

**SMC GLOBAL POWER HOLDINGS CORP.**  
**(A Wholly-owned Subsidiary of San Miguel Corporation)**  
**AND SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**  
**December 31, 2014 and 2013**

## REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders  
SMC Global Power Holdings Corp.

We have audited the accompanying consolidated financial statements of SMC Global Power Holdings Corp. (a wholly-owned subsidiary of San Miguel Corporation) and Subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2014 and 2013, and the consolidated statements of income, consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for the years then ended, and notes, comprising 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 auditors' 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 auditors consider 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 policies used and the 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 consolidated financial position of SMC Global Power Holdings Corp. and Subsidiaries as at December 31, 2014 and 2013, and the consolidated financial performance and consolidated cash flows for the years then ended in accordance with Philippine Financial Reporting Standards.

*R.G. Manabat & Co.*

March 25, 2015  
Makati City, Metro Manila

**SMC GLOBAL POWER HOLDINGS CORP.**  
**(A Wholly-owned Subsidiary of San Miguel Corporation)**  
**AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
(In Thousands)

|                                                              |                    | <b>December 31</b>  |              |
|--------------------------------------------------------------|--------------------|---------------------|--------------|
|                                                              | <i>Note</i>        | <b>2014</b>         | 2013         |
| <b>ASSETS</b>                                                |                    |                     |              |
| <b>Current Assets</b>                                        |                    |                     |              |
| Cash and cash equivalents                                    | 8, 25, 26          | <b>P38,304,294</b>  | P29,125,171  |
| Trade and other receivables - net                            | 4, 9, 18, 25, 26   | <b>18,208,339</b>   | 31,540,444   |
| Inventories                                                  | 4, 10              | <b>1,365,033</b>    | 1,499,135    |
| Prepaid expenses and other current assets                    | 7, 11              | <b>9,137,202</b>    | 7,234,892    |
| <b>Total Current Assets</b>                                  |                    | <b>67,014,868</b>   | 69,399,642   |
| <b>Noncurrent Assets</b>                                     |                    |                     |              |
| Property, plant and equipment - net                          | 4, 12              | <b>228,133,323</b>  | 217,021,519  |
| Investments and advances - net                               | 4, 13              | <b>10,612,277</b>   | 6,011,799    |
| Deferred exploration and development costs                   | 4, 6               | <b>671,783</b>      | 525,999      |
| Goodwill and other intangible assets                         | 4, 6, 14           | <b>2,322,241</b>    | 1,728,592    |
| Deferred tax assets                                          | 4, 22              | <b>2,779,380</b>    | 2,909,105    |
| Other noncurrent assets - net                                | 15, 25, 26         | <b>2,215,415</b>    | 3,506,310    |
| <b>Total Noncurrent Assets</b>                               |                    | <b>246,734,419</b>  | 231,703,324  |
|                                                              |                    | <b>P313,749,287</b> | P301,102,966 |
| <b>LIABILITIES AND EQUITY</b>                                |                    |                     |              |
| <b>Current Liabilities</b>                                   |                    |                     |              |
| Accounts payable and accrued expenses                        | 13, 16, 18, 25, 26 | <b>P28,117,804</b>  | P22,971,933  |
| Finance lease liabilities - current portion                  | 4, 7, 25, 26       | <b>16,205,224</b>   | 15,630,430   |
| Current portion of long-term debt - net of debt issue costs  | 17, 25, 26         | <b>1,330,037</b>    | 142,403      |
| Income tax payable                                           |                    | <b>151,360</b>      | 218,519      |
| <b>Total Current Liabilities</b>                             |                    | <b>45,804,425</b>   | 38,963,285   |
| <b>Noncurrent Liabilities</b>                                |                    |                     |              |
| Long-term debt - net of current portion and debt issue costs | 17, 25, 26         | <b>47,383,208</b>   | 46,946,482   |
| Finance lease liabilities - net of current portion           | 4, 7, 25, 26       | <b>170,098,521</b>  | 179,372,291  |
| Deferred tax liabilities                                     | 22                 | <b>3,043,470</b>    | 2,088,065    |
| Other noncurrent liabilities - net of current portion        | 16                 | <b>670,486</b>      | -            |
| <b>Total Noncurrent Liabilities</b>                          |                    | <b>221,195,685</b>  | 228,406,838  |
|                                                              |                    | <b>267,000,110</b>  | 267,370,123  |

