balance at beginning of year	–	–	–
Amortization for the year	19	–	19
Balance at end of year	19	–	19
Net book value	₱255	₱–	₱255

AFS Investments

AFS investments consist mainly of proprietary club shares, which are stated in their fair market values:

	2010	2009
	(Amounts in Millions)	
Rockwell Leisure Club, Inc.	**₱267**	₱242
Manila Golf and Country Club, Inc.	**53**	46
Wack-Wack Golf Club, Inc.	**24**	19
Others	**59**	54
	₱403	₱361

14. **Cash and Cash Equivalents**

This account consists of:

	2010	2009
	(Amounts in Millions)	
Cash on hand and in banks	**₱3,631**	₱6,399
Cash equivalents	**20,739**	10,669
	₱24,370	₱17,068

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 months depending on the *Company*'s immediate cash requirements, and earn interest at the prevailing short-term investment rates.

15. Trade and Other Receivables

This account consists of:

	Notes	2010	2009
		(Amounts in Millions)	
Trade:			
Electricity:			
Billed		**₱17,776**	₱15,362
Unbilled	*2 and 13*	**5,011**	5,537
Current portion of installment contracts receivable	*13*	**2,183**	367
Service contracts and others		**1,326**	1,278
Nontrade	*27*	**1,014**	1,378
		27,310	23,922
Less allowance for doubtful accounts		**1,701**	2,322
		₱25,609	₱21,600

Billed receivables from sale of electricity of the *Parent Company* and *CEDC* consist of the following:

	2010	2009
	(Amounts in Millions)	
Residential	**₱6,007**	₱5,338
Commercial	**8,058**	6,988
Industrial	**3,300**	2,584
Flat streetlights	**411**	452
	17,776	15,362
Less allowance for doubtful accounts	**1,518**	2,088
	₱16,258	₱13,274

Movements of allowance for doubtful accounts for trade and other receivables are as follows:

2010	Balance at Beginning of Year	Provisions (see Note 29)	Recoveries (see Note 29)	Write-offs	Balance at End of Year
			(Amounts in Millions)		
Billed trade receivables:					
Commercial	**₱1,007**	**₱509**	**(₱25)**	**(₱633)**	**₱858**
Residential	**529**	**412**	**(232)**	**(348)**	**361**
Industrial	**259**	**100**	**(4)**	**(298)**	**57**
Flat streetlights	**293**	**105**	**(4)**	**(152)**	**242**
	2,088	**1,126**	**(265)**	**(1,431)**	**1,518**
Other receivables	**234**	**121**	**–**	**(172)**	**183**
	₱2,322	**₱1,247**	**(₱265)**	**(₱1,603)**	**₱1,701**

2010	Residential	Commercial	Industrial	Flat Streetlights	Others	Total
			(Amounts in Millions)			
Individually impaired	**₱247**	**₱73**	**₱41**	**₱2**	**₱–**	**₱363**
Collectively impaired	**114**	**785**	**16**	**240**	**183**	**1,338**
Total	**₱361**	**₱858**	**₱57**	**₱242**	**₱183**	**₱1,701**

2009	Balance at Beginning of Year	Provisions (see Note 29)	Recoveries (see Note 29)	Write-offs	Balance at End of Year
			(Amounts in Millions)		
Billed trade receivables:					
Residential	₱774	₱319	(₱84)	(₱480)	₱529
Commercial	608	478	(8)	(71)	1,007
Industrial	267	22	(8)	(22)	259
Flat streetlights	278	26	(1)	(10)	293
	1,927	845	(101)	(583)	2,088
Other receivables	92	148	(6)	–	234
	₱2,019	₱993	(₱107)	(₱583)	₱2,322

2009	Residential	Commercial	Industrial	Flat Streetlights	Others	Total
			(Amounts in Millions)			
Individually impaired	₱452	₱303	₱187	₱87	₱185	₱1,214
Collectively impaired	77	704	72	206	49	1,108
Total	₱529	₱1,007	₱259	₱293	₱234	₱2,322

Trade Receivables – Electricity

Trade receivables of the *Parent Company* and *CEDC* include charges for pass-through costs. Pass-through costs consist of generation and transmission charges, which constitute 67% and 11%, respectively, of the total billed amount in 2010. 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 succeeding billing period. This also includes the current portion of pass-through cost under-recoveries already approved for recovery by the *ERC*. The *Parent Company's* and *CEDC*'s trade receivables are noninterest-bearing and are substantially secured by bill deposits. See *Note 22 – Customers' Deposits.*

Installment Contracts Receivable

Installment contracts receivable represent receivables from sale of condominium units with credit terms ranging from one to five years. As at December 31, 2010 and 2009, the gross undiscounted trade receivables (both recognized and future receivables) from sale of the "Number One Rockwell" or *One Rockwell* and "The Grove by Rockwell" or *The Grove*, condominium projects amounting to ₱1,400 million and ₱1,100 million, respectively, have been assigned as security for interest-bearing long-term financial liabilities. Under the terms of the assignment, *Rockwell Land* will deliver all Contracts to Sell and customers' copies of the Condominium Certificates of Title covered by these receivables to be held in custody by the counterparty until the receivables are paid and/or repurchased by *Rockwell Land*. *Rockwell Land* also agreed that the counterparty may at its sole option, assign, sell, transfer or otherwise dispose of, or encumber or create a lien or liability on the receivables in favor of any third party. See *Note 21 – Interest Bearing Long-term Financial Liabilities.*

Service Contracts and Others

Service contracts receivable arise from contracts entered into by *Miescor* and subsidiaries, *e-MVI*, *RSIC*, *CIS* and *Bayad Center* for construction, engineering, consulting, insurance underwriting, bill payment collection, tellering, data transport and e-business development services to third parties.

Receivables from service contracts and others are noninterest-bearing and are generally on 30 to 60-day terms.

16. **Inventories**

	2010	2009
	(Amounts in Millions)	
Materials and supplies:		
At net realizable value	**₱2,030**	₱1,801
At cost	**2,088**	1,862
Condominium units for sale:		
At net realizable value	**13**	56
At cost	**13**	56
Total inventories at the lower of cost or net realizable value	**₱2,043**	₱1,857

No significant writedown of inventories and supplies was recognized in December 31, 2010, 2009 and 2008.

See *Note 6 – Significant Accounting Judgments and Estimates,* and *Note 29 – Expenses and Income.*

17. Land and Development Costs

As at December 31, 2010 and 2009, this account represents land and development costs of *Rockwell Land*, consisting of the following:

	Note	**2010**	2009
		(Amounts in Millions)	
Land and development costs:	*11*		
At net realizable value		**₱1,708**	₱1,191
At cost		**1,717**	1,200
Land and development costs at the lower of cost or net realizable value		**₱1,708**	₱1,191

Development costs pertain to the Edades Tower and Garden Villas Project or *Edades*, and *One Rockwell* residential condominium projects within the Rockwell Center in Makati City and *The Grove* located in Pasig City.

Total cash received from pre-selling activities for *Edades* and *The Grove* projects amounted to ₱741 million as of December 31, 2010 and ₱343 million as at December 31, 2009, respectively. These are shown under "Deposits from pre-selling of condominium units" account in the consolidated statements of financial position.

18. Other Current Assets

	Notes	**2010**	2009
		(Amounts in Millions)	
Advances to suppliers		**₱847**	₱1,197
Prepaid expenses		**512**	497
Creditable withholding tax		**172**	905
Input *VAT*		**156**	177
Current portion of derivative assets	*13 and 31*	**24**	11
Others		**316**	182
		₱2,027	₱2,969

Advances to Suppliers

This mainly represents advances made to suppliers and contractors of *Rockwell Land* for various construction projects.

19. Equity

Common Stock

The movements of the *Company*'s common stock as at December 31, 2010 and 2009 are as follows:

	Number of Shares	Amount
	(In Millions)	
Authorized - ₱10 par value a share	1,250	₱12,500
Issued:		
Balance as at January 1, 2009	1,104	₱11,038
Issuances	23	235
Balance as at December 31, 2009	1,127	₱11,273
Balance as at January 1, 2010	**1,127**	**₱11,273**
Issuances	**–**	**–**
Balance as at December 31, 2010	**1,127**	**₱11,273**

See *Note 20 – Share-based Payment Plan* for discussion of common stock issuances.

Unappropriated Retained Earnings

The balance of unappropriated retained earnings as at December 31, 2010 and 2009 include the balance of revaluation increment in utility plant and others and investment properties carried at deemed cost amounting to ₱18,375 million and ₱19,232 million, respectively. Such amounts are restricted for dividend declaration purposes until they are realized through depreciation or disposal of the related assets.

The following are cash dividends declared on common shares in 2010 and 2009:

Declaration Date	Record Date	Payment Date	Dividend Per Share	Amount
				(In Millions)
March 22, 2010	April 21, 2010	May 11, 2010	₱3.15	₱3,551
July 26, 2010	August 23, 2010	September 16, 2010	2.50	2,818
December 13, 2010	December 29, 2010	January 17, 2011	1.30	1,465
May 26, 2009	June 9, 2009	June 30, 2009	1.00	1,078
October 29, 2009	November 13, 2009	December 11, 2009	1.50	1,617

The *Parent Company* pays regular cash dividends equivalent to 50% of core earnings, which may be supplemented by a special dividend determined on a "look-back" basis. Any declaration and payment of a special dividend is dependent on the availability of unrestricted retained earnings and cash. The declaration, record and payment dates shall be consistent with the guidelines of the *SEC* and the *PSE*. The foregoing policy was previously approved by the *BOD*.

On February 28, 2011, the *BOD* declared cash dividend equivalent to ₱2.65 per share to all common stockholders of record as at March 28, 2011 payable on April 20, 2011.

Appropriated Retained Earnings

As at December 31, 2010, retained earnings of ₱6,000 million have been appropriated for planned business expansion of the *Parent Company.* Plans for business expansion are being developed.

20. Share-based Payment Plan

The *Parent Company* has an *ESPP*, which entitles participants to purchase common shares of the *Company* subject to certain terms and conditions, during a nominated offer period. Following are the salient features of the *ESPP*:

Participants	• Qualified regular employees of the *Parent Company* and subsidiaries • Retirees of the *Parent Company*
Purchase Price	• No less than 80% of the weighted average daily closing market price at the *PSE* during a 30-day calendar period that ends two weeks before the start of the offer period.
Holding Period	• Maximum of three years (as approved by the Board of Administrators or *BOA* for each offering)
Cancellation	• Cancellation option at anytime prior to full payment of the purchase price with refund of net amount paid by the grantee

Movements in the number of option shares outstanding under the *ESPP* are as follows:

			2010		
	12th	**13th**	**13th A**	**14th**	**Total**
Balance as at January 1, 2010	**–**	**1,911,319**	**407,137**	**12,416,994**	**14,735,450**
Issued	**–**	**(362,915)**	**–**	**(6,478)**	**(369,393)**
Balance as at December 31, 2010	**–**	**1,548,404**	**407,137**	**12,410,516**	**14,366,057**

			2009		
	12th	13th	13th A	14th	Total
Balance as at January 1, 2009	2,789,031	6,978,620	–	–	9,767,651
Issued	(2,789,031)	(5,008,902)	–	–	(7,797,933)
Subscriptions during the offer period	–	–	419,453	12,448,838	12,868,291
Cancelled	–	(58,399)	(12,316)	(31,844)	(102,559)
Balance as at December 31, 2009	–	1,911,319	407,137	12,416,994	14,735,450

The *Parent Company* allotted a total of 55 million common shares for *ESPP* awards. As at December 31, 2010, 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, which considered annual stock volatility, risk-free interest rate, expected life of the offering, exercise price of ₱51.00 to ₱74.00 a share for the 13th to the 14th offerings. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may not necessarily be the actual outcome.

Below are the grant dates and inputs to the models used for each of the grants:

	12th	13th	13th A	14th
Grant dates	December 31, 2003	May 31, 2007	January 12, 2009	April 28, 2009
Historical volatility (%)	50.00	52.62	46.77	50.99
Weighted average share price on grant date (₱)	18.70	62.00	51.00	74.00
Risk-free interest rate (%)	10.28	4.67	5.60	5.77
Expected life of option (years)	3.17	3.17	3.22	3.43

In July 2009, the *BOD* ratified the resolution of the *BOA* of the *ESPP* to shorten the vesting period of the 13th offering from three years to two years. This resulted in the acceleration of the recognition of the cost of the grant. Total expense arising from the share-based payment plan amounted to ₱174 million in 2010, ₱301 million in 2009 and ₱116 million in 2008.

See *Note 29 – Expenses and Income*.

21. Interest-bearing Long-term Financial Liabilities

This account consists of the following:

	2010	2009
	(Amounts in Millions)	
Long-term portion of interest-bearing financial liabilities:		
Long-term debt	**₱15,498**	₱16,909
Redeemable preferred stock	**–**	325
	15,498	17,234
Current portion of interest-bearing financial liabilities:		
Long-term debt	**3,654**	2,285
Redeemable preferred stock	**1,920**	1,784
	5,574	4,069
	₱21,072	₱21,303

The current portion of redeemable preferred shares includes shares which have matured and have been called for redemption by the *Company* totaling ₱1,318 million and ₱1,149 million as at December 31, 2010 and 2009, respectively. Interest is no longer accrued on the preferred shares, which has been called for redemption.

The details of interest-bearing financial liabilities are as follows:

Description	**2010**	2009
	(Amounts in Millions)	
Peso-denominated Debt		
Parent Company		
₱5.0 Billion Fixed Rate Note Facility Agreement	**₱5,000**	₱–
₱4.8 Billion Fixed Rate Note Facility Agreement	**4,800**	–
₱5.0 Billion Note Facility Agreement	**2,443**	2,715
₱3.0 Billion Term Loan Facility	**2,400**	3,000
₱5.5 Billion Note Facility Agreement:		
Fixed rate notes	**1,600**	1,600
Floating rate notes	**–**	3,900
₱12.0 Billion Note Facility Agreement* -		
Fixed rate notes	**–**	5,127
Loans payable to government entities in quarterly installments	**–**	1
Rockwell Land		
₱2.0 Billion Note Facility Agreement	**1,579**	1,860
Bridge Facilities and Term Loan	**1,444**	1,060

Description	2010	2009
	(Amounts in Millions)	
Euro-denominated Debt		
Parent Company		
Availment under the Master Credit Agreement payable in equal semi-annual installments	**₱–**	₱35
CHF-denominated Debt		
Parent Company		
Availment under the Master Credit Agreement payable in equal semi-annual installments	**–**	19
Total long-term debt	**19,266**	19,317
Less unamortized debt issue costs	**114**	123
	19,152	19,194
Redeemable Preferred Stock	**1,920**	2,109
	21,072	21,303
Less portion maturing within one year	**5,574**	4,069
Long-term portion of interest-bearing financial liabilities	**₱15,498**	₱17,234

** Includes value of embedded call option in 2009. See Note 31 – Financial Assets and Liabilities.*

The scheduled maturities of the *Company*'s outstanding long-term debt at nominal values as at December 31, 2010 and 2009 are as follows:

December 31, 2010

Year	Peso Debt
	(Amounts in Millions)
2011	**₱3,654**
2012	**1,126**
2013	**1,000**
2014	**3,958**
2015	**97**
After 2015	**9,431**
Total	**₱19,266**

As at December 31, 2010, all of the interest-bearing long-term financial liabilities are denominated in Philippine peso.

December 31, 2009

		Euro Debt		Swiss Franc Debt		
Year	Peso Debt	In €	In ₱	In CHF	In ₱	Total
			(Amounts in Millions)			
2010	₱2,230	€0.54	₱35	CHF0.44	₱19	₱2,284
2011	2,233	–	–	–	–	2,233
2012	1,779	–	–	–	–	1,779
2013	4,902	–	–	–	–	4,902
2014	4,718	–	–	–	–	4,718
After 2014	3,315	–	–	–	–	3,315
Total	₱19,177	€0.54	₱35	CHF0.44	₱19	₱19,231

Peso-denominated Debt

₱5.0 Billion Fixed Rate Note Facility Agreement

In December 2010, *MERALCO* entered into a Note Facility Agreement for the issuance of ₱23 million, 5-year fixed rate notes with maturity 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 at maturity while the 5.5-year fixed rate notes are payable in annual installments of 1% of the original principal amount from 2011 to 2015 with the remaining balance payable in 2016.

₱4.8 Billion Fixed Rate Note Facility Agreement

In November 2010, *MERALCO* signed a Fixed Rate Note Facility Agreement for the issuance of ₱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. The 7-year fixed rate notes are payable in annual installments of 0.5% of the original amount from 2011 to 2016 with the remaining balance payable in 2017. The 10-year fixed rate notes are payable in annual installments of 0.5% of the original amount from 2011 to 2019 with the remaining balance payable in 2020.

₱5.0 Billion Note Facility Agreement

In January 2009, *MERALCO* entered into a Note Facility Agreement for the issuance of ₱2,715 million fixed rate notes with final maturity in January 2014 and ₱2,285 million floating rate due in January 2010. The floating rate notes were prepaid in October 2009 while the fixed rate notes are payable in annual installments of 10% of the original principal amount from 2010 to 2013 with the remaining balance payable in 2014.

₱3.0 Billion Term Loan Facility

The ₱3,000 million, 5-year bilateral term loan agreement with Unionbank of the Philippines is due in October 2014.

₱5.5 Billion Note Facility Agreement

On December 9, 2009, *MERALCO* signed a ₱5,500 million Note Facility Agreement for the issuance of fixed and floating rate notes. The ₱1,600 million fixed rate notes mature in 2014 while the ₱3,900 million floating rate notes mature in 2015. The fixed rate notes are payable at maturity while the floating rate notes are payable in annual installments of 3% of the original principal amount from 2010 to 2014 with the remaining balance payable in 2015. In December 2010, the *Parent Company* prepaid the floating rate notes without penalty.