Forward

| December 31                             |             |                     |              |
|-----------------------------------------|-------------|---------------------|--------------|
|                                         | <i>Note</i> | 2014                | 2013         |
| <b>Equity</b>                           | <i>19</i>   |                     |              |
| Capital stock                           |             | <b>P1,062,504</b>   | P1,062,504   |
| Additional paid-in capital              |             | <b>2,490,000</b>    | 2,490,000    |
| Undated subordinated capital securities |             | <b>13,110,066</b>   | -            |
| Retained earnings                       |             | <b>29,301,328</b>   | 29,395,060   |
| Reserves                                |             | <b>785,279</b>      | 785,279      |
| <b>Total Equity</b>                     |             | <b>46,749,177</b>   | 33,732,843   |
|                                         |             | <b>P313,749,287</b> | P301,102,966 |

See Notes to the Consolidated Financial Statements.

**SMC GLOBAL POWER HOLDINGS CORP.**  
**(A Wholly-owned Subsidiary of San Miguel Corporation)**  
**AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF INCOME**

(In Thousands, Except Per Share Data)

|                                                                               |                     | <b>Years Ended December 31</b> |              |
|-------------------------------------------------------------------------------|---------------------|--------------------------------|--------------|
|                                                                               | <i>Note</i>         | <b>2014</b>                    | <b>2013</b>  |
| <b>REVENUES</b>                                                               | <i>5, 7, 18, 27</i> |                                |              |
| Sale of power                                                                 |                     | <b>P80,080,157</b>             | P73,882,922  |
| Sale of electricity                                                           |                     | <b>4,213,433</b>               | 160,865      |
|                                                                               |                     | <b>84,293,590</b>              | 74,043,787   |
| <b>COST AND EXPENSES</b>                                                      |                     |                                |              |
| Cost of power sold:                                                           |                     |                                |              |
| Energy fees                                                                   | <i>7</i>            | <b>30,775,896</b>              | 31,269,293   |
| Coal, fuel oil and other consumables                                          | <i>7, 10, 18</i>    | <b>11,945,280</b>              | 11,179,322   |
| Depreciation and amortization                                                 | <i>12</i>           | <b>6,143,866</b>               | 5,382,435    |
| Power purchases                                                               | <i>7</i>            | <b>6,045,468</b>               | 3,929,184    |
| Plant operations and maintenance fees                                         |                     | <b>575,632</b>                 | 194,388      |
| Operating expenses                                                            | <i>7, 18, 20</i>    | <b>2,911,930</b>               | 1,547,750    |
|                                                                               |                     | <b>58,398,072</b>              | 53,502,372   |
|                                                                               |                     | <b>25,895,518</b>              | 20,541,415   |
| <b>INTEREST INCOME</b>                                                        |                     | <b>549,977</b>                 | 447,843      |
| <b>INTEREST EXPENSE AND OTHER FINANCING CHARGES</b>                           | <i>7, 17</i>        | <b>(13,168,470)</b>            | (12,673,891) |
| <b>EQUITY IN NET EARNINGS (LOSSES) OF ASSOCIATES AND JOINT VENTURES - Net</b> | <i>13</i>           | <b>(22,345)</b>                | 795,004      |
| <b>GAIN ON SALE OF INVESTMENT</b>                                             | <i>13</i>           | -                              | 2,587,044    |
| <b>OTHER INCOME (CHARGES) - Net</b>                                           | <i>21</i>           | <b>68,225</b>                  | (8,491,062)  |
| <b>INCOME BEFORE INCOME TAX</b>                                               |                     | <b>13,322,905</b>              | 3,206,353    |
| <b>INCOME TAX EXPENSE (BENEFIT) - Net</b>                                     | <i>22, 23</i>       | <b>2,693,423</b>               | (836,302)    |
| <b>NET INCOME</b>                                                             |                     | <b>P10,629,482</b>             | P4,042,655   |
| <b>Basic/Diluted Earnings Per Share</b>                                       | <i>24</i>           | <b>P8.50</b>                   | P3.23        |

*See Notes to the Consolidated Financial Statements.*

**SMC GLOBAL POWER HOLDINGS CORP.**  
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**AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(In Thousands)

|                                           |             | <b>Years Ended December 31</b> |             |
|-------------------------------------------|-------------|--------------------------------|-------------|
|                                           | <i>Note</i> | <b>2014</b>                    | <b>2013</b> |
| <b>NET INCOME</b>                         |             | <b>P10,629,482</b>             | P4,042,655  |
| <b>OTHER COMPREHENSIVE INCOME</b>         |             |                                |             |
| <b>ITEM THAT WILL NOT BE</b>              |             |                                |             |
| <b>RECLASSIFIED TO PROFIT OR LOSS</b>     |             |                                |             |
| Share in other comprehensive income of an |             |                                |             |
| associate, net of disposal                | 13, 19      | -                              | 39,306      |
| <b>TOTAL COMPREHENSIVE INCOME</b>         |             | <b>P10,629,482</b>             | P4,081,961  |

*See Notes to the Consolidated Financial Statements.*

**SMC GLOBAL POWER HOLDINGS CORP.**  
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**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013**  
(In Thousands)

|                                                                    | <b>Capital<br/>Stock<br/>(Note 19)</b> | <b>Additional<br/>Paid-in<br/>Capital</b> | <b>Retained<br/>Earnings<br/>(Note 19)</b> | <b>Undated<br/>Subordinated<br/>Capital<br/>Securities<br/>(Note 19)</b> | <b>Reserves<br/>(Note 19)</b> | <b>Total Equity</b> |
|--------------------------------------------------------------------|----------------------------------------|-------------------------------------------|--------------------------------------------|--------------------------------------------------------------------------|-------------------------------|---------------------|
| <b>Balance as of January 1, 2014</b>                               | <b>P1,062,504</b>                      | <b>P2,490,000</b>                         | <b>P29,395,060</b>                         | <b>P -</b>                                                               | <b>P785,279</b>               | <b>P33,732,843</b>  |
| Issuance of undated subordinated capital securities                | -                                      | -                                         | -                                          | <b>13,110,066</b>                                                        | -                             | <b>13,110,066</b>   |
| Net income for the year / total comprehensive income               | -                                      | -                                         | <b>10,629,482</b>                          | -                                                                        | -                             | <b>10,629,482</b>   |
| Dividends declared                                                 | -                                      | -                                         | <b>(10,000,000)</b>                        | -                                                                        | -                             | <b>(10,000,000)</b> |
| Distributions paid                                                 | -                                      | -                                         | <b>(723,214)</b>                           | -                                                                        | -                             | <b>(723,214)</b>    |
| <b>Balance as of December 31, 2014</b>                             | <b>P1,062,504</b>                      | <b>P2,490,000</b>                         | <b>P29,301,328</b>                         | <b>P13,110,066</b>                                                       | <b>P785,279</b>               | <b>P46,749,177</b>  |
| Balance as of January 1, 2013                                      | P1,062,504                             | P2,490,000                                | P29,852,405                                | P -                                                                      | P745,973                      | P34,150,882         |
| Share in other comprehensive income of an associate,<br>net of tax | -                                      | -                                         | -                                          | -                                                                        | 39,306                        | 39,306              |
| Net income for the year                                            | -                                      | -                                         | 4,042,655                                  | -                                                                        | -                             | 4,042,655           |
| Total comprehensive income                                         | -                                      | -                                         | 4,042,655                                  | -                                                                        | 39,306                        | 4,081,961           |
| Dividends declared                                                 | -                                      | -                                         | (4,500,000)                                | -                                                                        | -                             | (4,500,000)         |
| Balance as of December 31, 2013                                    | P1,062,504                             | P2,490,000                                | P29,395,060                                | P -                                                                      | P785,279                      | P33,732,843         |

*See Notes to the Consolidated Financial Statements.*

**SMC GLOBAL POWER HOLDINGS CORP.**  
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**AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In Thousands)