₱12.0 Billion Note Facility Agreement

The ₱12,000 million Note Facility Agreement consists of ₱6,000 million fixed-rate notes and ₱6,000 million floating rate corporate notes. The proceeds were utilized to prepay all of the *Parent Company*'s secured loans. In December 2009, the *Parent Company* prepaid the balance of its floating rate notes. The fixed rate notes are payable in 24 quarterly installments until December 2013 inclusive of a one-year grace period. The amortization schedule is back-ended with the first 20 quarterly installments representing 2% of the original principal amount while the last four quarterly installments represent 15% of the original principal amount.

The fixed rate note has an embedded call option (prepayment option), which gives the *Parent Company* the right to redeem all or a part of any of the outstanding notes at an amount equivalent to 105% of the outstanding principal amount on any interest payment starting at the end of the second year from issue date. The *Parent Company* prepaid the balance of its fixed rate note in December 2010.

₱2.0 Billion Note Facility Agreement

The ₱2.0 billion fixed rate corporate notes were drawn by *Rockwell Land* from a consortium of local banks and were used to finance the development of the *BPO* buildings located in the *MERALCO* compound. The notes consist of two tranches at ₱1,000 million each, ₱1,400 million of which is payable in 20 quarterly installments starting August 2009 and the balance of ₱600 million is due in August 2014.

On February 2, 2011, *Rockwell Land* also took a bridge loan from a local bank and preterminated the facility agreement. Accordingly, such loan was classified as current liability in the 2010 consolidated statement of financial position.

See *Note 11 – Investment Properties.*

Peso Bridge Facilities and Term Loan

As at December 31, 2010, *Rockwell Land*'s loans from various banks and financial institutions consist of bridge facilities payable in 2011 and a term loan payable in December 2014.

Euro-denominated Debt

The €3.764 million loan was drawn under the Master Credit Agreement with a foreign financial institution to finance the supply and installation of a 115 kV gas-insulated substation at the Central Business Park. The loan was fully paid in November 2010.

CHF-denominated Debt

The CHF3.055 million loan was drawn under the Master Credit Agreement with a foreign financial institution to finance the supply and installation of another 115 kV gas-insulated substation at the Central Business Park. The loan was fully paid in November 2010.

Fixed Rate Loans

Principal Amount	Interest Rate	Maturity Date	**2010**	2009
			(Amounts in Millions)	
₱5.0 Billion Fixed Rate Note Facility Agreement				
5.5-year notes	interpolated 5.5-year *PDST-F** plus spread	2016	**₱4,977**	₱–
5-year notes	5-year *PDST-F** plus spread	2015	**23**	–
₱4.8 Billion Fixed Rate Note Facility Agreement				
7-year notes	7-year *PDST-F** plus spread	2017	**1,997**	–
10-year notes	10-year *PDST-F** plus spread	2020	**2,803**	
₱5.0 Billion Note Facility Agreement	5-year *PDST-F** plus spread	2014	**2,443**	2,715
₱5.5 Billion Note Facility Agreement	5-year *PDST-F** plus spread	2014	**1,600**	1,600
₱12.0 Billion Note Facility Agreement	9%	2013**	**–**	5,127
₱2.0 Billion Notes	8.8%	2014	**1,579**	1,860
€3.764 Million Availment under the Master Credit Agreement	5.56%	2010	**–**	35
₱200 Million Term Loan	7.2632%	2010	**–**	149
₱150 Million Term Loan	8.5%	2014	**123**	148
₱100 Million Term Loan	8.5%	2014	**84**	**–**
Loans payable to government entities	3.5%	2011	**–**	1
Total			**₱15,629**	₱11,635

* *Philippine Dealing System Treasury Fixing or PDST-F*
** *The Company prepaid the outstanding balance in December 2010.*

Floating Rate Loans

Principal Amount	Interest Rate	Maturity Date	**2010**	2009
			(Amounts in Millions)	
₱3.0 Billion Term Loan	6-month *PDST-F* plus spread	2014	**₱2,400**	₱3,000
₱5.5 Billion Note Facility Agreement	3-month *PDST-F* plus spread	2015*	**–**	3,900
Bridge Facilities and Term Loan	1-year *PDST-F* plus spread, 3-month *PDST-F* plus spread in 2009 and 3-month *PDST-F* plus spread;1-year *PDST-F* plus spread		**1,237**	763
CHF3.055 Million Availment under the Master Credit Agreement	6-month CHF LIBOR plus spread	2010	**–**	19
Total			**₱3,637**	₱7,682

* *The Company prepaid the outstanding balance in December 2010.*

The average annual interest rates for the loans as at December 31, 2010 are as follows:

	Fixed Rate Note	Floating Rate Note
Parent Company	4.00% to 8.79%	4.60% to 5.88%
Rockwell Land	8.5% to 8.8%	4.2% to 7.01%

On December 21, 2010, the *Parent Company* signed a 7-year, ₱2,500 million floating rate Term Loan Agreement with a local bank. The loan was fully drawn on January 10, 2011. Interest rate is repriced every six months based on 6-month *PDST-F* plus a spread.

Debt Covenants and Security Arrangements

The *Parent Company*'s loan agreements require compliance with financial ratios such as debt service coverage of 1.2 times calculated at relevant measurement dates.

The *Parent Company*'s loan 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 of December 31, 2010, the *Parent Company* is in compliance with all covenants of the loan agreements.

The interest-bearing financial obligations of *Rockwell Land* are secured by the assignment of receivables from the sale of *One Rockwell* and *The Grove* units and Mortgage Participation Certificates on a Mortgage Trust Indenture and its amendments and supplements over the Rockwell Power Plant Mall.

Unamortized Debt Issuance Costs

Unamortized debt discount, representing debt issuance costs and any difference between the fair value of consideration given or received upon initial recognition, included in the financial liabilities amounted to ₱114 million and ₱123 million as at December 31, 2010 and 2009, respectively.

The following presents the changes to the unamortized debt issuance costs as at December 31, 2010 and 2009:

	Note	2010	2009
		(Amounts in Millions)	
Unamortized debt issuance costs at beginning of year		**₱123**	₱80
Additions during the year		**67**	97
Accretions during the year charged to interest and other financial charges	29	**(76)**	(54)
Unamortized debt issuance costs at end of year		**₱114**	₱123

Redeemable Preferred Stock

The movements, in terms of number of shares, of the *Company*'s redeemable preferred stock are as follows:

	2010	2009
Balance at beginning of year	**210,928,655**	266,364,384
Redemptions	**(18,964,630)**	(55,435,729)
Balance at end of year	**191,964,025**	210,928,655

The original "Terms and Conditions" of *MERALCO*'s Special Stock Subscription Agreement, which require an applicant to subscribe to preferred stock with 10% dividend to cover the cost of such extension or new distribution facilities, has been amended by the *Magna Carta* and the *DSOAR* effective July 19, 2004 and January 18, 2006, respectively. The amendment sets forth the issuance of preferred stock, only if such instrument is available.

The following table details the total quarterly dividends paid at 10% per annum to preferred shareholders in 2010 and 2009:

Record Date	Payment Date	Amount
		(In Millions)
March 22, 2010	April 30, 2010	₱13
June 28, 2010	July 30, 2010	12
September 27, 2010	October 29, 2010	12
December 29, 2010	January, 29 2011	11
March 31, 2009	April 30, 2009	37
June 30, 2009	July 31, 2009	35
September 30, 2009	October 30, 2009	33
December 31, 2009	January 29, 2010	14

22. **Customers' Deposits**

This account consists of:

	2010			2009		
	Current Portion (see Note 26)	**Long-term Portion**	**Total**	Current Portion (see Note 26)	Long-term Portion	Total
			(Amounts in Millions)			
Meter deposits:						
Principal	**₱1,226**	**₱–**	**₱1,226**	₱744	₱645	₱1,389
Accrued interest	**1,175**	**–**	**1,175**	628	644	1,272
Bill deposits:						
Principal	**541**	**16,675**	**17,216**	518	15,256	15,774
Accrued interest	**137**	**7,086**	**7,223**	167	8,518	8,685
	₱3,079	**₱23,761**	**₱26,840**	₱2,057	₱25,063	₱27,120

Meter Deposits

Meter deposit is intended to guarantee the cost of meter 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.

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 to be completed not later than 66 months from the effectivity of the said *Rules* on July 5, 2008. Under the terms of the Resolution No. 8, Series of 2008, a customer has the option of receiving his refund through cash, credit to future monthly billings, or as an offset to other due and demandable claims of the private utility 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.

Interests due on meter deposits are calculated at 6% or 10% depending on when such deposits were paid.

On August 8, 2008, in compliance with *ERC* Resolution No. 8, the *Parent Company* submitted to the *ERC* an accounting of the total meter deposit principal amount for refund which was at ₱1,507 million as at June 30, 2008. The actual refund of meter deposits commenced on November 3, 2008.

As at December 31, 2010 and 2009, the *Parent Company* has refunded ₱546 million (inclusive of ₱274 million in interests) and ₱251 million (inclusive of ₱123 million in interests), respectively.

Bill Deposits

Bill deposit serves to guarantee payment of bills by a customer, which based on existing regulation is to equal the value of one month's consumption or bill of the customer.

As required under the *Magna Carta* and *DSOAR*, residential and non-residential customers, respectively, 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 apply for the full refund of the bill deposit, together with the accrued interests, anytime thereafter, prior to the termination of his service. Otherwise, bill deposits and accrued interests shall be refunded within one month from termination of service, provided all bills have been paid and identification requirements have been complied with.

A series of exchanges was initiated by *MERALCO* with the Energy Regulatory Board or *ERB* and its successor organization, *ERC* to seek clarification with respect to the interest rate applicable to the bill deposits of the customers as well as the effectivity dates.

Up to March 31, 2010, the interest rate on bill deposits collected from residential and non-residential customers ranged from 1% to 10% depending on the contract effectivity date. The *ERC,* on February 22, 2010, promulgated the amended *DSOAR,* which became effective on April 1, 2010. Under such 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 approval of the *ERC.* Based on the foregoing, the interest rate effective April 1, 2010 through December 31, 2010 was 0.75% per annum.

The following are the movements of bill deposits account:

	December 31, 2010		
	Deposits	**Interest**	**Total**
Balance as at January 1	**₱15,774**	**₱8,685**	**₱24,459**
Additions	**1,857**	**–**	**1,857**
Reversals	**–**	**(1,326)**	**(1,326)**
Payments	**(415)**	**(136)**	**(551)**
Balance as at December 31	**17,216**	**7,223**	**24,439**
Less portion maturing within one year	**541**	**137**	**678**
Long-term portion of bill deposits and interest	**₱16,675**	**₱7,086**	**₱23,761**

	December 31, 2009		
	Deposits	Interest	Total
Balance as at January 1	₱14,448	₱7,733	₱22,181
Additions	1,713	1,119	2,832
Payments	(387)	(167)	(554)
Balance as at December 31	15,774	8,685	24,459
Less portion maturing within one year	518	167	685
Long-term portion of bill deposits and interest	₱15,256	₱8,518	₱23,774

23. Provisions

Provisions consist of amounts provided for legal and regulatory claims, as well as probable losses and possible refunds on for transmission charge over-recoveries, among others.

Movements in 2010 and 2009 are as follows:

	2010			2009		
	Claims	**Losses and Refunds**	**Total**	Claims	Losses and Refunds	Total
			(Amounts in Millions)			
Balance at beginning of year	**₱4,978**	**₱2,514**	**₱7,492**	₱1,645	₱4,098	₱5,743
Provisions	**4,636**	**887**	**5,523**	3,351	3,333	6,684
Reversals	**–**	**–**	**–**	–	(4,917)	(4,917)
Settlements	**(140)**	**–**	**(140)**	(18)	–	(18)
Balance at end of year	**₱9,474**	**₱3,401**	**₱12,875**	₱4,978	₱2,514	₱7,492

See *Note 6 – Significant Accounting Judgments and Estimates* and *Note 33 – Contingencies*.

24. Customers' Refund

This account represents the balance of the unclaimed refund related to the *SC* decision promulgated on April 30, 2003:

	2010	2009
	(Amounts in Millions)	
Gross refund amounts:		
Phase I	**₱361**	₱335
Phase II	**321**	295
Phase III	**385**	181
Phase IV	**6,064**	8,561
	7,131	9,372
Less present value effect:		
Balance at beginning of year	**225**	780
Less interest accretion during the year	**225**	555
Balance at end of year	**–**	225
	₱7,131	₱9,147

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 covering the period February 1994 to April 2003. The refund was implemented in four phases up to December 2010 as follows:

a. Phase I, covered refunds to residential and general service customers who consumed 100 kWh or less of electricity as at April 2003 (or in their last complete month's bill for services whose contracts with the *Parent Company* have been terminated), from June 2003 to August 2003.

b. Phase II, covered refunds to residential and general service customers who consumed 101 to 300 kWh as at April 2003 (or in their last complete month's bill for services whose contracts with the *Parent Company* have been terminated), from September 2003 to February 2004.

c. Phase III, covered refunds to residential and general service customers who consumed more than 300 kWh of electricity as at April 2003, was implemented by the *Parent Company* over a period of 12 months starting January 2004.

d. Phase IV, covered refunds to commercial and industrial customers and all government accounts and other customers not covered by Phases I–III. There are two sub-phases for Phase IV, based on the kWh consumption, which were implemented by the *Parent Company* from July 2005 until December 2010.

Based on the *ERC* order, the *Parent Company* shall complete payment of all refund claims by December 31, 2010. In an order dated February 7, 2011, the *ERC* approved the *Parent Company*'s proposal for the extension of the *SC* refund process for five years up to December 31, 2015, in view of difficulties encountered by (i) the customers in meeting the necessary documentation requirements for approval and payment of the refund and (ii) the *Parent Company* in contacting or locating customers entitled to the refund.

25. Notes Payable

Notes payable represent unsecured, peso-denominated, interest-bearing working capital loans obtained from various local financial institutions maturing within a year or less. Annual interest rates ranged from 8.5% to 11% in 2010 and 4.00% to 9.50% in 2009.

Interest expense on notes payable amounted to ₱26 million, ₱170 million and ₱595 million in 2010, 2009 and 2008, respectively. See *Note 29 – Expenses and Income*.

26. Trade Payables and Accrued Expenses

This account consists of the following:

	Note	**2010**	2009
		(Amounts in Millions)	
Trade accounts payable	*27*	**₱15,538**	₱16,943
Output *VAT* - net		**2,435**	2,238
Accrued expenses:			
Taxes		**1,387**	770
Interest	*21*	**487**	430
Liability for *GSL* payout		**446**	124
Current portions of:			
Meter deposits	*22*	**1,226**	744
Interest on meter deposits	*22*	**1,175**	628
Bill deposits	*22*	**541**	518
Security deposit		**192**	191
Interest on bill deposits	*22*	**137**	167
Deferred lease income		**27**	62
Retentions payable		**23**	96
Derivative liability	*31*	**1**	28
CERA I and II overrecoveries and carrying charges		**–**	983
Liability arising from deferred pass-through fuel costs	*12*	**–**	433
Dividends payable on:			
Common stock	*19*	**1,672**	26
Redeemable preferred stock		**284**	288
Accrued employee benefits		**1,300**	739
Advances for construction		**774**	163
Accrued development costs		**525**	276
Regulatory fees		**318**	199
Reinsurance liability		**225**	122
Accrued universal charges		**219**	425
Excess collections over recognized receivables		**185**	–
Transmission backbillings		**131**	132
Government grants		**106**	35
Other current liabilities		**1,784**	1,501
		₱31,138	₱28,261

Trade Accounts Payable

Trade accounts payable mainly represent obligations to power suppliers, namely, *NPC*, *NGCP* (effective January 15, 2009), *TransCo* (for transmission costs up to January 14, 2009) Philippine Electricity Market Corporation or *PEMC*, *FGPC* and *FGP*, Quezon Power (Philippines) Limited Company or *QPPL*, Philippine Power Development Corporation and Montalban Methane Power Corporation or *MMPC* for costs of power purchased. In addition, this account includes liabilities due to local and foreign suppliers for purchase of goods and services, which are mainly transformers, poles, operating materials and supplies, and contracted services.

As at December 31, 2009, the *Parent Company*'s obligation to *NPC* (assigned to Power Sector Assets and Liabilities Management Corporation or *PSALM*) of ₱5,712 million was included in a ₱64 million garnishment issued by the Municipal Trial Court of Pili, Camarines Sur on December 16, 2009 in favor of the Estate of Susano J. Rodriguez. Separately, on December 23, 2009, another order of garnishment in favor of *NPC* Drivers and Mechanics Association, et. al., amounting to ₱38 million was issued by the *SC*. Thus, as at December 31, 2009, the *Parent Company* was legally prevented from paying its obligation to *NPC*. Such balance was paid in January 2010.

Trade payables are noninterest-bearing and are generally settled within the 15 to 60-day terms. Other payables are noninterest-bearing and are due in no more than six months from incurrence.

See *Note 27 – Related Party Transactions* and *Note 34 - Significant Contracts and Commitments.*

CERA I and II

The amounts of *CERA* I and II refunds pertain to over-recoveries of foreign exchange adjustments related to foreign currency-denominated debt outstanding from June 2003 to December 2006. The related foreign currency-denominated loans were substantially settled in 2006.

MERALCO began to refund such over-recoveries amounting to ₱3,092 million plus carrying charge of ₱833 million, at the rate of ₱0.1461 per kWh. The refund was implemented since March 2009 and shall continue until such time that the full amount shall have been fully refunded.

As at December 31, 2010, there was an over-refund of ₱30 million while the outstanding balance as at December 31, 2009 is ₱983 million, inclusive of ₱209 million in carrying charges. The refund was completed in April 2010.

Transmission Backbillings

This account pertains to the amount refundable to customers related to *ERC*'s decision on the revision of the minimum charge provision in the *Parent Company*'s rate schedules. This revision, which involves a change in the basis of the computation of the transmission charge component of the minimum charge, resulted in a liability to customers estimated at ₱1,085 million. *MERALCO* implemented the refund based on an *ERC* order beginning 2006.