|                                                                        |             | <b>Years Ended December 31</b> |              |
|------------------------------------------------------------------------|-------------|--------------------------------|--------------|
|                                                                        | <i>Note</i> | <b>2014</b>                    | <b>2013</b>  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                            |             |                                |              |
| Income before income tax                                               |             | <b>P13,322,905</b>             | P3,206,353   |
| Adjustments for:                                                       |             |                                |              |
| Interest expense and other financing charges                           | 7, 17       | <b>13,168,470</b>              | 12,673,891   |
| Depreciation and amortization                                          | 7, 12       | <b>6,187,640</b>               | 5,404,184    |
| Unrealized foreign exchange losses - net                               | 25          | <b>1,584,500</b>               | 9,592,617    |
| Impairment losses on trade receivables                                 | 9           | <b>144,393</b>                 | 32,850       |
| Equity in net earnings (losses) of associates and joint ventures - net | 13          | <b>22,345</b>                  | (795,004)    |
| Interest income                                                        |             | <b>(549,977)</b>               | (447,843)    |
| Gain on sale of investment                                             | 13          | <b>-</b>                       | (2,587,044)  |
| Operating income before working capital changes                        |             | <b>33,880,276</b>              | 27,080,004   |
| Decrease (increase) in:                                                |             |                                |              |
| Trade and other receivables - net                                      | 9           | <b>(3,037,652)</b>             | (1,633,834)  |
| Inventories                                                            | 10          | <b>134,102</b>                 | (314,185)    |
| Prepaid expenses and other current assets                              | 11          | <b>(1,902,310)</b>             | (240,126)    |
| Other noncurrent assets                                                | 15          | <b>1,290,895</b>               | (1,789,482)  |
| Increase in:                                                           |             |                                |              |
| Accounts payable and accrued expenses                                  | 16          | <b>5,145,871</b>               | 3,128,087    |
| Other noncurrent liabilities                                           |             | <b>670,486</b>                 | -            |
| Cash generated from operations                                         |             | <b>36,181,668</b>              | 26,230,464   |
| Interest income received                                               |             | <b>546,350</b>                 | 527,661      |
| Finance cost paid                                                      | 17          | <b>(2,196,778)</b>             | (800,071)    |
| Income taxes paid                                                      |             | <b>(1,675,452)</b>             | (294,055)    |
| Net cash flows provided by operating activities                        |             | <b>32,855,788</b>              | 25,663,999   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                            |             |                                |              |
| Proceeds from sale of investment                                       | 9, 13       | <b>16,228,991</b>              | -            |
| Net additions to property, plant and equipment                         | 12          | <b>(17,299,444)</b>            | (19,122,531) |
| Additions to investments and advances                                  | 13          | <b>(4,622,823)</b>             | (2,145,936)  |
| Additions to intangible assets                                         | 14          | <b>(593,649)</b>               | -            |
| Deferred exploration and development costs                             | 6           | <b>(145,784)</b>               | (200,780)    |
| Dividends received                                                     | 13          | <b>-</b>                       | 704,407      |
| Net cash flows used in investing activities                            |             | <b>(6,432,709)</b>             | (20,764,840) |

Forward

| <b>Years Ended December 31</b>                                      |             |                     |                    |
|---------------------------------------------------------------------|-------------|---------------------|--------------------|
|                                                                     | <i>Note</i> | <b>2014</b>         | <b>2013</b>        |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                         |             |                     |                    |
| Proceeds from issuance of undated subordinated capital securities   |             | <b>P13,110,066</b>  | P -                |
| Proceeds from long-term debt                                        | 17          | <b>1,500,000</b>    | 33,191,756         |
| Payments of finance lease liabilities                               | 7           | <b>(20,123,987)</b> | (19,146,035)       |
| Dividends paid                                                      | 19          | <b>(10,000,000)</b> | (4,500,000)        |
| Distributions to undated subordinated capital securities holders    | 19          | <b>(723,214)</b>    | -                  |
| Payment of long-term debt                                           | 17          | <b>(193,200)</b>    | (8,708,000)        |
| Net cash flows provided by (used in) financing activities           |             | <b>(16,430,335)</b> | 837,721            |
| <b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b> |             | <b>(813,621)</b>    | <b>(167,154)</b>   |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>                    |             | <b>9,179,123</b>    | <b>5,569,726</b>   |
| <b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>               |             | <b>29,125,171</b>   | <b>23,555,445</b>  |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>                     | 8           | <b>P38,304,294</b>  | <b>P29,125,171</b> |

*See Notes to the Consolidated Financial Statements.*

**SMC GLOBAL POWER HOLDINGS CORP.**  
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**AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
(Amounts in Thousands, Except Per Share Data and Number of Shares)

**1. Reporting Entity**

SMC Global Power Holdings Corp. (the Parent Company) was incorporated in the Philippines and registered with the Philippine Securities and Exchange Commission (SEC) on January 23, 2008, and its primary purpose of business is to purchase, sell, lease, develop and dispose of all properties of every kind and description, and shares of stocks or other securities or obligations, created or issued by any corporation or other entity. The Parent Company's registered office address is located at 155 EDSA, Brgy. Wack-Wack, Mandaluyong City, Metro Manila.

The accompanying consolidated financial statements comprise the financial statements of the Parent Company and its Subsidiaries (collectively referred to as the Group).

The Parent Company is a wholly-owned subsidiary of San Miguel Corporation (SMC). The ultimate parent company of the Group is Top Frontier Investment Holdings, Inc. (Top Frontier). SMC and Top Frontier are public companies under Section 17.2 of the Securities Regulation Code and whose shares are listed in the Philippine Stock Exchange (PSE).

The Parent Company's subsidiaries, primarily engaged in power generation and retail power-related services, are incorporated in the Philippines and registered with the Philippine SEC. The subsidiaries are as follows:

|                                                                  | <i>Note</i>  | <b>Percentage of Ownership</b> |             |
|------------------------------------------------------------------|--------------|--------------------------------|-------------|
|                                                                  |              | <b>2014</b>                    | <b>2013</b> |
| <i>Power Generation</i>                                          | <i>7, 18</i> |                                |             |
| San Miguel Energy Corporation (SMEC)                             |              | <b>100</b>                     | 100         |
| South Premiere Power Corp. (SPPC)                                |              | <b>100</b>                     | 100         |
| Strategic Power Devt. Corp. (SPDC)                               |              | <b>100</b>                     | 100         |
| SMC PowerGen Inc. (SPI)                                          |              | <b>100</b>                     | 100         |
| Limay Power Generation Corporation <sup>(c)</sup>                |              | <b>100</b>                     | 100         |
| SMC Consolidated Power Corporation (SCPC) <sup>(b)</sup>         |              | <b>100</b>                     | 100         |
| San Miguel Consolidated Power Corporation (SMCPC) <sup>(b)</sup> |              | <b>100</b>                     | 100         |
| PowerOne Ventures Energy Inc. (PVEI)                             |              | <b>100</b>                     | 100         |
| <i>Retail and Power-related Service Provider</i>                 | <i>7</i>     |                                |             |
| San Miguel Electric Corp. (SMELC)                                |              | <b>100</b>                     | 100         |
| SMC Power Generation Corp. (SPGC)                                |              | <b>100</b>                     | 100         |
| Albay Power and Energy Corp. (APEC)                              |              | <b>100</b>                     | 100         |
| <i>Others - Coal Mining</i>                                      | <i>6</i>     |                                |             |
| Daguma Agro-Minerals, Inc. (DAMI) <sup>(a)</sup>                 |              | <b>100</b>                     | 100         |
| Sultan Energy Phils. Corp. (SEPC) <sup>(a)</sup>                 |              | <b>100</b>                     | 100         |
| Bonanza Energy Resources, Inc. (BERI) <sup>(a)</sup>             |              | <b>100</b>                     | 100         |

(a) Indirectly owned by the Parent Company through SMEC and has not yet started commercial operations as of December 31, 2014.

(b) Construction of power plants on-going as of December 31, 2014.

(c) Incorporated on February 19, 2013; indirectly owned by the Parent Company through SPI and has not yet started commercial operation as of December 31, 2014.

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## 2. Basis of Preparation

### Statement of Compliance

The consolidated financial statements have been prepared in compliance with Philippine Financial Reporting Standards (PFRS). PFRS are based on International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). PFRS which are issued by the Philippine Financial Reporting Standards Council (FRSC), consist of PFRS, Philippine Accounting Standards (PAS), and Philippine Interpretations.

The consolidated financial statements are also prepared to comply with the requirements under Section 4.12, *Provision of Financial Statements and Reports*, of the US\$300,000 7% Notes due 2016 issued by the Parent Company (Note 17).

The consolidated financial statements were authorized for issue by the Board of Directors (BOD) on March 25, 2015.

### Basis of Measurement

The consolidated financial statements of the Group have been prepared on a historical cost basis of accounting.

### Functional and Presentation Currency

The consolidated financial statements are presented in Philippine peso, which is the Parent Company's functional currency. All financial information are rounded off to the nearest thousand (P000), except when otherwise indicated.

### Basis of Consolidation

A subsidiary is an entity controlled by the Group. The Group controls an entity if and only if, the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control.

When the Group has less than majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including the contractual arrangement with the other vote holders of the investee, rights arising from other contractual arrangements and the Group's voting rights and potential voting rights.

The financial statements of the subsidiaries are included in the consolidated financial statements from the date when the Group obtains control, and continue to be consolidated until the date when such control ceases.

The financial statements of the subsidiaries are prepared for the same reporting period as the Parent Company, using uniform accounting policies for like transactions and other events in similar circumstances. Intergroup balances and transactions, including intergroup unrealized profits and losses, are eliminated in preparing the consolidated financial statements.

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### 3. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all years presented in the consolidated financial statements.