As at December 31, 2010 and 2009, the outstanding liability amounted to ₱131 million and ₱132 million, respectively.

Advances for Construction

Article 14 of the *Magna Carta*, specifically, "Right to Extension of Lines and Facilities" requires customers requesting for an extension of lines and facilities beyond 30-meter serving distance from the nearest voltage facilities of the *DU* to advance the cost of the project. Up to March 31, 2010 such advances from customers were being refunded at the rate of 25% of the distribution revenue generated from the extension lines and facilities until such amounts are fully refunded or five years, whichever is shorter. The customer advances are noninterest-bearing. The related asset forms part of the *Company*'s rate base only at the time a refund has been paid out.

The amended *DSOAR*, which became effective April 1, 2010 increased the refund rate from 25% to 75% of the gross distribution revenue generated from the extension lines and facilities until such amounts are fully refunded.

As at December 31, 2010 and 2009, the noncurrent portion of advances for construction of ₱3,271 million and ₱2,989 million, respectively, is presented as "Advances for construction- net of current portion" account in the consolidated statement of financial position.

27. **Related Party Transactions**

The following provides the total amount of transactions, which have been provided and/or contracted by the *Company* with related parties for the relevant financial year. The outstanding balances are unsecured, interest-free (except those relating to deferred pass-through fuel costs) and settled in cash. There have been no guarantees provided or received for any receivables from or payables to related parties. See *Note 12 – Deferred Pass-Through Fuel Costs* and *Note 34 - Significant Contracts and Commitments* for the related discussions.

PPA with FGPC and FGP

MERALCO has distinct *PPAs* with *FGPC* and *FGP* for the purchase of 7,271 million kWh from the Sta. Rita Power Plant and 3,635 million kWh of power from the San Lorenzo Power Plant, respectively. Total power purchased from *FGCP* and *FGP* amounted to ₱53,322 million, ₱48,519 million and ₱55,283 million for the years ended December 31, 2010, 2009, and 2008, respectively. As at December 31, 2010 and 2009, outstanding accounts payable to *FGPC* and *FGP* under the *PPA* amounted to ₱2,038 million and ₱2,909 million, respectively.

Pole Attachment Contracts with PLDT

The *Parent Company* has a Pole Attachment Contract with *PLDT* for a period of three year up to December 31, 2011. *PLDT* facilities shall be attached to their designated pole space in accordance with the standards similar to other pole attachment contracts set forth by *MERALCO*. Under the Pole Attachment Contract, *PLDT* shall use the contacted cable position exclusively for its telecommunication cable network facilities.

For the year ended December 31, 2010, total fees billed under this contract amounted to ₱199 million and ₱67 million for the period July 14, 2009 (date at which PLDT has effective ownership interests in *MERALCO*) to December 31, 2009. As at December 31, 2010 and 2009, outstanding receivable of the *Parent Company* from *PLDT* under this contract amounted to less than a million and ₱126 million, respectively.

Sale of Electricity under Various Service Contracts

Several offices, service branches, manufacturing facilities of *the Company's* shareholders and affiliates are located within the franchise area of *MERALCO*. Thus, *MERALCO* sells electricity to such shareholders and affiliates. The rates charged to related parties are the same *ERC*-mandated rates charged to all unrelated customers within the franchise area.

Total revenues billed to its shareholders, *PLDT*, *MPIC*, *SMC* and *First Holdings* and their respective subsidiaries are as follows:

	2010	2009
	(Amounts in Millions)	
PLDT	**₱2,104**	₱719*
MPIC	**518**	105**
SMC	**1,026**	1,004***
First Holdings	**295**	81***
	₱3,943	₱1,909

** For the period July 14, 2009 to December 31, 2009.*
*** For the period October 2, 2009 to December 31, 2009.*
**** For the period January 1 to December 31, 2009.*

Purchase of Telecommunication Services from PLDT and Subsidiaries

The *Company*'s primary telecommunications carriers are *PLDT* for its wireline and *SMART* for its wireless services. Such services are covered by distinct service contracts between the telecommunications carriers and each legal entity within the *MERALCO* group.

The total amount of services purchased by the *Parent Company* from *PLDT* and *SMART* for the period ended December 31, 2010 and for the period July 14, 2009 (date at which *PLDT* has effective ownership interests in *MERALCO*) to December 31, 2009 is as follows:

	2010	2009
	(Amounts in Millions)	
PLDT and affiliates	**₱53**	₱33
SMART	**8**	6
	₱61	₱39

Purchase of Goods and Services

In the ordinary course of business, the *Company* purchases goods and services from its affiliates and sells power to such affiliates. The details of the transactions are as follows:

Related Party	Relationship	Nature of Transaction	Year	Purchases	Amount Owed by Related Party	Amount Owed to Related Party
				(Amounts in Millions)		
GEPMICI	Associate	Purchase of meters and devices	**2010**	**₱52**	**₱–**	**₱–**
			2009	194	–	–
Indra Philippines	Associate	IT solutions provider	**2010**	**510**	**5**	**13**
			2009	571	6	15
Philippine Electric Corporation	Affiliate	Purchase of power transformers	**2010**	**1,070**	**–**	**25**
			2009	957	–	24

Compensation of Key Management Personnel of the Company

The compensation of key officers of the *Company* by benefit type is as follows:

	2010	2009	2008
		(Amounts in Millions)	
Short-term employee benefits	**₱376**	₱312	₱275
Long-term and retirement benefits	**133**	66	71
Share-based payments	**14**	11	25
Total compensation paid to key management personnel	**₱523**	₱389	₱371

Each of the directors is entitled to a director's fee of ₱120,000 for every *BOD* meeting attended. Each of the members or advisors of the Audit and Risk Management, Compensation and Benefits, Finance, Governance and Nomination Committees is entitled to a fee of ₱20,000 for every committee meeting attended.

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 retirement and pension plans.

28. Revenues and Purchased Power

Electricity Revenue

Electricity revenues account for 97% of the total revenues both in 2010 and in 2009 and 98% in 2008. Following is a breakdown of electricity revenues:

	2010	2009	2008
		(Amounts in Millions)	
Pass-through charges:			
Generation charge	**₱159,292**	₱106,695	₱120,445
Transmission charge	**25,429**	23,250	25,511
System loss charge	**11,567**	16,108	16,139
Power Act reduction	**(219)**	(660)	(814)
Inter-class, lifeline subsidies and others	**(634)**	1,600	(488)
Wheeling charges:			
Distribution charges	**29,518**	21,276	17,594
Supply charge	**8,705**	6,560	5,753
Metering charge	**5,506**	3,923	2,923
	239,164	178,752	187,063
Less intersegment sales	**87**	66	64
	₱239,077	₱178,686	₱186,999

Distribution revenue accounted for 18% of total revenues in 2010 and 2009 and 14% in 2008.

See *Note 7 – Segment Information*

Purchased Power

Actual purchased power costs are pass-through costs and revenue-neutral to the *Parent Company*. The details are as follows:

	2010	2009	2008
		(Amounts in Millions)	
Generation charge	**₱172,946**	₱127,116	₱131,863
Transmission charge	**27,970**	23,812	25,009
	₱200,916	₱150,928	₱156,872

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*. These amounted to ₱19,960 million, ₱20,900 million and ₱21,592 million in 2010, 2009 and 2008, respectively, and are presented as part of "Purchased power" account in the consolidated statements of income. This also includes the allowable system loss charge up to 8.5% in 2010 and 9.5% in 2009 and 2008. In 2010, 2009 and 2008, the *Parent Company*'s actual *SL* rates were 7.9%, 8.6% and 9.3%, respectively.

The details of purchased power follow:

	2010	2009	2008
		(Amounts in Millions)	
FGPC and *FGP*	**₱53,322**	₱48,519	₱55,283
NPC/PSALM (including NPC successor generating companies)	**65,170**	51,807	49,406
WESM/PEMC	**39,140**	11,284	13,083
TransCo/NGCP	**27,970**	23,812	25,009
QPPL	**15,238**	15,477	14,072
Others	**76**	29	19
	₱200,916	₱150,928	₱156,872

29. Expenses and Income

Operations and Maintenance

	Note	2010	2009	2008
			(Amounts in Millions)	
Salaries, wages and employee benefits	*20, 27 and 30*	**₱8,843**	₱7,866	₱7,279
Contractors' services		**3,975**	3,626	3,283
Provision for doubtful accounts, net of recoveries	*15*	**982**	886	1,566
Transportation and travel		**354**	398	272
Materials and supplies		**433**	326	338
Corporate expenses		**297**	302	306
Supervision and regulatory fees		**88**	55	52
Others		**739**	152	255
		₱15,711	₱13,611	₱13,351

Cost of Services

	2010	2009	2008
		(Amounts in Millions)	
Salaries, wages and employee benefits	**₱783**	₱708	₱584
Contractors' cost	**496**	661	517
Materials and supplies	**428**	171	163
Others	**289**	263	192
	₱1,996	₱1,803	₱1,456

Salaries, Wages and Employee Benefits

	Note	2010	2009	2008
			(Amounts in Millions)	
Operations and maintenance:				
Salaries and wages		**₱5,748**	₱5,198	₱4,809
Net pension costs	*30*	**1,767**	1,887	1,890
Health, medical and related benefits		**755**	267	176
Employee share-based payments	*20*	**174**	301	116
Other long-term employee benefits	*30*	**285**	109	184
Social security costs		**114**	104	104
Cost of services -				
Salaries, wages and employee benefits		**783**	708	584
		₱9,626	₱8,574	₱7,863

Interest and Other Financial Charges

	Note	2010	2009	2008
			(Amounts in Millions)	
Interest expense on interest-bearing long-term financial liabilities, net of interest capitalized	*21*	**₱1,333**	₱1,366	₱1,237
Interest expense on bill deposits	*22*	**(1,326)**	1,120	925
Carrying charge on *ERC*-approved over-recoveries	*2*	**108**	543	934
Interest expense on notes payable	*25*	**26**	170	595
Interest expense on meter deposits	*22*	**76**	81	89
Amortization of:				
Debt issue costs	*21*	**76**	54	18
Loan premium	*21*	**(24)**	(27)	(27)
Interest expense on deferred pass-through fuel costs		**9**	15	141
Others		**215**	6	223
		₱493	₱3,328	₱4,135

Interest and Other Financial Income

	Note	**2010**	2009	2008
			(Amounts in Millions)	
Carrying costs on *ERC*-approved under-recoveries	*2*	**₱723**	₱2,782	₱813
Interest income on placements		**536**	413	321
Amortization of unearned interest on installment trade receivables		**551**	293	450
Gain on return of investment		**355**	–	–
MTM gains (losses) from derivative instruments	*31*	**3**	82	(167)
Loss on disposal of investment		**–**	(46)	–
Others		**522**	722	1,502
		₱2,690	₱4,246	₱2,919

30. **Long-term Employee Benefits**

Accrued long-term employee benefits consist of the following:

	2010	2009
	(Amounts in Millions)	
Pension asset (included in "Other noncurrent assets" account)	**(₱50)**	(₱66)
Long-term employee benefits:		
Pension liability	**₱8,227**	₱10,301
Long-term incentives	**400**	–
Other long-term employee benefits	**920**	686
	₱9,547	₱10,987

Retirement Plan

The features of the *Company*'s defined benefit plans are discussed in *Note 5 – Summary of Significant Accounting Policies.*

Actuarial valuations are prepared annually by independent actuaries.

Net Pension Costs (included in "Operations and maintenance expenses - Salaries, wages and employee benefits" account)

	2010			
	Parent	**Rockwell Land**	**MIESCOR Group and Other Subsidiaries**	**Total**
		(Amounts in Millions)		
Interest costs	**₱2,006**	**₱12**	**₱5**	**₱2,023**
Current service costs	**865**	**14**	**4**	**883**
Expected return on plan assets	**(1,132)**	**(17)**	**(1)**	**(1,150)**
Past service costs	**1**	**7**	**–**	**8**
Actuarial loss	**–**	**–**	**2**	**2**
Net pension costs	**₱1,740**	**₱16**	**₱10**	**₱1,766**
Actual return on plan assets	**₱4,178**	**₱44**	**₱–**	**₱4,222**

	2009			
	Parent	Rockwell Land	MIESCOR Group and Other Subsidiaries	Total
		(Amounts in Millions)		
Interest costs	₱2,033	₱6	₱4	₱2,043
Current service costs	793	5	2	800
Expected return on plan assets	(722)	(4)	(1)	(727)
Past service costs	1	17	–	18
Actuarial loss (gain)	–	(1)	5	4
Settlement gain	(252)	–	–	(252)
Net pension costs	₱1,853	₱23	₱10	₱1,886
Actual return on plan assets	₱4,127	₱21	₱2	₱4,150

	2008			
	Parent	Rockwell Land	MIESCOR Group and Other Subsidiaries	Total
	(Amounts in Millions)			
Interest costs	₱1,730	₱6	₱4	₱1,740
Current service costs	964	9	3	976
Expected return on plan assets	(826)	(4)	(1)	(831)
Past service costs	1	1	–	2
Actuarial loss	–	–	2	2
Net pension costs	₱1,869	₱12	₱8	₱1,889
Actual return (loss) on plan assets	(₱1,695)	(₱6)	₱1	(₱1,700)

Pension Liability (Asset)

	2010			
	Parent	**Rockwell Land**	**MIESCOR Group and Other Subsidiaries**	**Total**
	(Amounts in Millions)			
Defined benefit obligation	**₱32,483**	**₱168**	**₱77**	**₱32,728**
Fair value of plan assets	**(22,775)**	**(208)**	**(21)**	**(23,004)**
Unrecognized net actuarial gains (losses)	**(1,505)**	**13**	**(29)**	**(1,521)**
Unrecognized past service costs	**(3)**	**(23)**	**–**	**(26)**
Pension liability (asset)	**₱8,200**	**(₱50)**	**₱27**	**₱8,177**

	2009			
	Parent	Rockwell Land	MIESCOR Group and Other Subsidiaries	Total
	(Amounts in Millions)			
Defined benefit obligation	₱25,067	₱126	₱62	₱25,255
Fair value of plan assets	(16,166)	(164)	(18)	(16,348)
Unrecognized net actuarial gains (losses)	1,380	2	(20)	1,362
Unrecognized past service cost	(4)	(30)	–	(34)
Pension liability (asset)	₱10,277	(₱66)	₱24	₱10,235

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

	2010			
	Parent	**Rockwell Land**	**MIESCOR Group and other Subsidiaries**	**Total**
	(Amounts in Millions)			
Defined benefit obligation at beginning of year	**₱25,067**	**₱126**	**₱62**	**₱25,255**
Interest costs	**2,006**	**12**	**5**	**2,023**
Current service costs	**865**	**14**	**4**	**883**
Benefits paid	**(1,386)**	–	**(4)**	**(1,390)**
Past service costs				
Actuarial losses (gains) due to:				
Changes in assumptions	**6,385**	**15**	**8**	**6,408**
Experience adjustments	**(454)**	**1**	**2**	**(451)**
Defined benefit obligation at end of year	**₱32,483**	**₱168**	**₱77**	**₱32,728**

	2009			
	Parent	Rockwell Land	MIESCOR Group and Other Subsidiaries	Total
		(Amounts in Millions)		
Defined benefit obligation at beginning of year	₱22,594	₱50	₱50	₱22,694
Interest costs	2,033	6	4	2,043
Current service costs	793	5	2	800
Benefits paid	(1,282)	–	(4)	(1,286)
Past service costs	–	40	–	40
Actuarial losses (gains) due to:				
Changes in assumptions	2,051	18	2	2,071
Experience adjustments	(482)	7	8	(467)
Effect of settlement	(640)	–	–	(640)
Defined benefit obligation at end of year	₱25,067	₱126	₱62	₱25,255

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

	2010			
	Parent	**Rockwell Land**	**MIESCOR Group and Other Subsidiaries**	**Total**
		(Amounts in Millions)		
Fair value of plan assets at beginning of year	**₱16,166**	**₱164**	**₱18**	**₱16,348**
Expected return on plan assets	**1,132**	**17**	**1**	**1,150**
Actuarial gains (losses)	**3,046**	**27**	**(1)**	**3,072**
Benefits paid	**(1,386)**	**–**	**–**	**(1,386)**
Contributions by employer	**3,817**	**–**	**3**	**3,820**
Fair value of plan assets at end of year	**₱22,775**	**₱208**	**₱21**	**₱23,004**

	2009			
	Parent	Rockwell Land	MIESCOR Group and Other Subsidiaries	Total
		(Amounts in Millions)		
Fair value of plan assets at beginning of year	₱10,309	₱82	₱17	₱10,408
Expected return on plan assets	722	4	1	727
Actuarial gains	3,405	17	1	3,423
Benefits paid	(1,705)	–	(4)	(1,709)
Contributions by employer	3,435	61	3	3,499
Fair value of plan assets at end of year	₱16,166	₱164	₱18	₱16,348

The *Parent Company* expects to contribute ₱3,045 million to its defined benefit pension plan in 2011.

The major categories of plan assets of the *MERALCO* Pension Fund as a percentage of the fair value of total plan assets are as follows:

	2010	2009
	(In Percentage)	
Marketable equity securities	**39**	94
Government securities	**26**	–
Cash and cash equivalents	**16**	–
Bonds and commercial notes	**14**	1
Real properties	**4**	5
Receivables	**1**	–
	100	100

Marketable equity securities, government securities, bonds and commercial notes are investments held by the trustee banks. The Pension Fund does not have any direct interests in the Company's shares.

The overall expected rate of return on assets is determined based on the prevailing rates of return on equity and fixed income securities applicable to the period over which the obligation is to be settled.

The key information of the retirement plan is as follows:

	For the years ended				
	2010	2009	2008	2007	2006
	(Amounts in Millions)				
Present value of defined benefit obligation	**₱32,728**	₱25,255	₱22,694	₱24,825	₱27,473
Fair value of plan assets	**(23,004)**	(16,348)	(10,408)	(11,857)	(5,967)
Excess of present value of defined benefit obligation over fair value of plan assets	**9,724**	8,907	12,286	12,968	21,506
Experience losses (gains) on plan liabilities	**(451)**	(467)	165	(748)	233
Experience gains (losses) on plan assets	**(3,072)**	3,423	(2,531)	5,518	3,176

Other Long-term Employee Benefits (included as part of "Operations and maintenance expenses - Salaries, wages and employee benefits" account)

	2010	2009	2008
	(Amounts in Millions)		
Interest costs	**₱151**	₱78	₱92
Current service costs	**34**	43	33
Actuarial loss	**100**	36	59
Settlement gain	**–**	(48)	–
Net other long-term employee benefits	**₱285**	₱109	₱184

Other Long-term Employee Benefits Liability

	2010	2009
	(Amounts in Millions)	
Other long-term employee benefits obligation	**₱2,471**	₱1,887
Unrecognized net actuarial losses	**(1,551)**	(1,201)
Benefits liability at end of year	**₱920**	₱686

Changes in the present value of other long-term employee benefits liability are as follows:

	2010	2009
	(Amounts in Millions)	
Balance at beginning of year	**₱1,887**	₱1,115
Actuarial losses	**450**	835
Interest costs	**151**	78
Current service costs	**34**	43
Benefits paid	**(51)**	(51)
Effect of settlement	**–**	(133)
Balance at end of year	**₱2,471**	₱1,887

The principal assumptions used as at January 1, 2010, 2009 and 2008 in determining pension and other long-term employee benefits obligations are shown below:

	2010	2009	2008
Annual discount rate	**6%–8%**	8%–9.2%	7%–10.2%
Expected annual rate of return on assets	**7%–10%**	6%–10%	7%
Future range of annual salary increases	**5%–9.6%**	5%–10%	5%–10%

Defined Contribution Plan or Provident Fund

In addition to its defined benefit retirement plan, *MIESCOR* has a contributory defined contribution retirement plan. The annual contribution of *MIESCOR* to the Provident Fund is equivalent to 6% of the current monthly basic salaries of covered employees. The Provident Fund is maintained primarily for the purpose of establishing periodically the amounts of the benefits pertaining to the covered employees and is managed by a Board of Trustees. The employees' shares are represented by the units of the Provident Fund. Each unit is determined by dividing the net asset value of the Provident Fund by the aggregate number of units earned by the employee. Although the plan is a defined contribution, *MIESCOR* regularly monitors compliance with *RA* 7641, otherwise known as "The Retirement Pay Law." As at December 31, 2010 and 2009, *MIESCOR* is in compliance with the requirements of *RA* 7641.

Pension expense under this plan amounted to ₱1 million in 2010, 2009 and 2008.

The investment portfolio of such defined contribution plan seeks to achieve regular income and consistent long-term capital growth over its own portfolio benchmark. In order to attain this objective, the trustee's mandate is to invest in a diversified portfolio of bonds and equities, primarily domestic instruments. The portfolio mix is kept at 75% to 100% for debt and fixed income securities while 0% to 25% is allotted to equity securities.

As at December 31, 2010 and 2009, the investment portfolio consists of bonds and commercial notes. There are no equity instruments held. *MIESCOR* expects to contribute ₱2 million to the defined benefit plan in 2011.

Consolidated Pension Benefit Costs

	2010	2009
	(Amounts in Millions)	
Expense recognized for defined benefit plans	**₱1,766**	₱1,886
Expense recognized for defined contribution plan	**1**	1
Consolidated pension benefit costs	**₱1,767**	₱1,887

Long-term Incentive Plan or LTIP

On October 22, 2010, the *BOD* approved the *Parent Company*'s *LTIP* for selected executives with at least the rank of superintendent. The plan hinges on the achievement of a certain level of consolidated core net income determined on an aggregate basis for the three year period ending December 31, 2012. Executives invited to the plan have to serve a minimum uninterrupted period to be entitled to any pay-out under the plan.

31. Financial Assets and Liabilities

The *Company*'s principal financial liabilities, other than derivatives, consist of bank loans, including redeemable preferred shares and, trade and non-trade payables. The main purpose of such financial liabilities is to finance operations. Financial assets consist of and cash and cash equivalents and, trade and non-trade receivables, which arise directly from operations. Accounting policies related to financial assets and liabilities are set out in *Note 5 – Summary of Significant Accounting Policies*.

The following table sets forth the financial and nonfinancial assets and liabilities as at December 31, 2010 and 2009:

	Loans and Receivables	Held-to-maturity Investments	Designated at Fair Value through Profit or Loss	Held-for-trading	Available-for-sale Financial Assets	Liabilities Carried at Amortized Cost	Total Financial Assets and Liabilities	Non-financial Assets and liabilities	Total
					(Amounts in Millions)				
Assets as at December 31, 2010									
Noncurrent									
Utility plant and others - net	₱–	₱–	₱–	₱–	₱–	₱–	₱–	₱101,009	₱101,009
Construction in progress	–	–	–	–	–	–	–	2,241	2,241
Investment in associates and a joint venture	–	–	–	–	–	–	–	321	321
Investment properties - net	–	–	–	–	–	–	–	8,037	8,037
Deferred pass-through fuel costs	–	–	–	–	–	–	–	1,222	1,222
Deferred tax assets - net	–	–	–	–	–	–	–	42	42
Other noncurrent assets	4,163	61	–	–	403	–	4,627	5,712	10,339
Current									
Cash and cash equivalents	24,370	–	–	–	–	–	24,370	–	24,370
Trade and other receivables - net	25,609	–	–	–	–	–	25,609	–	25,609
Inventories	–	–	–	–	–	–	–	2,043	2,043
Land and development costs	–	–	–	–	–	–	–	1,708	1,708
Other current assets	–	–	24	–	–	–	24	2,003	2,027
Total assets	54,142	61	24	–	403	–	54,630	124,338	178,968
Liabilities as at December 31, 2010									
Noncurrent									
Interest-bearing long-term financial liabilities - net of current portion	–	–	–	–	–	15,498	15,498	–	15,498
Customers' deposits - net of current portion	–	–	–	–	–	23,761	23,761	–	23,761
Deposits from condominium units sold	–	–	–	–	–	–	–	741	741
Deferred tax liabilities - net	–	–	–	–	–	–	–	3,322	3,322
Long-term employee benefits	–	–	–	–	–	–	–	9,547	9,547
Provisions	–	–	–	–	–	–	–	12,875	12,875
Advances for construction	–	–	–	–	–	3,271	3,271	–	3,271
Other noncurrent liabilities	–	–	–	–	–	1,777	1,777	575	2,352
Current									
Notes payable	–	–	–	–	–	149	149	–	149
Trade payables and accrued expenses	–	–	1	–	–	23,913	23,914	7,224	31,138
Income tax payable	–	–	–	–	–	–	–	413	413
Customers' refund	–	–	–	–	–	7,131	7,131	–	7,131
Interest-bearing long-term financial liabilities - current portion	–	–	–	–	–	5,574	5,574	–	5,574
Total liabilities	–	–	1	–	–	81,074	81,075	34,697	115,772
Net Assets (Liabilities)	₱54,142	₱61	₱23	₱–	₱403	(₱81,074)	(₱26,445)	₱89,641	₱63,196

	Loans and Receivables	Held-to-maturity Investments	Designated at Fair Value through Profit or Loss	Held-for-trading	Available-for-sale Financial Assets	Liabilities Carried at Amortized Cost	Total Financial Assets and Liabilities	Non-financial Assets and liabilities	Total
				(Amounts in Millions)					
Assets as at December 31, 2009									
Noncurrent									
Utility plant and others - net	₱–	₱–	₱–	₱–	₱–	₱–	₱–	₱98,231	₱98,231
Construction in progress	–	–	–	–	–	–	–	3,627	3,627
Investment in associates and a joint venture	–	–	–	–	–	–	–	1,203	1,203
Investment properties - net	–	–	–	–	–	–	–	8,021	8,021
Deferred pass-through fuel costs	–	–	–	–	–	–	–	3,161	3,161
Deferred tax assets - net	–	–	–	–	–	–	–	17	17
Other noncurrent assets	6,404	57	172	–	361	–	6,994	6,190	13,184
Current									
Cash and cash equivalents	17,068	–	–	–	–	–	17,068	–	17,068
Trade and other receivables - net	21,600	–	–	–	–	–	21,600	–	21,600
Inventories	–	–	–	–	–	–	–	1,857	1,857
Land and development costs	–	–	–		–	–	–	1,191	1,191
Other current assets	–	–	11	–	–	–	11	2,958	2,969
Total assets	45,072	57	183	–	361	–	45,673	126,456	172,129
Liabilities as at December 31, 2009									
Noncurrent									
Interest-bearing long-term financial liabilities - net of current portion	–	–	–	–	–	17,234	17,234	–	17,234
Customers' deposits - net of current portion	–	–	–	–	–	25,063	25,063	–	25,063
Deposits from condominium units sold	–	–	–		–	–	–	343	343
Deferred tax liabilities - net	–	–	–	–	–	–	–	4,230	4,230
Long-term employee benefits	–	–	–	–	–	–	–	10,987	10,987
Provisions	–	–	–	–	–	–	–	7,492	7,492
Advances for construction - net of current portion	–	–	–	–	–	2,989	2,989	–	2,989
Other noncurrent liabilities	–	–	–	–	–	–	–	522	522
Current									
Notes payable	–	–	–	–	–	513	513	–	513
Trade payables and accrued expenses	–	–	28	–	–	22,888	22,916	5,345	28,261
Income tax payable	–	–	–	–	–	–	–	133	133
Customers' refund	–	–	–	–	–	9,147	9,147	–	9,147
Interest-bearing long-term financial liabilities - current portion	–	–	–	–	–	4,069	4,069	–	4,069
Total liabilities	–	–	28	–	–	81,903	81,931	29,052	110,983
Net Assets (Liabilities)	₱45,072	₱57	₱155	₱–	₱361	(₱81,903)	(₱36,258)	₱97,404	₱61,146

The following table sets forth the consolidated carrying values and estimated fair values of the *Company*'s financial assets and liabilities recognized as at December 31, 2010 and 2009:

	Carrying Value		**Fair Value**	
	2010	2009	**2010**	2009
		(Amounts in Millions)		
Noncurrent Financial Assets				
AFS financial assets:				
Quoted equity securities	**₱381**	₱339	**₱381**	₱339
Unquoted equity securities	**22**	22	**22**	22
Other noncurrent assets:				
Unbilled receivables	**3,063**	5,406	**3,063**	5,406
SC GRAM case refund	**780**	780	**780**	780
Advance payment to suppliers	**253**	135	**253**	135
Installment contract receivable	**39**	54	**39**	54
Derivative assets	**–**	172	**–**	172
HTM	**61**	57	**61**	57
Notes receivable	**28**	29	**28**	29
Total noncurrent financial assets	**4,627**	6,994	**4,627**	6,994
Current Financial Assets				
Cash and cash equivalents:				
Cash on hand and in banks	**3,631**	6,399	**3,631**	6,399
Temporary cash placements	**20,739**	10,669	**20,739**	10,669
Trade and other receivables - net:				
Billed electricity	**16,258**	13,274	**16,258**	13,274
Unbilled electricity	**5,011**	5,537	**5,011**	5,537
Current portion of installment contracts	**2,183**	367	**2,183**	367
Service contracts and others	**1,326**	1,278	**1,326**	1,278
Nontrade - others	**831**	1,144	**831**	1,144
Other current assets -				
Derivative assets	**24**	11	**24**	11
Total current financial assets	**50,003**	38,679	**50,003**	38,679
Total Financial Assets	**₱54,630**	₱45,673	**₱54,630**	₱45,673

	Carrying Value		Fair Value	
	2010	2009	**2010**	2009
	(Amounts in Millions)			
Noncurrent Financial Liabilities				
Interest-bearing long-term financial liabilities:	**₱15,498**	₱17,234	**₱15,498**	₱17,574
Customers' deposits - net of current portion	**23,761**	25,063	**23,761**	25,063
Advances for construction	**3,271**	2,989	**3,271**	3,022
Other noncurrent liabilities	**1,777**	–	**1,777**	–
Total noncurrent financial liabilities	**44,307**	45,286	**44,307**	45,659
Current Financial Liabilities				
Trade payables and accrued expenses:				
Trade accounts payable	**15,538**	16,943	**15,538**	16,943
Accrued expenses:				
Interest	**487**	430	**487**	430
Liability for *GSL* payout	**446**	124	**446**	124
Current portion of:				
CERA I and II over-recoveries and carrying charges	–	983	–	983
Meter deposits	**1,226**	744	**1,226**	744
Interest on meter deposits	**1,175**	628	**1,175**	628
Bill deposits	**541**	518	**541**	518
Liability arising from deferred pass-through fuel costs	–	433	–	433
Security deposits	**192**	191	**192**	191
Interest on bill deposits	**137**	167	**137**	167
Retentions payable	**23**	96	**23**	96
Derivative liability	**1**	28	**1**	28
Dividends payable	**1,956**	314	**1,956**	314
Advances for construction	**774**	163	**774**	163
Accrued development costs	**525**	276	**525**	276
Regulatory fees	**318**	199	**318**	199
Reinsurance liabilities	**225**	122	**225**	122
Accrued universal charges	**219**	425	**219**	425
Transmission backbillings	**131**	132	**131**	132
Customers' refund - current portion	**7,131**	9,147	**7,131**	9,147
Interest-bearing financial liabilities:				
Notes payable	**149**	513	**149**	513
Current portion of long-term debt	**5,574**	4,069	**5,574**	4,069
Total current financial liabilities	**36,768**	36,645	**36,768**	36,645
Total Financial Liabilities	**₱81,075**	₱81,931	**₱81,075**	₱82,304

The fair value of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. 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 – Billed, Unbilled, Service Contracts and Others and Nontrade, Refundable Deposits, Trade payables and accrued expenses, Notes Payable and Liability Arising from Deferred Pass-Through Fuel Costs

Due to the short-term nature of transactions, the fair values of these instruments approximate their carrying amounts as at reporting date. The value of "Trade payables and accrued expenses" includes the value of bifurcated embedded currency forwards.

Installment Contracts Receivable

The fair values of installment contracts receivable were calculated by discounting the expected future cash flows at prevailing credit adjusted *PDEx* interest rates ranging from 1.08% to 6.59% in 2010 and 6.5% to 8.3% in 2009.

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.

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.

Bifurcated Call Option

The fair values of the embedded prepayment option were estimated based on prices derived using the binomial pricing model. The following inputs were used to determine the fair value of the bifurcated call option; contractual future cash flows, exercise price of ₱105, interest rate volatility of 26.29%, interest rate spot curves ranging from 6.28% to 8.12% in 2009. The related interest-bearing long-term financial liabilities were prepaid in December 2010.

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.

Interest-bearing Long-term Financial Liabilities

The fair values of interest bearing long-term financial liabilities were computed by discounting the expected future cash flows using the prevailing credit adjusted USD London interbank offered rate or *USD LIBOR*, Philippine Dealing System Treasury Fixing or *PDST-F*, *CHF LIBOR* and Euro interbank offered rates or *EURIBOR* ranging from 1.08% to 6.59% in 2010 and 4.68% to 7.30% in 2009. There were no foreign currency denominated long-term financial liabilities in 2010.

Bill Deposits

The fair values of bill deposits are not determinable since the timing of each refund is linked to the termination of service, which is not reasonably predictable. Bill deposits are presented at cost.

Preferred Stock

The carrying cost of the preferred stock represents the fair value. Except with respect to ₱192 million of such preferred stocks, which are callable and redeemable as at December 31, 2010, the remaining balance of preferred stock have been called and are redeemable anytime upon presentation by such shareholder of their certification. Preferred stock is presented at cost. This is included under “Interest-bearing long-term financial liabilities” account.

Retention Payable and Security Deposits

The fair values were calculated by discounting the expected future cash flows at prevailing credit adjusted *PDEx* interest rates ranging from 1.08% to 6.6% in 2010 and 6.3% to 7.4% in 2009.

Fair Value Hierarchy

The *Parent Company* held the following financial instruments measured at fair value. The *Parent Company* uses the following hierarchy for 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 for all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques with inputs which 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 liabilities carried at fair value that are classified using a fair value hierarchy:

	December 31, 2010			December 31, 2009		
	Level 1	**Level 2**	**Total**	Level 1	Level 2	Total
			(Amounts in millions)			
Noncurrent financial assets:						
AFS investments	**₱275**	**₱128**	**₱403**	₱–	₱361	₱361
Derivative assets	**–**	**–**	**–**	–	11	11
Current financial assets -						
Derivative assets	**–**	**24**	**24**	–	172	172
Total	**₱275**	**₱152**	**₱427**	₱–	₱544	₱544
Current financial liability -						
Derivative liability	**₱–**	**(₱1)**	**(₱1)**	₱–	(₱28)	(₱28)

As at December 31, 2010 and 2009, the *Company* does not have financial instruments with fair values determined using inputs that are not based on observable market data (Level 3).

For the years ended December 31, 2010 and 2009, 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.

Derivative Financial Instruments

Embedded Currency Forward

The *Parent Company* has bifurcated embedded currency forwards noted in various purchases and service agreements denominated in currencies other than Philippine peso, which includes U.S. dollar, Euro, among others. As at December 31, 2010 and 2009, these agreements represent 25% and 15% of the *Parent Company*'s trade payables, respectively. As at December 31, 2010, the U.S. dollar- and Euro-denominated agreements amounted to $9 million (equivalent to ₱404 million) and €8 million (equivalent to ₱450 million), respectively. As at December 31, 2009, the U.S dollar and Euro-denominated agreements amounted to $12 million (equivalent to ₱572 million) and €4 million (equivalent to ₱259 million), respectively. These are part of "Trade payables and accrued expenses" account in the consolidated statements of financial position. The net fair value of the embedded currency forward amounted to ₱22 million asset and ₱13 million liability as at December 31, 2010 and 2009, respectively.