#### Adoption of New or Revised Standards, Amendments to Standards and Interpretations

The Group has adopted the following amendments to standards and new interpretation starting January 1, 2014. Except as otherwise indicated, the adoption of these amendments to standards and interpretation did not have any significant impact on the Group's consolidated financial statements.

#### *Amendments to Standards and Interpretations Adopted in 2014*

The Group has adopted the following PFRS effective January 1, 2014:

- Offsetting Financial Assets and Financial Liabilities (*Amendments to PAS 32, Financial Instruments*). These amendments clarify that:
  - an entity currently has a legally enforceable right to set-off if that right is:
    - not contingent on a future event; and
    - enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties; and
  - gross settlement is equivalent to net settlement if and only if the gross settlement mechanism has features that:
    - eliminate or result in insignificant credit and liquidity risk; and
    - process receivables and payables in a single settlement process or cycle.
- Recoverable Amount Disclosures for Non-Financial Assets (*Amendments to PAS 36*). These narrow-scope amendments to PAS 36, *Impairment of Assets*, address the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The amendments clarified that the scope of those disclosures is limited to the recoverable amount of impaired assets that is based on fair value less costs of disposal.
- Measurement of Short-term Receivables and Payables (*Amendment to PFRS 13*). Amendment to PFRS 13, *Fair Value Measurement*, is part of the Annual Improvements to PFRS 2010-2012 Cycle. The amendment clarifies that, in issuing PFRS 13 and making consequential amendments to PAS 39, *Financial Instruments: Recognition and Measurement*, and PFRS 9, *Financial Instruments*, the intention is not to prevent entities from measuring short-term receivables and payables that have no stated interest rate at their invoiced amounts without discounting, if the effect of not discounting is immaterial. The amendment to PFRS 13 is effective immediately.

#### Standards Issued But Not Yet Adopted

A number of new standards and amendments to standards are effective for annual periods beginning after January 1, 2014. However, the Group has not applied the following new or amended standards in preparing the consolidated financial statements. Unless otherwise stated, none of these are expected to have a significant impact on the Group's consolidated financial statements.

#### *Effective July 1, 2014*

- **Defined Benefit Plans: Employee Contributions (*Amendments to PAS 19*).** The amendments apply to contributions from employees or third parties to defined benefit plans. The objective of the amendments is to simplify the accounting for contributions that are independent of the number of years of employee service, for example, employee contributions that are calculated according to a fixed percentage of salary.

The amendments apply retrospectively for annual periods beginning on or after July 1, 2014. Earlier application is permitted.

- **Annual Improvements to PFRS: 2010 - 2012 and 2011 - 2013 Cycles - Amendments** were made to a total of nine standards, with changes made to the standards on business combinations and fair value measurement in both cycles. Most amendments will apply prospectively for annual periods beginning on or after July 1, 2014. Earlier application is permitted, in which case the related consequential amendments to other PFRS would also apply. Special transitional requirements have been set for amendments to the following standards: PFRS 2, *Share-based Payment*, PAS 16, *Property, Plant and Equipment*, PAS 38, *Intangible Assets*, and PAS 40, *Investment Property*. The following are the said improvements or amendments to PFRS which are applicable to the Group:
  - **Meaning of 'Vesting Condition' (*Amendment to PFRS 2*).** PFRS 2 has been amended to clarify the definition of 'vesting condition' by separately defining 'performance condition' and 'service condition.' The amendment also clarifies both: how to distinguish between a market and a non-market performance condition; and the basis on which a performance condition can be differentiated from a non-vesting condition.
  - **Scope Exclusion for the Formation of Joint Arrangements (*Amendment to PFRS 3, Business Combinations*).** PFRS 3 has been amended to clarify that the standard does not apply to the accounting for the formation of all types of joint arrangements in PFRS 11, *Joint Arrangements*, - i.e. including joint operations - in the financial statements of the joint arrangements themselves.
  - **Disclosures on the Aggregation of Operating Segments (*Amendment to PFRS 8, Operating Segments*).** PFRS 8 has been amended to explicitly require the disclosure of judgments made by management in applying the aggregation criteria. The disclosures include: (i) a brief description of the operating segments that have been aggregated; and (ii) the economic indicators that have been assessed in determining that the operating segments share similar economic characteristics. In addition, the amendments clarify that a reconciliation of the total of the reportable segments' assets to the entity's assets is required only if this information is regularly provided to the entity's chief operating decision maker. This change aligns the disclosure requirements with those for segment liabilities.