Currency Forward

Rockwell Land entered into deliverable currency forward contracts to hedge its foreign currency exposure arising from its U.S. dollar-denominated receivables. As at December 31, 2010 and 2009, the *Company* has outstanding currency forward contracts to sell U.S. dollar with an aggregate notional amount of $0.09 million and $2.4 million, respectively, and weighted average contracted forward rate of ₱43.88 to $1.00 and ₱46.21 to $1.00, respectively. Outstanding derivatives will mature in 2011. The net fair value gain on the outstanding currency forward contracts amounted to ₱10 million as of December 31, 2010 and 2009.

Embedded Call Option

As discussed in Note 21, the *Parent Company* has an embedded call option (prepayment option) in its ₱6,000 million 9% Tranche A Fixed rate corporate note issued in December 2006. In December 2010, the call option on the ₱6,000 million fixed rate corporate note was exercised by the *Parent Company*. As at December 31, 2009, the fair value of this derivative amounted ₱172 million.

The net movements in fair value changes of the *Company*'s derivative instruments for the year ended December 31, 2010 and 2009 are as follows:

	2010	2009
	(Amounts in Millions)	
Balance at beginning of year	**₱155**	₱72
Net changes in fair value of derivatives not designated as accounting hedges	**3**	82
Fair value of settled instruments	**(135)**	1
Balance at end of year	**₱23**	₱155

The fair value changes of the *Company*'s derivative instruments as of December 31, 2010 and 2009 are presented as follows:

	Note	**2010**	2009
		(Amounts in Millions)	
Derivative assets:			
Current portion	*18*	**₱24**	₱11
Noncurrent portion	*13*	**–**	172
Derivative liabilities - current	*26*	**(1)**	(28)
		₱23	₱155

Financial Risk Management Objectives and Policies

The main risks arising from the *Company*'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:

Cash Flow Interest Rate Risk

The *Company*'s exposure to the changes in market interest rates relates primarily to the *Company*'s debt obligations with floating interest rates since the *Company*'s interest-bearing short-term investments mature within 90 days or less.

The *Company*'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. As at December 31, 2010 and 2009, approximately 85% and 61% of the *Company*'s borrowings are at a fixed rate of interest, respectively.

Rockwell Land's policy is to source loans with fixed interest rates whenever available.

The following table sets out the maturity profile of the *Company*'s financial instruments that are exposed to interest rate risk (exclusive of debt issuance costs):

	Within 1 Year	**1–2 Years**	**2–3 Years**	**3–4 Years**	**4–5 Years**	**More than 5 Years**	**Total**
			(Amounts in Millions)				
2010 Floating Rate							
Parent Company	**₱600**	**₱600**	**₱600**	**₱600**	**₱–**	**₱–**	**₱2,400**
Rockwell Land	**1,107**	**130**	**–**	**–**	**–**	**–**	**1,237**
2009 Floating Rate							
Parent Company	1,044	1,173	717	717	716	3,315	7,682
Rockwell Land	763	–	–	–	–	–	763

Interest on bank loans classified as floating rate is repriced at intervals of less than one year. The other financial liabilities of the *Company* that are not included in the foregoing have fixed interest rate, are noninterest-bearing or have no fixed or determinable maturity and are, therefore, not subject to cash flow interest rate risk. As previously mentioned, the *Company*'s short-term investments are not exposed to significant changes in market rates because they mature within 90 days or less to coincide with the *Company*'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 the *Parent Company's* and *Rockwell Land*'s profit before tax as at December 31, 2010 and 2009 (through the impact on floating rate borrowings). There is no other impact on the *Parent Company's* and *Rockwell Land*'s equity other than those already affecting the consolidated statement of income.

	2010		2009	
	Increase (Decrease) in Basis Points	**Effect on Profit before Tax**	Increase (Decrease) in Basis Points	Effect on Profit before Tax
		(Amounts in Millions)		
Parent Company				
Floating rate loans from various banks	**+100**	**(₱24 million)**	+100	(₱69 million)
	(100)	**24 million**	(100)	69 million
Rockwell Land				
Floating rate loans from various banks	**+100**	**(₱9 million)**	+100	(₱3 million)
	(100)	**9 million**	(100)	3 million

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 the management in the foregoing analysis.

Foreign Currency Risk

The revaluation of any of the *Company*'s foreign currency-denominated financial assets and 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 debt. While an insignificant percentage of the *Company*'s revenues and debt is denominated in U.S. dollars, a substantial portion of the *Company*'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 *Company*'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.

To manage foreign currency risks and stabilize cash flows, the *Parent Company* is allowed to recover foreign exchange losses on foreign currency-denominated loans through adjustments in customers' bills in accordance with *CERA* II.

The following table shows the consolidated foreign currency-denominated financial assets and liabilities as at December 31, 2010 and 2009, translated to Philippine peso at the following exchange rates:

	2010	2009
U.S. Dollar ($)	**₱43.84**	₱46.20
Euro (€)	**58.03**	66.67

	December 31, 2010		
	Foreign Currency		
	U.S. Dollar	**Euro**	**Peso Equivalent**
Financial assets:			
Cash and cash equivalents	**$9**	**€–**	**₱395**
Trade and other receivables	**5**	**–**	**219**
Advance payments to suppliers	**7**	**–**	**307**
	21	**–**	**921**
Financial liabilities:			
Trade payables and accrued expenses	**(78)**	**–**	**(3,420)**
	(78)	**–**	**(3,420)**
	($57)	**(€–)**	**(₱2,499)**

	December 31, 2009		
	Foreign Currency		
	U.S. Dollar	Euro	Peso Equivalent
Financial assets:			
Cash and cash equivalents	$85	€–	₱3,936
Trade and other receivables	4	–	150
Advance payments to suppliers	3	–	138
	92	–	4,224
Financial liabilities:			
Trade payables and accrued expenses	(140)	(2)	(6,582)
Liability arising from deferred pass-through fuel costs	(9)	–	(433)
Interest-bearing long-term financial liabilities	–	(1)	(54)
	(149)	(3)	(7,069)
	($57)	(€3)	(₱2,845)

a. All of the *Parent Company*'s long-term financial liabilities are denominated in Philippine Peso. However, an insignificant portion of its trade payables are denominated in U.S. dollars. Thus, the impact of ₱1 movement of the Philippine Peso against the U.S. dollar will not have a significant impact on the *Parent Company*'s principal and interest payments. Further, *PBR* assumes a forecast level of foreign currency movements in its calculation of the forecasted regulatory asset base and expenditures. *PBR* also allows for adjustment of the rates the *Parent Company* charges under *PBR* should there be significant deviations in the foreign exchange forecast from what is actually realized.

b. *Rockwell Land* markets its developments in the United States. Thus, its statement of financial position may be affected significantly by movements in the U.S. dollar exchange rates.

   It is *Rockwell Land*'s policy to limit its U.S. dollar-denominated receivables to an amount that approximately matches the U.S. dollar-denominated component of its development costs as well as its U.S. dollar-denominated borrowings. Also, *Rockwell Land* enters into deliverable currency forward contracts to hedge its foreign currency exposure should there be an excess in U.S. dollar-denominated assets over the U.S. dollar-denominated liabilities.

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 *Company*'s profit before tax as at December 31, 2010 and 2009 (due to changes in the fair value of financial assets and liabilities). There is no other impact on the *Company*'s equity other than those already affecting the profit and loss.

	2010		2009	
	Change in US$ Rate	**Effect on Profit before Tax**	Change in US$ Rate	Effect on Profit before Tax
	(In %)	*(In Millions)*	*(In %)*	*(In Millions)*
U.S. dollar-denominated financial assets and liabilities	**+5**	**(₱125)**	+5	(₱140)
	–5	**125**	–5	140
Euro-denominated financial assets and liabilities	**+5**	**–**	+5	(9)
	–5	**–**	–5	9

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-U.S. dollar conversion rate using the year end balances of U.S. dollar-denominated cash and cash equivalents, accounts receivable, loans, 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. The *Company*'s exposure to price risk is minimal. The cost of fuel is part of the *Parent Company*'s and *CEDC's* generation cost that is recoverable from the customers through their generation charge.

Credit Risk

Credit risk is the risk that the *Company* will incur a loss arising from customers, clients or counterparties who fail to discharge their contracted obligations. The *Company* manages and controls credit risk by setting limits on the amount of risk that the *Company* is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

The *Company* trades only with recognized, creditworthy third parties. It is the *Company*'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. Power distribution receivables are, to a certain extent, backed by bill deposits. Also, as a policy, disconnection notices are sent three days after the due date and disconnections are carried out on the third day after receipt of disconnection notice.

Trade receivables from sale of condominium units are secured with pre-completed condominium units the legal title and ownership of which are transferred to the customers upon full payment of the contract price. Receivables from leases are secured by security deposits, while receivables from sale of club shares are guaranteed by the shares held by the *Company*.

With respect to placements of excess cash with financial institutions, these institutions are subject to the *Company*'s accreditation evaluation based on liquidity and solvency ratios and on the bank's credit rating. The *Company* shall transact only derivatives with similarly accredited financial institutions.

Credit risk arising from the other financial assets, which include cash and cash equivalents, trade and other receivables, *AFS* financial assets and certain derivative instruments, result from the *Company*'s exposure to credit risk and 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. The *Company*'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 *Company*.

The table below shows the maximum exposure to credit risk for the components of the consolidated statement of financial position, including derivatives. The maximum exposure is equivalent to the nominal amount of the accounts.

	Gross Maximum Exposure	
	2010	2009
Cash and cash equivalents:		
Cash on hand and in banks	**₱3,631**	₱6,399
Cash equivalents	**20,739**	10,669
Trade and other receivables:		
Billed	**16,258**	13,274
Unbilled	**5,011**	5,537
Current portion of installment contracts receivables	**2,183**	367
Service contracts and others	**1,326**	1,278
Other receivables	**831**	1,144
Other current assets -		
Derivative assets	**24**	11
Other noncurrent assets:		
AFS investments	**403**	361
Derivative assets	**–**	172
Unbilled receivables	**3,063**	5,406
SC GRAM case refund	**780**	780
Advance payment to suppliers	**253**	135
HTM	**61**	57
Installment contracts receivables	**39**	54
Notes receivable	**28**	29
	₱54,630	₱45,673

The credit quality of financial assets is managed by the *Parent Company* using “High Grade,” “Standard Grade” and “Sub-standard Grade” as internal credit ratings. The following tables show the credit quality by asset class:

	2010					
	Neither Past Due nor Impaired					
	High Grade	**Standard Grade**	**Sub-standard Grade**	**Past Due but not Impaired**	**Impaired Financial Assets**	**Total**
	(Amounts in Millions)					
Cash and cash equivalents	**₱22,504**	**₱–**	**₱–**	**₱–**	**₱–**	**₱22,504**
Trade and other receivables:						
Trade:						
Billed	**5,532**	**3,357**	**5,328**	**1,886**	**1,516**	**17,619**
Unbilled	**5,011**	**–**	**–**	**–**	**–**	**5,011**
Nontrade:						
Related parties	**1**	**3**	**12**	**304**	**–**	**320**
Others	**276**	**–**	**33**	**180**	**–**	**489**
AFS investments	**109**	**–**	**–**	**–**	**–**	**109**
Derivative assets	**23**	**–**	**–**	**–**	**–**	**23**
Other noncurrent assets	**–**	**–**	**4,121**	**–**	**–**	**4,121**
	₱33,456	**₱3,360**	**₱9,494**	**₱2,370**	**₱1,516**	**₱50,196**

	2009					
	Neither Past Due nor Impaired					
	High Grade	Standard Grade	Sub-standard Grade	Past Due but not Impaired	Impaired Financial Assets	Total
	(Amounts in Millions)					
Cash and cash equivalents	₱15,430	₱–	₱–	₱–	₱–	₱15,430
Trade and other receivables:						
Trade:						
Billed	3,676	2,835	4,547	2,100	2,088	15,246
Unbilled	–	5,537	–	–	–	5,537
Nontrade	372	–	236	233	50	891
Other current assets -					–	
Derivative assets	11	–	–	–	–	11
Other noncurrent assets:						
AFS investments	98	–	–	–	–	98
Derivative assets	172	–	–	–	–	172
Unbilled receivables	–	6,186	–	–	–	6,186
	₱19,759	₱14,558	₱4,783	₱2,333	₱2,138	₱43,571

Credit ratings are determined as follows:

- "High Grade"

  This includes cash and cash equivalents, derivative assets and *AFS* investments to counterparties with good credit rating or bank standing, thus credit risk is minimal. This normally includes large prime financial institutions, companies and government agencies. For trade receivables, this consists 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"

  This includes *AFS* investments that are not classified as "High Grade." For trade receivables, these consist of current month's billings (less than 30 days) that are expected to be collected before expiry date (10 to 14 days after billed date).

- "Sub-standard Grade"

  This includes trade receivables that consist of current month's billings, which are not expected to be collected within 60 days.

The credit quality of financial assets of *Rockwell Land is managed* using an internal credit ratings method. The table below shows the credit quality by class of asset as at December 31:

		2010	
	A Rating	**B Rating**	**Total**
		(Amounts in Millions)	
Cash and cash equivalents	**₱321**	**₱–**	**₱321**
Trade receivables from:			
Sale of condominium units	**919**	**467**	**1,386**
Leases	**65**	**–**	**65**
Advances to officers and employees	**7**	**–**	**7**
Other receivables	**50**	**–**	**50**
AFS investments	**278**	**–**	**278**
	₱1,640	**₱467**	**₱2,107**

		2009	
	A Rating	B Rating	Total
		(Amounts in Millions)	
Cash and cash equivalents	₱393	₱–	₱393
Trade receivables from:			
Installment contracts	175	140	315
Leases	60	7	67
Advances to officers and employees	9	–	9
Other receivables	17	–	17
AFS investments	245	–	245
	₱899	₱147	₱1,046

For trade receivables from sale of condominium units, customers who have no history of delayed payment are classified as having an "A" credit rating while customers who have history of delayed payment but is currently updated are given a "B" credit rating.

Trade receivables from leases are classified as having a credit rating of "A" when tenants pay within the discount period and "B" when tenants pay on or before due date.

The following table shows the aging analysis of financial assets of the *Company* as at December 31:

	2010					
	Neither Past Due nor Impaired	**Past Due But Not Impaired**			**Impaired Financial Assets**	**Total**
		31–Days	**61–Days**	**Over 90 I**		
	(Amounts in Millions)					
Cash and cash equivalents:						
Cash on hand and in banks	**₱3,631**	**₱–**	**₱–**	**₱–**	**₱–**	**₱3,631**
Cash equivalents	**20,739**	**–**	**–**	**–**	**–**	**20,739**
Trade and other receivables:						
Trade:						
Billed electricity	**14,353**	**1,303**	**393**	**209**	**1,518**	**17,776**
Unbilled electricity	**5,011**	**–**	**–**	**–**	**–**	**5,011**
Current portion of installment contracts receivables	**1,385**	**525**	**46**	**227**	**–**	**2,183**
Service contracts and others	**848**	**95**	**48**	**163**	**172**	**1,326**
Nontrade receivables	**434**	**118**	**37**	**414**	**11**	**1,014**
Other current assets -						
Derivative assets	**24**	**–**	**–**	**–**	**–**	**24**
Other noncurrent assets:						
Unbilled receivables	**3,063**	**–**	**–**	**–**	**–**	**3,063**
SC GRAM case refund	**780**	**–**	**–**	**–**	**–**	**780**
AFS investments	**403**	**–**	**–**	**–**	**–**	**403**
Advance payment to suppliers	**253**	**–**	**–**	**–**	**–**	**253**
HTM	**61**	**–**	**–**	**–**	**–**	**61**
Installment contracts receivable	**39**	**–**	**–**	**–**	**–**	**39**
Derivative assets	**–**	**–**	**–**	**–**	**–**	**–**
Others	**28**	**–**	**–**	**–**	**–**	**28**
	₱51,052	**₱2,041**	**₱524**	**₱1,013**	**₱1,701**	**₱56,331**

	2009					
	Neither Past Due nor Impaired	Past Due But Not Impaired			Impaired Financial Assets	Total
		31–Days	61–Days	Over 90 I		
	(Amounts in Millions)					
Cash and cash equivalents:						
Cash on hand and in banks	₱6,399	₱–	₱–	₱–	₱–	₱6,399
Cash equivalents	10,669	–	–	–	–	10,669
Trade and other receivables:						
Trade:						
Billed electricity	11,165	–	1,064	1,045	2,088	15,362
Unbilled electricity	5,537	–	–	–	–	5,537
Current portion of installment contracts receivables	262	62	15	28	–	367
Service contracts and others	1,144	78	18	38	–	1,278
Nontrade receivables	902	2	4	236	234	1,378
Other current assets -						
Derivative assets	11	–	–	–	–	11
Other noncurrent assets:						
Unbilled receivables	5,406	–	–	–	–	5,406
SC GRAM case refund	780	–	–	–	–	780
AFS investments	361	–	–	–	–	361
Derivative assets	172	–	–	–	–	172
Advance payment to suppliers	135	–	–	–	–	135
HTM	57	–	–	–	–	57
Installment contracts receivable	54	–	–	–	–	54
Notes receivable	29	–	–	–	–	29
	₱43,083	₱142	₱1,101	₱1,347	₱2,322	₱47,995

Liquidity Risk

Liquidity risk is the risk that the *Company* will be unable to meet its payment obligations when they fall due. The *Company* manages this risk through monitoring of cash flows in consideration of future payment of obligations and the collection of its trade receivables. The *Company* also ensures that there are sufficient, available and approved working capital lines that it can draw from at any time.

The *Company* maintains an adequate amount of cash and cash placements in the event of unforeseen interruption of its cash collections and if available, government securities. The *Company* also maintains accounts with several relationship banks to avoid significant concentration of cash with one institution.

The following table sets out the maturity profile of the *Company*'s financial liabilities based on contractual undiscounted payments:

	2010				
	Less than 3 Months	**3–12 Months**	**1–5 Years**	**More than 5 Years**	**Total**
	(Amounts in Millions)				
Notes payable	**₱149**	**₱–**	**₱–**	**₱–**	**₱149**
Trade payables and accrued expenses	**20,563**	**1,193**	**29**	**–**	**21,785**
Customers' refund	**1,787**	**5,344**	**–**	**–**	**7,131**
Interest-bearing long-term financial liabilities:					
Floating rate borrowings	**1,107**	**688**	**2,028**	**–**	**3,823**
Fixed rate borrowings	**2,077**	**762**	**7,226**	**10,682**	**20,747**
Preferred stock	**551**	**1,653**	**–**	**–**	**2,204**
Customers' deposits	**600**	**600**	**–**	**–**	**1,200**
Other noncurrent liabilities	**22**	**142**	**241**	**–**	**405**
Total undiscounted financial liabilities	**₱26,856**	**₱10,382**	**₱9,524**	**₱10,682**	**₱57,444**

	2009				
	Less than 3 Months	3–12 Months	1–5 Years	More than 5 Years	Total
	(Amounts in Millions)				
Notes payable	₱513	₱–	₱–	₱–	₱513
Trade payables and accrued expenses	23,602	495	32	–	24,129
Customers' refund	365	8,782	–	–	9,147
Interest-bearing long-term financial liabilities:					
Floating rate borrowings	104	1,366	4,968	3,668	10,106
Fixed rate borrowings	807	1,395	12,711	–	14,913
Preferred stock	–	1,784	325	–	2,109
Customers' deposits	350	1,188	26,595	–	28,133
Other noncurrent liabilities	–	–	3,180	–	3,180
Total undiscounted financial liabilities	₱25,741	₱15,010	₱47,811	₱3,668	₱92,230

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, the *Company* estimates that a portion of bill deposits (including related interest), amounting to ₱678 million, will be refunded in 2011. This is shown as part of "Trade payables and accrued expenses" account in the 2010 consolidated statement of financial position.

Capital Management

The primary objective of the *Company*'s capital management is to enhance shareholder value. It reviews its capital structure 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.

To do this, the *Company* manages its level of debt versus *EBITDA* ratio based on levels with comparable electric utilities.

The *Company* monitors capital using debt to *EBITDA* ratio, which is debt divided by *EBITDA*. The *Company* considers long-term debt, redeemable preferred stocks and notes payable as debt.

	2010	2009
	(Amounts in Millions, except Debt to EBITDA)	
Long-term debt	**₱19,152**	₱19,194
Redeemable preferred stocks	**1,920**	2,109
Notes payable	**149**	513
Debt (a)	**21,221**	21,816
EBITDA (b)	**18,452**	13,169
Debt to *EBITDA* (a/b)	**1.15**	1.66

32. **Income and Franchise Taxes**

Income Tax

The components of deferred tax assets (liabilities) as at December 31, 2010 and 2009 are as follows:

	Note	**2010**	2009
		(Amounts in Millions)	
Deferred tax assets:			
Unfunded pension cost and unamortized past service cost		**₱2,786**	₱3,685
Provision for various claims	*23*	**2,842**	991
Provision for probable losses from refund	*23*	**1,020**	1,257
Allowance for doubtful accounts		**464**	648
Allowance for nonrecovery of receivables		**334**	758
Allowance for excess of cost over net realizable value		**18**	19
Others		**526**	173
		7,990	7,531
Deferred tax liabilities:			
Revaluation increment in utility plant and others	*19*	**8,030**	8,242
Depreciation method differential		**1,337**	1,477
Capitalized interest		**858**	866
Capitalized duties and taxes deducted in advance		**708**	728
Net book value of capitalized/realized foreign exchange losses		**99**	109
Excess of effective interest rate amortization over straight-line amortization of debt issue costs		**(1)**	(1)
Present value of impact on customers' refund		**–**	68
Others		**239**	255
		11,270	11,744
		(₱3,280)	(₱4,213)

The deferred tax assets and liabilities are presented in the consolidated statements of financial position as follows:

	2010	2009
	(Amounts in Millions)	
Deferred tax assets - net	**₱42**	₱17
Deferred tax liabilities - net	**(3,322)**	(4,230)
	(₱3,280)	(₱4,213)

There is no income tax consequence for payment of dividends by the *Parent Company* to its shareholders, which are domestic corporations.

Provision for (benefit from) income tax consists of:

	2010	2009	2008
		(Amounts in Millions)	
Current	**₱5,233**	₱3,218	₱5,122
Deferred	**(913)**	(595)	(3,055)
	₱4,320	₱2,623	₱2,067

A reconciliation between the provision for (benefit from) income tax computed at statutory income tax rate using tax rates of 30% in 2010 and 2009 and 35% in 2008, and provision for (benefit from) income tax as shown in the consolidated statements of income is as follows:

	2010	2009	2008
		(Amounts in Millions)	
Income tax computed at statutory tax rates	**₱4,331**	₱2,695	₱1,820
Income tax effects of:			
Interest income subjected to lower final tax rate	**(183)**	(113)	(105)
Nondeductible interest expense	**61**	43	77
Equity in net earnings of associates and a joint venture	**(85)**	(73)	(70)
Nondeductible expenses	**79**	265	65
Nontaxable income	**(63)**	(54)	(4)
Others	**180**	(140)	284
	₱4,320	₱2,623	₱2,067

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 allowed both individual and corporate taxpayers to use *OSD* in computing their taxable income. For corporations, they may elect a standard deduction in an amount not exceeding 40% of gross income in lieu of the itemized allowed deduction. For the years ended December 31, 2010 and 2009, none of the entities in the *MERALCO Group* availed of the *OSD* in computing taxable income, except for *RSIC*.

The *Company*'s temporary difference for which deferred tax assets have not been recognized pertains to the allowance for doubtful accounts amounting ₱39 million and ₱41 million as at December 31, 2010 and 2009, respectively.

In 2009, *MCIT* amounting to ₱6 million was applied to current *RCIT* due.

Franchise Tax

Local Franchise Tax

Consistent with the Decisions of the *ERC* on Case Nos. 2001-646 and 2001-900, franchise tax is presented as a separate line item in the customers' bill and computed as a percentage of the sum of all charges, except taxes and the universal charge.

Further, the Implementing Rules and Regulations provide that franchise taxes shall be paid only on its distribution wheeling and captive market supply revenues. At present, pending the promulgation of guidelines from the Department of Finance, the *Parent Company* is paying local franchise tax based on the sum of the charges in the customers' bill, except on taxes and the universal charge.

33. **Contingencies**

Contingent Assets

Advances for Pass-Through Costs

As at December 31, 2010, *MERALCO* has contingent assets relating to unrecovered system loss charges of ₱805 million.

Up to May 2008, *MERALCO* referred to the "Guidelines for the Calculation of the Over-under- Recovery in the Implementation of the System Loss Rate by Distribution Utilities" issued by the *ERC* on November 23, 2005 to recover the system loss under-recoveries and began to bill customers for such under-recoveries beginning the February 2006 billing month. The guidelines allowed the recovery to be implemented over a period of 17 months or until such time that the amount has been collected. Following such guideline, a total of ₱284 million in unbilled system loss charges have been billed as at February 28, 2011. However, on June 4, 2008, the *ERC* decided and directed *MERALCO* to file a new application for the recovery of the system loss adjustments after the former has confirmed and approved the average transmission rate to be used in computing the system loss adjustment.

Overpayment of Income Tax related to SC Refund

As a result of the Decision of the *SC* for *MERALCO* to refund ₱0.167 per kWh to affected customers covering the 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. Hence, *MERALCO* filed a claim 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 on the ground that the period for filing a claim has prescribed.

The *BIR* then approved the refund of ₱894 million through issuance of tax credit certificates or *TCC*s, proportionate to the actual refund of claims to utility customers. The BIR initially issued TCC amounting to ₱317 million corresponding to actual refund to customers as at August 31, 2005.

As at December 31, 2010 and 2009, the amount of unissued *TCC*s of ₱577 million out of the ₱894 million refund entitlement is presented as part of “Other noncurrent assets” account in the consolidated statement of financial position.

MERALCO filed a Petition assailing the denial by the *BIR* of its tax refund claim of ₱5,796 million, net of ₱894 million, as approved by the *BIR* for taxable year 2001. In a *Decision* dated December 6, 2010, the Court of Tax Appeals 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. The said *Decision* is now subject of a Motion for Clarification and Partial Reconsideration filed by *MERALCO* and a Motion for Reconsideration filed by the *BIR*. Both motions are pending resolution as at February 28, 2011.

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 stemmed from 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. As at February 28, 2011, *Meralco* is in the process of filing its application for the issuance of the *TCC*.

Contingent Liabilities

Real Property Tax or RPT Assessments

Six local governments units or *LGUs* assessed *MERALCO* for deficiency real property taxes on certain assets of the *Parent Company.* The assets include any of electric poles, wires, insulators, and transformers, collectively referred to as *TWIP*. Of these *LGUs*, one has secured a favorable decision from the *CA*, whereby the appellate court directed the *LGU* concerned to present an assessment of the foregoing properties and collect the pertinent tax in accordance with the Local Government Code or *LGC* of 1991. Such Decision was further appealed to the *SC* where it is now submitted for resolution. With respect to the cases of the five other *LGUs*, these are pending with their respective administrative bodies or government offices.

Accordingly, *MERALCO* deemed it prudent to include in its third *RP* operating expenses, payment of *RPT* on its *TWIP* commencing *RY* 2011. The *Company*, however, continues to pursue its legal actions and avail of legal remedies with respect to the legality, validity and applicability of the assessments, and in the event, payment is warranted or appropriate, to recover any resulting real estate tax payments through separate application under Article 11 of the “Rules for Setting Distribution Wheeling Rates for Privately Owned Distribution Utilities Operating under Performance Based Regulation (First Entry Group: Third Regulatory Period).”

Local Franchise Tax Assessments

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, the management of *MERALCO* and its legal counsel believe that it has strong legal grounds to contest such assessments.

Income Tax Assessment on Taxable Year 1999

In line with the Decision of the *SC* ordering *MERALCO* to refund ₱0.167 per kWh to affected consumers for the period February 1994 to May 2002, *MERALCO* amended its tax return for taxable year 1999, which had then been served a Letter of Authority to examine its books by the *BIR*. The amended tax return for 1999 reflected an overpayment of ₱977 million, which was subsequently applied against the income tax liability for taxable year 2002. As discussed under "*Overpayment of Income Tax related to SC Refund*" section of this Note, a claim for refund has been filed for taxable years 2000 and 2001.

In February 2010, the *BIR* issued *MERALCO* a tax clearance, which included taxable year 1999.

Mediation with NPC

The *NPC* embarked into 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, to avoid a 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 *MERALCO* to enter into a long-term supply contract with *NPC.*

On November 21, 1994, *MERALCO* entered into a 10-year *CSE* with *NPC* to commence on January 1, 1995, the terms of the *CSE* and the rates charged to *MERALCO* of which approved by the *BOD* of *NPC* and the then *ERB*, respectively.

Separately, the *DOE* further asked *MERALCO*'s support and commitment to provide a market for half of the output of the Camago-Malampaya gas field, which was to generate significant revenues for the Philippine Government.

MERALCO's purchases from *NPC* exceeded the contract level in the first seven years of the *CSE*. However, the 1997 Asian crisis resulted in a significant dip in energy sales.

While the events were beyond the control of *MERALCO*, *NPC* refused to honor the *Parent Company*'s good faith notification. A dispute ensued and both parties agreed to go into mediation.

The mediation resulted in the signing of a *SA* conditioned on *ERC*'s approval on July 15, 2003. The *SA* was approved by the respective *BOD*s of *NPC* and *MERALCO*. The net settlement amount of ₱14.3 billion was agreed upon by *NPC* and *MERALCO* and manifested before the *ERC* through a Joint Compliance dated January 19, 2006.

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 the *Parent Company*." As a result, *MERALCO* separately sought judicial clarifications with RTC-Pasig. Pre-trials are ongoing. However, the *OSG* refused to participate in the pre-trial and opted to seek a Temporary Restraining Order or *TRO* from the *CA.*

In the event the *SA* is disapproved, *MERALCO* and *NPC* shall revert to their respective positions before the mediation, which shall be resolved through arbitration. On the other hand, a decision by the *RTC Pasig* shall mean that the agreement is valid although enforcement of the *SA* is dependent on the final approval by the *ERC*, which shall be the basis for the recognition of any liability or receivable.

Deferred PPA

On October 14, 2009, the *ERC* released its findings on the *Parent Company*'s implementation of the collection of the approved pass-through cost under-recoveries. According to the *ERC*, *MERALCO* over-recovered ₱268 million of deferred *PPA*, transmission line costs related to *QPPL* and deferred accounting adjustments, or *DAA* incurred in 2004. Consequently, it directed *MERALCO* to refund said amount 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 under-recovered deferred *PPA* of ₱106 million. As at December 31, 2010, *MERALCO* has filed a Motion for Reconsideration, which is pending decision of the *ERC.*

COA Audit

As discussed in *Note 2 – Rate Regulations,* the *SC*, in its Decision dated December 6, 2006 on the *MERALCO* Unbundling case, ruled that a *COA* audit was not a prerequisite for the determination of a utility's rates in connection with *MERALCO*'s rate unbundling case. While affirming the *ERC*'s authority on rate-fixing, the *SC* nevertheless directed the *ERC* to request the *COA* to conduct a complete audit of the books, records and accounts of *MERALCO.* Thus, in compliance with the *SC* directive , the *ERC* engaged the *COA* on January 15, 2007 to conduct an audit 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 *Parent Company* received a copy of the *ERC* Order related to Case No. 2001-900 RC, entitled "In the Matter of the Application for the Approval of the Unbundled Rates pursuant to the Provision of the Application for the Approval of the Unbundled Rates pursuant to the Provision of *RA* No. 9136, *MERALCO*, Applicant," which directed all intervenors in the case to submit within 15 days from receipt of their respective comments on the *COA*'s "Report No. 2009-01 Rate Audit Unbundled Charges."

The *Company* has already submitted its comment on the *COA* audit report. Similarly, the intervenors have filed their comments to the *COA* audit report and the *Company* has responded to the same. The *Company* is awaiting the action of the *ERC* on the *COA* Audit Report.

Others

Related provisions for items estimable amounted to ₱4,636 million, ₱3,351 million, ₱318 million in 2010, 2009 and 2008 respectively, gross of potential recoveries.

Management, together with its internal and external counsels, believes that the probable resolution of these issues will not materially affect the *Company*'s financial position and results of operations.

34. **Significant Contracts and Commitments**

NPC

Transition Supply Contract or TSC with NPC

MERALCO and *NPC* have a Transition Supply Contract or *TSC*, effective the shorter of five years from November 16, 2006 or one year after the introduction of open access, should open access 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 *GHW* up to 2011. The terms of the *TSC* include the following among others:

a. Billings for the contracted volume to be based on *NPC*'s time-of-use or *TOU* generation rate as approved by the *ERC*, plus certain mandated adjustments;

b. Submission of month-end and day-ahead nominations of energy quantities in kilowatt hours for committed purchase quantity;

c. Adjustments to the monthly contracted energy subject to certain conditions;

d. Conditions of and when *MERALCO* may source power from *NPC* in excess of the Contracted Energy responsibility of *NPC* to provide replacement power; and

e. Energy off-take in excess of the *TSC* quantities deemed to be taken.

While additional *TSC* volumes have been contracted , discussions between the *Parent Company* and *NPC* for the extension of the *TSC* are ongoing.

FGPC and FGP

MERALCO is committed to contract 1,500-*MW* of the 3,000-*MW* output of the Camago-Malampaya gas field, as directed by the Department of Energy.

Hence, the *Parent Company* entered into separate 25-year *PPA*s 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. The *PPA* with *FGPC* terminates on March 13, 2020, while that of *FGP* ends on January 8, 2022.

On January 7, 2004, *Meralco*, *FGP* and *FGPC* signed the Amendment to their respective *PPA*s. The negotiations resulted in a package of concessions including the assumption of *FGP* and *FGPC* of community taxes at current tax rate, while conditional concessions include 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 *PPA*s of *FGP* and *FGPC* were approved by the *ERC* on May 31, 2006.

Under the respective *PPA*s 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

The *Parent Company* 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 Power Purchase Contract is for a period of 25 years.

In the amended *PPA* signed on February 21, 2008, the amount billable by *QPPL* included a transmission line charge reduction in lieu of a previous rebate program. The Agreement also included an advance payment mechanism under which requires *Meralco* to pay QPPL $2.85 million per annum for ten years beginning 2008. Thereafter, *QPPL* shall return the same amount annually without adjustment for cost of money in equal annual payments. 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 the $2.85 million in that year. This advance Payment Mechanism was requested by *QPPL* to offset the difference between the transmission line charge specified in the *TLA* and the *ERC*-approved T/line charge in March 2003.

On December 16, 1997, *NPC*, *QPPL* and *Meralco* entered into a Substation Interconnection Agreement, similar to the one entered with *FGPC*.