- Scope of Portfolio Exception (*Amendment to PFRS 13*). The scope of the PFRS 13 portfolio exception - whereby entities are exempted from measuring the fair value of a group of financial assets and financial liabilities with offsetting risk positions on a net basis if certain conditions are met - has been aligned with the scope of PAS 39 and PFRS 9.

PFRS 13 has been amended to clarify that the portfolio exception potentially applies to contracts in the scope of PAS 39 and PFRS 9 regardless of whether they meet the definition of a financial asset or financial liability under PAS 32, *Financial Instruments: Presentation*, - e.g. certain contracts to buy or sell non-financial items that can be settled net in cash or another financial instrument.

- Definition of 'Related Party' (*Amendment to PAS 24*). The definition of a 'related party' is extended to include a management entity that provides key management personnel (KMP) services to the reporting entity, either directly or through a group entity. For related party transactions that arise when KMP services are provided to a reporting entity, the reporting entity is required to separately disclose the amounts that it has recognized as an expense for those services that are provided by a management entity; however, it is not required to 'look through' the management entity and disclose compensation paid by the management entity to the individuals providing the KMP services. The reporting entity will also need to disclose other transactions with the management entity under the existing disclosure requirements of PAS 24, *Related Party Disclosures*.

*Effective January 1, 2016*

- Clarification of Acceptable Methods of Depreciation and Amortization (*Amendments to PAS 16 and PAS 38*). The amendments to PAS 38 introduce a rebuttable presumption that the use of revenue-based amortization methods for intangible assets is inappropriate. This presumption can be overcome only when revenue and the consumption of the economic benefits of the intangible asset are 'highly correlated', or when the intangible asset is expressed as a measure of revenue.

The amendments to PAS 16 explicitly state that revenue-based methods of depreciation cannot be used for property, plant and equipment. This is because such methods reflect factors other than the consumption of economic benefits embodied in the asset - e.g. changes in sales volumes and prices.

The amendments are effective for annual periods beginning on or after January 1, 2016, and are to be applied prospectively. Early application is permitted.

- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (*Amendments to PFRS 10 and PAS 28*). The amendments address an inconsistency between the requirements in PFRS 10, *Consolidated Financial Statements*, and in PAS 28, *Investments in Associates and Joint Ventures*, in dealing with the sale or contribution of assets between an investor and its associate or joint venture.

The amendments require that a full gain or loss is recognized when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary.

The amendments apply prospectively for annual periods beginning on or after January 1, 2016. Early adoption is permitted.

*Effective January 1, 2018*

- PFRS 9 (2014). PFRS 9 (2014) replaces PAS 39 and supersedes the previously published versions of PFRS 9 that introduced new classifications and measurement requirements (in 2009 and 2010) and a new hedge accounting model (in 2013). PFRS 9 includes revised guidance on the classification and measurement of financial assets, including a new expected credit loss model for calculating impairment, guidance on own credit risk on financial liabilities measured at fair value and supplements the new general hedge accounting requirements published in 2013. PFRS 9 incorporates new hedge accounting requirements that represent a major overhaul of hedge accounting and introduces significant improvements by aligning the accounting more closely with risk management.

The new standard is to be applied retrospectively for annual periods beginning on or after January 1, 2018 with early adoption permitted.

The Group is assessing the potential impact on its consolidated financial statements resulting from the application of PFRS 9.

#### Financial Assets and Financial Liabilities

*Date of Recognition.* The Group recognizes a financial asset or a financial liability in the consolidated statements of financial position when it becomes a party to the contractual provisions of the instrument. In the case of a regular way purchase or sale of financial assets, recognition is done using trade date accounting.

*Initial Recognition of Financial Instruments.* Financial instruments are recognized initially at fair value of the consideration given (in case of an asset) or received (in case of a liability). The initial measurement of financial instruments, except for those designated as at fair value through profit or loss (FVPL), includes transaction costs.

The Group classifies its financial assets in the following categories: held-to-maturity (HTM) investments, available-for-sale (AFS) financial assets, financial assets at FVPL and loans and receivables. The Group classifies its financial liabilities as either financial liabilities at FVPL or other financial liabilities. The classification depends on the purpose for which the investments are acquired and whether they are quoted in an active market. Management determines the classification of its financial assets and financial liabilities at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

*‘Day 1’ Profit.* 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 Group recognizes the difference between the transaction price and the fair value (a ‘Day 1’ profit) in profit or loss unless it qualifies for recognition as some other type of asset. In cases where data used is not observable, the difference between the transaction price and model value is only recognized in profit or loss when the inputs become observable or when the instrument is derecognized. For each transaction, the Group determines the appropriate method of recognizing the ‘Day 1’ profit amount.