TSCs with Privatized Generating Assets and IPP Contracts of NPC

From 2008 to 2009, *NPC* privatized a number of its generating assets and *IPP* contracts and the assets and contracts were taken over by 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. Following are the privatized plants and *IPP* contracts:

Year	Power Plant	Successor Owner	% Volume
2008	Masinloc coal-fired power plant	Masinloc Power Partners Co. Ltd. or *Masinloc Power*	14.8
2009	Tiwi-Makban geothermal power plants	Aboitiz Power Renewable, Inc. or *Aboitiz Power*	9.6
	Pagbilao power plant	Therma Luzon Inc. or *Therma*	22.04
	Sual coal-fired power plant - 1,000 *MW*	San Miguel Energy Corporation or *SMEC*	5.253
	Coal-fired Calaca power plant - 600 *MW*	Sem-Calaca Power Corporation or *Sem-Calaca*	7.34
2010	Combined cycle gas turbine, natural gas-fired Ilijan power plant - 1,200 *MW*	South Premiere Power Corporation or *SPPC*	19.87

Pending the finalization of the purchase agreement between each of the successor owners of the assets and *IPP* contracts with *NPC*, the supplier of power of *MERALCO* is still *NPC/PSALM*. Payments of the contracted volume are made based on the billing instructions received by *MERALCO.*

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 June 11, 2009, *MMPC* began delivering energy to *MERALCO* under a two year Contract for the Sale of Electricity or *CSE.* The *CSE* is a “take and pay” arrangement, without a minimum energy volume. Energy billed to *MERALCO* is billed on an hourly basis based on the *ERC* approved *NPC TOU* rate plus certain pre-agreed cost components. Being an embedded generator accounting for less than 0.1% of the Luzon-wide system capacity, as well as a renewable energy generator, purchases from *MMPC* are zero-rated *VAT* sales. Energy deliveries from *MMPC* are also exempt from power delivery service charge.

On July 1, 2009, the *ERC* approved the *CSE* on a provisional basis. In the event that the final rates approved by the *ERC* are lower that what *MMPC* currently charges *MERALCO,* the latter shall refund to its consumers excess payments return by *MMPC. MERALCO* is awaiting final approval of the *CSE* by the *ERC.*

Bacavalley Energy, Inc. or BEI

The *Parent Company* signed a *CSE* with *BEI* on November 12, 2010. *BEI* owns and operates a 4MW renewable energy generation facility powered by landfill gas in San Pedro, Laguna.

The terms of the *BEI CSE* are similar to that signed with *MMPC. MERALCO* filed an application for the approval of the *CSE* with the *ERC*, for the provisional implementation of the contract on December 15, 2010. The foregoing is still pending with the *ERC*.

Committed Energy Volume to be Purchased

The following are forecasted purchases/payments to *IPPs* corresponding to the *TOP* volume provisions of the contracts. The assumptions used for the *TOP* volume include (i) fixed cost components, (ii) variable cost components, (iii) fixed cost forecasts projected using the *U.S.* and Philippine Consumer Price Index or *CPI* and foreign exchange rate, (iv) fuel cost forecasts based on heat rates and fuel prices projected using *U.S. CPI*, among others.

Year	Minimum Energy Quantity (MEQ)	Equivalent Amount
	(In Million Kilowatt-Hours)	*(In Millions)*
2011	14,880	71,899
2012	14,880	72,306
2013	14,880	73,448
2014	14,880	74,615
2015	14,880	76,128
2016	14,780	77,230
2017-2025	133,024	746,208

Operating Lease Commitments

Rockwell Land is a lessor of commercial spaces included in the investment properties portfolio. These noncancellable leases have remaining terms between two to 10 years up to 2015. All leases include an annual escalation. Future minimum lease revenue follows:

	Amount
	(In Millions)
2011	₱365
2012	111
2013	68
2014	64
2015	18
	₱626

Construction Contracts of Rockwell Land

One Rockwell

In April 2008, *Rockwell Land* entered into a contract with *DATEM* incorporated for the construction of the superstructure of *One Rockwell*, amounting to ₱2,500 million, inclusive of all taxes and related costs. As at December 31, 2010 the accumulated amount incurred was ₱1,800 million.

The Grove

The superstructure works related to *The Grove* project was contracted by Hilmarc's Construction Corporation or *Hilmarc*. The contract sum for the work amounted to ₱1,600 million, inclusive of all pertinent local and national taxes, overhead and cost of labor and materials and all cost necessary for the proper execution of the work. Superstructure works commenced in February 2010 and is currently ongoing. As at December 31, 2010, total amount incurred and paid related to this contract amounted to ₱113 million.

Edades Garden and Villas

In October 2010, *Rockwell Land* contracted *Hilmarc* to do substructure works related to the *Edades Garden and Villas* Project. The contract amounted to a fixed fee of ₱2,500 million, inclusive of all pertinent local and national taxes, overhead and cost of labor and materials and all cost necessary for the proper execution of the works. Substructure works commenced in November 2010 and is currently ongoing. As at December 31, 2010, ₱133 million has been incurred and was already paid.

35. Earnings Per Share Attributable to Equity Holders of the Parent

Basic and diluted earnings per share are calculated as follows:

	2010	2009	2008
	(In Millions, Except per Share Data)		
Net income attributable to equity holders of the parent (a)	**₱9,685**	₱6,005	₱2,800
Shares:			
Common shares at beginning of year	**1,127**	1,104	1,103
Weighted average common shares – issuances	–	4	1
Weighted average common shares (b)	**1,127**	1,108	1,104
Number of shares under option	**–**	–	10
Weighted average number of shares that would have been issued at fair value	**–**	–	(8)
Adjusted weighted average common shares – diluted (c)	**1,127**	1,108	1,106
Per Share Amounts:			
Basic earnings per share (a/b)	**₱8.59**	₱5.42	₱2.54
Diluted earnings per share (a/c)	**₱8.59**	₱5.42	₱2.53

36. Other Matters

Revised SL Caps

On September 29, 2004, the *ERC* issued the "Guidelines for the Application and Approval of Cap on the Recoverable Rate of Distribution System Losses" requiring the submission of segregated system loss caps for technical, non-technical and administrative losses and the *Parent Company* estimates for the succeeding five years. Thereafter, a series of exchanges were made between *ERC* and the different distribution utilities.

On December 8, 2008, the *ERC* promulgated Resolution No. 17, Series of 2008, entitled "A Resolution Adopting a New System Loss Cap for Distribution Utilities," where a lower maximum rate of system loss (technical and non-technical) that a utility can pass on to its customers. The new system loss cap shall be the lower of the actual but not to exceed 8.5% for private utilities, effective January 2010 billing, which is one percentage point lower than the 2009 system loss cap of 9.5%. The actual company use (administrative loss) shall be treated as part of the operation and maintenance expense in the next reset for utilities under *PBR*. The manner by which the utility will be rewarded for their efforts in system loss reduction shall be addressed by the *ERC* in the *PIS* under *PBR*.

On December 8, 2009, *MERALCO* filed a Petition to Amend the said Resolution and suspension of the implementation of the new system loss cap of 8.5% starting January 2010. The proposed amendment aims for the consistency with the provisions of *RA No. 9136* and *RA No. 7832*, by increasing the level of system loss cap to not less than 9%.

Prior to the Petition, the *ERC* denied *MERALCO*'s appeal contained in a letter to the *ERC*, seeking deferment of the imposition of the revised system loss cap.

As at February 28, 2011, the *ERC* has yet to act on the Petition.

Retail Competition

On February 18, 2011, the *ERC* pursuant to its mandate under Section 3, Rule 12 of the *EPIRA* Implementing Rules and Regulations issued an Order setting public hearings for the purpose of determining whether or not Open Access and Retail Competition may already be declared. The *DOE, NPC* and *PSALM* were directed to appear at the hearings and present evidence on the matter. *MERALCO* is an intervenor in said case. Hearings have been conducted and the parties have been directed to submit a legal memorandum on this matter. Another hearing has been set for April 6, 2011.

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." These Guidelines effectively give *PEZA* franchising and regulatory powers in ecozones. The Guidelines are the subject of an injunction case filed by the *DU*s at the *RTC*-Pasig.

Meantime, in support of the government's objective of providing lower cost to ecozone locators, the Company 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* allowed the immediate implementation of the program, which is still ongoing.

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.

Up to May 2001, *NPC* operated and developed the nationwide transmission grid. Thereafter, with the effectivity of the *EPIRA*, the authority and responsibility were transferred to *TransCo*. The distribution lines of *MERALCO* are connected to the transmission grid of *TransCo*. Since January 15, 2009, *NGCP* began to operate the transmission grid of *TransCo* under a Concession Agreement.

On March 10, 2000, the residents along Tamarind Road, Dasmariñas Village, Makati City or *plaintiffs,* filed a case with the *RTC-Makati* against *NPC* enjoining the latter 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. On March 13, 2000, the *RTC-Makati* initially issued an Order directing the parties to maintain the status quo. On April 3, 2000, *RTC-Makati* granted the preliminary injunction prayed for by the *plaintiffs*. The decision was confirmed 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*, as moved by the *plaintiffs. 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 a counter bond by defendant *NPC* in the amount of ₱10 million, intervenor *MERALCO* in the amount of ₱2 million, and intervenor *NGCP* in the amount of ₱2 million, 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 February 28, 2011, this case remains pending for resolution in the *CA*.

Purchase of Subtransmission Assets or STAs

On June 30, 2008, the *ERC* approved the sale of various *STA*s of *Transco* to the *Parent Company* as covered by a Contract to Sell for ₱188 million, which was fully paid in September 2008. The *Parent Company* began billing customers connected to the *STA*s from August 26, 2009 to September 25, 2009.

On November 25, 2009, the *Parent Company* signed a Contract to Sell with *Transco* for the sale and purchase of subtransmission assets for ₱86 million. On December 3, 2009, the *Parent Company* and *Transco* jointly filed an application with the *ERC* for the sale of various subtransmission lines/assets of *Transco* to *MERALCO.* On February 25, 2010, the *ERC* approved the sale of *Transco's* subtransmission assets in favor of *MERALCO* under the terms provided in the Contract to Sell. As at February 28, 2011, the actual settlement between the *Parent Company* and *Transco* remains pending upon the request of *Transco.*

With respect to metering arrangement, *NGCP* will continue to be the meter service provider until *NGCP* is able to install its totalizing meters at the new delivery points. Thereon, it will be the *Parent Company*'s obligation and responsibility to meter the customers. However, even if the *Parent Company* has the technical capability to meter all these customers, it can assume the metering function from *NGCP* for the customers with electric service contracts only upon securing a *WESM* Metering Provider License from the *ERC*.

A *MOA,* which will cover in detail the protocol between the *Parent Company*, *NGCP*, the Suppliers (*NPC* and Team Energy) and *PEMC* with regard to the foregoing arrangements, is being finalized.

Acquisition of Carmelray Industrial Park II or CIP2's
existing Distribution System and Concession Agreement

On April 11, 2009, pursuant to a *MOA* entered into between *MERALCO* and Carmelray-JTCI Corporation or *CJC*, and duly approved by the *PEZA*, *MERALCO* took over the 13.8-kV distribution line facilities and switching stations of the *CIP2* in order to ensure adequate supply of electricity to the park and its locators for a period of 19 years from effective date until June 28, 2028. *CIP2* is located in Calamba, Laguna, which is within the franchise area of *MERALCO.* On April 17, 2009, the board of *PEZA* approved the registration by *MERALCO* as a *PEZA*-registered utilities enterprise subject to certain conditions.

As a *PEZA*-registered enterprise, *MERALCO* has the option to pay income tax at 5% of gross income generated from locators in CIP2, in lieu of all national and local taxes, except real property taxes. However, *Meralco* opted to file its income tax return under the regular corporate income tax calculation method.

Petition for Dispute Resolution

On September 9, 2008, *MERALCO* filed a Petition for Dispute Resolution with the *ERC*, 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 No.2 of *TransCo*'s San Jose, Bulacan substation on July 11, 2008. The Petition seeks to, among others, and 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; 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 relation to said Petition, *PEMC* has agreed to implement the segregation of the line rental amounts associated with the *Parent Company*'s bilateral contracts from the *WESM* energy trading amount in accordance with the *WESM* Rules, as requested by the *Parent Company*.

Hearings on the petition have been completed and pending the resolution by the *ERC*.

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 the *Parent Company* 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. A decision of the *ERC*, which directed 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 February 28, 2011, *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 amounted to ₱315 million during the May–June 2005 billing periods which has been paid for by the *Parent Company* and ₱318 million during the November 2005, February 2006 and April-June 2006 billing periods, which is being disputed and withheld by the *Parent Company*. *MERALCO* believes that there is no basis for the imposition of the premium charges as there was no *ERC*-approved *TSC* between petitioner and *NPC* and the premium charges imposed by *NPC* has not been approved by the *ERC*.

Glossary

MERALCO'S UNBUNDLED TARIFF COMPONENTS

DISTRIBUTION CHARGE refers to the cost of developing, building, operating and maintaining the distribution system of Meralco, which brings power from high-voltage transmission grids, to commercial and industrial establishments and to residential end-users.

ENVIRONMENTAL CHARGE is mandated by the Electric Power Industry Reform Act of 2001 (EPIRA) for the rehabilitation and maintenance of watershed areas surrounding hydroelectric plants for sustained power generation.

GENERATION CHARGE is the cost of power generated and sold to Meralco by its suppliers, the National Power Corporation (NPC), the Independent Power Producers (IPPs), and the Wholesale Electricity Spot Market (WESM).

INTER-CLASS CROSS SUBSIDY CHARGE is imposed on industrial and commercial end-users in order to reduce electricity rates of other customer sectors such as the residential end-users, hospitals, streetlights and charitable institutions. This subsidy was fully removed in November 2006.

LIFELINE DISCOUNT/LIFELINE SUBSIDY is a socialized pricing mechanism provided for by Section 73 of the EPIRA. In Meralco's case, as approved by the ERC, residential customers using up to 100 kWh in a given month will enjoy a Lifeline Discount to be applied to the total of the generation, transmission, system loss, distribution, supply and metering charges. The discount varies according to consumption and is funded by a Lifeline Subsidy Charge to be paid by all other customers.

LOCAL FRANCHISE TAX is paid to local government units in accordance with the provision of the Local Government Code.

METERING CHARGE refers to cost of reading, operating and maintaining power metering facilities and associated equipment, as well as other costs attributed to the provision of metering service.

MISSIONARY ELECTRIFICATION CHARGE is mandated by EPIRA to fund the electrification of remote and unviable areas, as well as areas not connected to the transmission system.

SUPPLY CHARGE refers to the cost of rendering service to customers, such as billing, collection, customer assistance and associated services.

SYSTEM LOSS CHARGE refers to the cost recovery for the cost of power lost due to technical and non-technical system losses. The maximum level of losses that may be recovered by private distribution utilities was set at 9.5%, by Republic Act 7832, but it was reduced to 8.5% starting 2010, as provided under ERC Resolution No. 17, Series of 2008.

TRANSMISSION CHARGE refers to the cost of delivery of electricity from generators, usually located in remote areas or provinces, to the distribution system of Meralco. This goes to the National Grid Corporation of the Philippines (NGCP).

UNIVERSAL CHARGE is remitted to the Power Sector Assets and Liabilities Management Corporation (PSALM), owned and controlled by the government, and created by Republic Act 9136. At present, this includes the missionary electrification and environmental charges.

VALUE ADDED TAX (VAT) is the percent tax imposed on the value of the sale of electricity and related services through all the stages of generation, transmission, distribution and sale of electricity to the final consumer. It is a form of indirect sales tax because the totality of the VAT collected on each sale transaction in all the stages mentioned is charged to the final consumer as part of the purchased price with sellers acting merely as tax collectors.

MERALCO'S TARIFF CATEGORIES

FLAT STREETLIGHTING SERVICE (FS) is the rate class applicable to customers who wish to avail of public streetlighting at a fixed monthly rate. Street lamps for this service are installed by Meralco on existing distribution poles in accordance with company specifications for equipment, installation, maintenance and operation.

GOVERNMENT HOSPITALS AND METERED STREETLIGHTING SERVICE (GHMS) is the rate class applicable to government-owned metered streetlights; government hospitals and traffic lights; certain public parks; and, duly registered facilities of charitable institutions.

INDUSTRIAL SERVICE (IS) is the rate class applicable to industrial customers with demand of more than five kilowatts for general power, heating, and/or lighting purposes. This rate category has five sub-classifications:

- Small, for customers with demands greater than five kilowatts but less than 40 kilowatts
- Medium, for customers with demands of at least 40 kilowatts but not more than 200 kilowatts
- Large, for customers with demands greater than 200 kilowatts but less than 2,000 kilowatts
- Very large, for customers with demands of at least 2,000 kilowatts, but less than 10,000 kilowatts
- Extra large, for customers with demand of at least 10,000 kilowatts

NON-INDUSTRIAL SERVICE (NIS) is the rate class applicable to non-industrial customers with demands of more than five kilowatts for general power, heating and/or lighting purposes. This rate class has four sub-classifications: small, medium, large and very large depending on load, as similarly defined for industrial service, except that very large covers all nonindustrial customers with demand of at least 2,000 kilowatts.

RESIDENTIAL AND GENERAL SERVICE (RGS) is the rate class applicable to all domestic customers for purposes such as lighting, heating, etc., in a single dwelling unit. This rate class is also applicable to non-residential customers with a connected load of not more than 5,000 watts.

OTHER ELECTRICITY RATE TERMS

AUTOMATIC ADJUSTMENT OF GENERATION AND SYSTEM LOSS CHARGES is an automatic recovery mechanism promulgated by the ERC that allows the Generation and System Loss Charges to change monthly, depending on the movement in generation costs and the losses per voltage level. This mechanism better reflects the true cost of electricity, since changes in the generation cost are immediately manifested on customers' bills. The automatic nature of the mechanism was suspended in September 2006 following the Supreme Court Decision on Meralco's Second GRAM. The automatic adjustment mechanism resumed in July 2007 upon the effectivity of amendments to EPIRA IRR Section 4(e) of Rule 3. The suspension was lifted by the ERC.

GENERATION RATE ADJUSTMENT MECHANISM (GRAM) is a cost recovery mechanism implemented by the ERC, which allows distribution utilities to file with the ERC on a quarterly basis, for an adjustment in the Generation Charge to cover fluctuation in the price of electricity sourced from the NPC and IPPs. This has been replaced by a new mechanism, covered by the Guidelines for the Automatic Adjustment of the Generation and System Loss Rates by Distribution Utilities.

PERFORMANCE-BASED REGULATION (PBR) is an internationally accepted ratemaking methodology allowed by Section 43 (f) of the Electric Power Industry Reform Act (Republic Act 9136). Replacing the Return-on-Rate Base (RORB) or Cost-Plus regulation, the PBR entails the use of incentive and penalty mechanisms as determined by the performance of the public utility . These incentive and penalty mechanisms include:

a) GUARANTEED SERVICE LEVEL (GSL) refers to the incentive scheme under the Rules for Distribution Wheeling Rates (RDWR) for distribution utilities (DU) governed by PBR which provides customers guarantees regarding responsiveness and effectiveness. If GSLs are not met, pre-determined penalties will be paid by distribution utilities directly to customers.

b) PERFORMANCE INCENTIVE SCHEME (PIS) refers to the scheme under the RDWR for DUs governed by PBR. Each regulated entity is rewarded for achieving specified performance target levels and penalizes it for failing to achieve specified target levels.

c) S-FACTOR refers to the performance incentive factor or S-factor under the RDWR which determines the rewards or penalties of DUs under the price-linked incentive scheme. This will be a weighted performance measure, based on the performance levels achieved against a number of indices over the calendar year preceding each Regulatory Year.

RATE BASE is the value established by the ERC, on which a utility is allowed to earn a specified rate of return. The rate base represents the utility's appraised asset value – or investment in facilities, equipment and other property used and useful in the provision of electric service – and one-sixth of the utility's annual operations and maintenance expenses.

RETURN ON RATE BASE (RORB) is the ratio of operating income to the utility's rate base expressed as a percentage. Meralco's current unbundled tariffs were based on an RORB equivalent to its weighted average cost of capital (WACC) for the year 2000, as determined by the ERC.

RULES FOR SETTING DISTRIBUTION WHEELING RATES (RDWR) alternative form of rate setting methodology recently adopted by the ERC. The RDWR is based on performance based regulation (PBR), as opposed to the traditional Return on Rate Base methodology. Under this new scheme, utilities are offered incentives to improve performance and reduce costs, which is expected to result in lower electricity rates in the long term. This is an update of the Distribution Wheeling Rates Guidelines (DWRG) considering specific entry points among private distribution utilities.

SENIOR CITIZEN DISCOUNT is a discount extended to qualified electric service customers as provided for by Republic Act 8884 or the Expanded Senior Citizens Act of 2010. There are two Senior Citizens Discounts provided to end-users. The first provides at least a 5% discount on the electricity bills of residential accounts registered under the name of a senior citizen which consume no more than 100 kWh a month. The second grants at least a 50% discount on the electricity bills of senior citizen institutions accredited by the Department of Social Welfare and Development.

The discounts are applied on the qualified customers' generation, transmission, system loss, distribution, supply and metering charges, and are funded through a subsidy to be paid by customers that are not availing of the Senior Citizen Discounts or the Lifeline Discount.

TIME-OF-USE RATES (TOU) the electricity prices that vary depending on the time periods in which energy is consumed. With time-of-use pricing, higher rates will be charged during hours when the demand for electricity is at its highest, and lower rates during off-peak hours. Demand for electricity peaks at about 11 am, 2 pm and 7 pm. Such rates provide an incentive for consumers to curb power use during peak times, thus reducing the peak system demand of the utility. This can avoid or defer the construction of new power plants, substations, transmission and distribution facilities, freeing much needed resources that can be redirected for other productive activities.

ELECTRIC INDUSTRY PARTICIPANTS

DISTRIBUTION UTILITY (DU) refers to any electric cooperative, private corporation, government-owned utility or existing local government unit which has an exclusive franchise to operate a distribution system in accordance with the EPIRA, including DUs operating in the economic zones.

ENERGY REGULATORY COMMISSION (ERC) the independent, quasi-judicial regulatory body created pursuant to Republic Act 9136.

INDEPENDENT POWER PRODUCER (IPP) an existing power generating entity which is not owned by the NPC.

NATIONAL GRID CORPORATION OF THE PHILIPPINES (NGCP) is a privately-owned corporation and is the corporate vehicle of the consortium awarded the concession to assume the power transmission functions of the National Transmission Corporation (TransCo). It is granted a franchise to operate and maintain the country's power transmission grid under Republic Act 9511.

NATIONAL POWER CORPORATION (NPC) is the government-owned and controlled corporation created under Republic Act 6395, as amended, whose generation assets, real estate and other disposable assets as well as IPP contracts of NPC, except the assets of SPUG, shall be transferred to the Power Sector Assets and Liabilities Management (PSALM) for privatization while its transmission assets shall be transferred to the TransCo.

NATIONA L TRANSMISSION CORPORATION (TransCo) is a government-owned and controlled corporation created under the EPIRA which shall assume the authority and responsibility of NPC for the planning, construction and centralized operation and maintenance of its high voltage transmission facilities, including grid interconnection and ancillary services.

PHILIPPINE ECONOMIC ZONE AUTHORITY (PEZA) refers to the government agency created under Republic Act 7916, as amended by Republic Act 8748, tasked to set the general policies on the establishment and operations of the ecozones industrial estates, export processing zones, free trade zones and the like.

PHILIPPINE ELECTRICITY MARKET CORPORATION (PEMC) is non-stock and non-profit corporation constituted pursuant to the EPIRA, as the Autonomous Group Market Operator (AGMO) tasked to undertake the preparatory work and initial operation of the Wholesale Electricity Spot Market (WESM).

POWER SECTOR ASSETS AND LIABILITIES MANAGEMENT CORPORATION (PSALM) is a government-owned and controlled corporation created under the EPIRA, which took ownership of all existing NPC generation assets, liabilities, IPP contracts, real estate and all other disposable assets.

PRIVATE ELECTRIC POWER OPERATORS ASSOCIATION, INC. (PEPOA) is an association of privately-owned electricity utilities franchised to operate an electric light and power distribution service in the urban areas outside of Metro Manila.

RETAIL ELECTRICITY SUPPLIER (RES) is a person or entity authorized by ERC to sell, broker, market or aggregate electricity to end-users in a Contestable Market.

WHOLESALE ELECTRICITY SPOT MARKET (WESM) is the market where trading of electricity will be made and is established by the Department of Energy (DOE) pursuant to the EPIRA.

OTHER ELECTRIC INDUSTRY TERMS

MAGNA CARTA FOR RESIDENTIAL ELECTRICITY CONSUMERS refers to the set of rules which governs the rights and obligations of residential consumers.

OPEN ACCESS refers to the system of allowing any qualified person the use of transmission and/or distribution system and associated facilities subject to the payment of transmission and/or distribution retail wheeling rates duly approved by the ERC.

RESTRUCTURING refers to the process of reorganizing the electric power industry in order to introduce higher efficiency, greater innovation and end-user choice. It shall be understood as covering a range of alternatives enhancing exposure of the industry to competitive market forces.

TRANSITION SUPPLY CONTRACT (TSC) is a document, as provided in Section 67 of Republic Act 9136 on the Electric Power Industry Reform Act that contains the agreement between the generator and distribution utility on the terms and conditions of the energy to be supplied and the corresponding scheduleof rates to be applied.

TECHNICAL TERMS

AUTOMATIC LOAD DROPPING (ALD) is the process of automatically and deliberately removing pre-selected loads from a power system in response to an abnormal condition in order to maintain the integrity of the power system.

CUMULATIVE INTERRUPTION TIME (CIT) is the cumulative length of power interruption, in hours, that a customer connected to the Meralco distribution system experiences on the average, within a certain time period.

DISTRIBUTION SYSTEM refers to the system of wires and associated facilities of a franchised DU extending between: (a) the delivery points on the Grid and any subtransmission system; and (b) the points of connection of embedded generators, on the one hand, and the points of connection of user systems and equipment of end-users, on the other hand.

ELECTRIC POWER GENERATION is the process of converting primary energy sources, e.g. flowing water, fossil fuels (oil,coal, and natural gas) and radioactive (uranium) materials, solar radiation, wind and geothermal, into electricity.

ELECTRIC POWER PLANT refers to facilities for producing electricity through electric power generation.

ENERGY is the amount of work done.

GIGAWATTHOUR (GWh) is the unit of electric energy equal to 1,000,000,000 watthours.

GIGAWATT (GW) is the unit of electric power equal to 1,000,000,000 watts.

GRID is a high voltage backbone system of interconnected transmission lines, substations and related facilities, located in each of Luzon, Visayas and Mindanao, or as may be determined by the ERC in accordance with Section 45 of the EPIRA.

INTERRUPTION FREQUENCY RATE (IFR) is the average number of times each customer connected to the Meralco distribution system experiences power interruption within a certain time period. IFR includes pre-arranged, forced and generation/transmission-related interruptions. Forced interruptions result from emergency conditions directly associated with a power system component, requiring that it be taken out of service immediately, either automatically or through a switching operation. Examples of interruptions of this nature include those that are initiated by typhoons, fires, earthquakes, equipment failures, trees and other foreign objects touching the lines, and transient faults.

KILOVOLT-AMPERE (kVA) is the practical unit of apparent power, equivalent to 1,000 volt-amperes.

KILOWATT (kW) is the unit of electric power equal to 1,000 watts.

KILOWATTHOUR (kWh) is the unit of energy equal to 1,000 watthours.

LOAD is entity or electrical equipment that consumes or draws electrical energy.

LOAD FACTOR is the ratio of the total energy delivered during a given period to the product of the maximum demand and the number of hours during the same period.

LUZON GRID is the electric power transmission network in the island of Luzon.

MAINTENANCE is any activity intended to keep equipment in satisfactory working condition including tests, measurements, replacements, adjustments and repairs that are either corrective or preventive in nature.

MANUAL LOAD DROPPING (MLD) is the process of manually and deliberately removing pre-selected Loads from a power system, in response to an abnormal condition, and in order to maintain the integrity of the power system.

POWER is the time rate of transferring or transforming energy.

SUBTRANSMISSION LINES carry power from a bulk power source to distribution substations.

SYSTEM LOSS, in a distribution system, is the difference between the electric energy purchased and/or generated and the electric energy sold by the distributor. More specifically, it refers to technical and non-technical losses occurring in a distribution system during the conveyance of electricity to end-users.

SYSTEM TROUBLES are interruptions resulting from equipment failure, operating problems, construction troubles and design deficiencies.

TRANSIENT FAULT is a fault that is self-clearing or one that can be cleared by momentary interruptions of the circuit.

WATT is the amount of usable (effective) power delivered or consumed.

OTHERS

CUSTOMER SATISFACTION INDEX is the weighted index that measures general and specific areas of customer satisfaction and priorities. Both satisfaction and level of importance by attribute are dictated by customers through an annual survey (quarterly reading starting 2009). This survey is conducted among residential, core and non-core customers.

Business Center Directory

CENTRAL

MERALCO CONSUMER ASSISTANCE OFFICE (MCAO)
Unit 506, 5th Floor, Pacific Center Bldg., San Miguel Ave., Pasig City
Direct Line: (632) 1622-6005, (632) 1622-6006
Fax: (632) 632-8946

ANGONO
M. L. Quezon Ave., Angono, Rizal
Direct Line: (632) 651-0482, (632) 651-0483, (632) 651-0419
Fax: (632) 1622-7532

Tanay BC Extension
J. Abad Santos St. corner Quirino St. Tanay, Rizal
Direct Line: (632) 693-1421, (632) 654-5449
Fax: (632) 654-1051

CAINTA
Ortigas Ave. Extn., Bgy. Sto. Domingo,
near Cainta Junction, Cainta Rizal
Direct Line: (632) 655-0865, (632) 656-7232, (632) 656-7442, (632) 656-7530
Fax: (632) 1622-7446

MASINAG AUXILIARY
6 Sumulong Hi-way, Mambugan, Antipolo City
Direct Line: (632) 1622-7780 to 81, (632) 632-8791, (632) 632-8749
Fax: (632) 632-8780

ESPAÑA
2200 España corner Josefina 3 St., Sampaloc, Manila
Direct Line: (632) 786-3700
Fax: (632) 632-8737

Lubiran Payment Office
Bacood, Sta. Mesa, Manila
Direct Line: (632) 632-8490
Fax: (632) 1622-7490

KAMUNING
761 EDSA, Kamuning, Quezon City
Direct Line: (632) 924-1080, (632) 924-0930, (632) 924-1062, (632) 924-0830, (02) 924-1071
Fax: (632) 1622-7437

Araneta (Ali Mall) BC Extn
Gen. Romulo St. corner P. Tuazon, Quezon City
Direct Line: (632) 911-3535
Fax: (632) 1622-7510

MAKATI
9581 Kamagong St. corner Ayala Ave. Extn,
Bgy. San Antonio, Makati City
Direct Line: (632) 729-9866 to 73, (632) 899-7119, (632) 899-7114, (02) 899-7115
Fax: (632) 729-9870 (1st floor), (632) 1622-8762 (2nd floor)

MALATE
957 Escoda St., Malate, Manila
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Fax: (632) 632-8433 (1st floor)

PASAY AUXILIARY
2238 F.B. Harrison St., Pasay City
Direct Line: (632) 831-1968, (632) 831-3352, (632) 834-0327
Fax: (632) 632-8475

MANDALUYONG
285 Shaw Blvd. corner Yulo St., Mandaluyong City
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Fax: (632) 1622-7749

MARIKINA
Bayan-Bayanan Ave. corner Gen. Ordoñez St.,
Concepcion, Marikina City
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Fax: (632) 632-8550

San Mateo BC Extension
Amado Bldg., 503 Gen. Luna St., Brgy. Malanday,
San Mateo, Rizal
Direct Line: (632) 997-7731, (632) 997-5523

PASIG
60 Dr. Sixto Ave. cor. Dr. Pilapil St., Sagad, Pasig City
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Fax: (632) 632-8892

ROOSEVELT
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Fax: (632) 632-8732

TUTUBAN
Tutuban Shopping Complex, Mayhaligue St.
corner Antonio Rivera St., Tondo, Manila
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Fax: (632) 632-8303

NORTH

BALAGTAS
Burol I, Mc Arthur Hi-way, Balagtas, Bulacan
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(6344) 693-3665, (044) 693-1196
Fax: (632) 632-8706

Marilao BC Extension
McArthur Hi-way, Abangan Sur, Marilao, Bulacan
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BALINTAWAK
1199 EDSA near Muñoz Market, Balintawak,
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BALIWAG
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(6344) 766-2552
Fax: (632) 1622-7435

San Miguel BC Extension
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COMMONWEALTH
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MALABON
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CALOOCAN AUXILIARY
135 Samson Road, Kalookan City
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(632) 363-8230, (632) 367-9119, (632) 435-7705
Fax: (632) 1622-7481

MALOLOS
Pariancillo St., Brgy. Sto. Nino, Malolos City, Bulacan
Direct Line: (6344) 791-6419, (6344) 791-0860
(6344) 791-6420
Fax: (632) 1622-7563

Hagonoy BC Extension
Puso ng Hagonoy Mall, Poblacion, Hagonoy, Bulacan
Direct Line: (044) 667-1494

Plaridel BC Extension
Gov. Padilla St., Brgy. Agnaya, Plaridel, Bulacan
Direct Line: (6344) 795-1094

NOVALICHES
Quirino Hi-way corner Forest Hills, Gulod, Novaliches,
Quezon City
Direct Line: (632) 936-2313, (632) 936-0859,
(632) 417-3561
Fax: (632) 632-8393

CAMARIN AUXILIARY
Fran-Glo Bldg, Susano Rd. corner Zapote Rd,
Camarin, Kalookan City
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STA MARIA
657 Paso Bagbaguin, Sta. Maria, Bulacan
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(6344) 641-0359, (6344) 641-2297
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San Jose Del Monte BC Extension
Tungkong Manga, San Jose del Monte City, Bulacan
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SOUTH

ALABANG
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Fax: (632) 1622-7471

Metropolis Extension
National Rd., Ground Flr., Metropolis Star, Alabang Muntinlupa City
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United Paranaque Extension
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Meadowood Ave. corner Aguinaldo Hiway, Bacoor, Cavite
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Bahayang Pag-asa PO
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BATANGAS
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DASMARIÑAS
Gen. Aguinaldo Hi-way, Dasmariñas, Cavite
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Fax: (632) 632-8756

Gen. Mariano Alvarez BC Extension
Governor's Drive., Bulihan, Silang, Cavite
Direct Line: (6346) 972-0305, (6346) 972-0307

LAS PIÑAS
EMC Drive, Alabang-Zapote Rd., Pamplona, Las Piñas City
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Fax: (632) 1622-7484

Parañaque Auxiliary Business Center
252 Quirino Ave., Tambo, Parañaque City
Direct Line: (632) 852-0385, (632) 851-2879, (632) 853-7052
Fax: (632) 632-8742

LUCENA
Doña Aurora Blvd., Gulang-Gulang, Lucena City
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Fax: (6342) 710-2332, 632-8673

Mauban PO
Quezon St., Bgy Bagumbayan, Mauban, Quezon
Direct Line: (6342)784-0580

ROSARIO
Gen. Trias Drive, Rosario, Cavite
Direct Line: (6346)438-1234, (6346)438-2869
Fax: (6346)438-4038,1622-7794

Trece Martirez BC Extension
Bgy Luciano near Capitolyo, Trece Martirez, Cavite
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Fax: (632) 632-8752

SAN PABLO
Maharlika Hi-way, Bgy San Ignacio, San Pablo City, Laguna
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Fax: (632) 1622-7771

Sta. Cruz Auxiliary Business Center
P. Guevarra St., Poblacion I, Sta. Cruz, Laguna
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COMMON STOCK

The Company's common stock is listed in the Philippine Stock Exchange (Ticker symbol: MER). The declassification of the Company's common stock removed the Class "A" and Class "B" classification effective September 3, 2007. The declassification does not entail a recall, a cancellation or a replacement of certificates previously issued. All existing stock certificates, whether Class "A" or Class "B", will remain valid. Shares are available to foreign investors up to a maximum of 40 percent of the outstanding capital stock.

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