### Financial Assets

*Financial Assets at FVPL.* A financial asset is classified as at FVPL if it is classified as held for trading or is designated as such upon initial recognition. Financial assets are designated as at FVPL if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Derivative instruments (including embedded derivatives), except those covered by hedge accounting relationships, are classified under this category.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term.

Financial assets may be designated by management at initial recognition as at FVPL, when any of the following criteria is met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on a different basis;
- the assets are part of a group of financial assets which are managed and their performances are evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recognized.

The Group carries financial assets at FVPL using their fair values. Attributable transaction costs are recognized in profit or loss as incurred. Fair value changes and realized gains or losses are recognized in profit or loss. Fair value changes from derivatives accounted for as part of an effective cash flow hedge are recognized in other comprehensive income and presented in the consolidated statements of changes in equity. Any interest earned shall be recognized as part of "Interest income" account in the consolidated statements of income. Any dividend income from equity securities classified as at FVPL shall be recognized in profit or loss when the right to receive payment has been established.

As of December 31, 2014 and 2013, the Group has no financial assets accounted for under this category.

*Loans and Receivables.* Loans and receivables are non-derivative financial assets with fixed or determinable payments and maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not designated as AFS financial assets or financial assets at FVPL.

Subsequent to initial measurement, loans and receivables are carried at amortized cost using the effective interest rate method, less any impairment in value. Any interest earned on loans and receivables is recognized as part of "Interest income" account in the consolidated statements of income on an accrual basis. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The periodic amortization is also included as part of "Interest income" account in the consolidated statements of income. Gains or losses are recognized in profit or loss when loans and receivables are derecognized or impaired.

Cash includes cash on hand and in banks which are stated at face value. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

The Group's cash and cash equivalents, trade and other receivables, restricted cash and noncurrent receivable are included under this category (Notes 8, 9, 15 and 26).

*HTM Investments.* HTM investments are non-derivative financial assets with fixed or determinable payments and fixed maturities for which the Group's management has the positive intention and ability to hold to maturity. Where the Group sells other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS financial assets. After initial measurement, these investments are measured at amortized cost using the effective interest method, less impairment in value. Any interest earned on the HTM investments is recognized as part of "Interest income" account in the consolidated statements of income on an accrual basis. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The periodic amortization is also included as part of "Interest income" account in the consolidated statements of income. Gains or losses are recognized in profit or loss when the HTM investments are derecognized or impaired.

As of December 31, 2014 and 2013, the Group has no investments accounted for under this category.

*AFS Financial Assets.* AFS financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other financial asset categories. Subsequent to initial recognition, AFS financial assets are measured at fair value and changes therein, other than impairment losses and foreign currency differences on AFS debt instruments, are recognized in other comprehensive income and presented in the "Fair value reserves" account in the consolidated statements of changes in equity. The effective yield component of AFS debt securities is reported as part of "Interest income" account in the consolidated statements of income. Dividends earned on holding AFS equity securities are recognized as dividend income when the right to receive the payment has been established. When individual AFS financial assets are either derecognized or impaired, the related accumulated unrealized gains or losses previously reported in equity are transferred to and recognized in profit or loss.

AFS financial assets also include unquoted equity instruments with fair values which cannot be reliably determined. These instruments are carried at cost less impairment in value, if any.

As of December 31, 2014 and 2013, the Group has no financial assets accounted for under this category.

#### Financial Liabilities

*Financial Liabilities at FVPL.* Financial liabilities are classified under this category through the fair value option. Derivative instruments (including embedded derivatives) with negative fair values, except those covered by hedge accounting relationships, are also classified under this category.

The Group carries financial liabilities at FVPL using their fair values and reports fair value changes in profit or loss. Fair value changes from derivatives accounted for as part of an effective accounting hedge are recognized in other comprehensive income and presented in the consolidated statements of changes in equity. Any interest expense incurred is recognized as part of “Interest expense and other financing charges” account in the consolidated statements of income.

As of December 31, 2014 and 2013, the Group has no financial liabilities accounted for under this category.

*Other Financial Liabilities.* This category pertains to financial liabilities that are not designated or classified as at FVPL. After initial measurement, other financial liabilities are carried at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any premium or discount and any directly attributable transaction costs that are considered an integral part of the effective interest rate of the liability.

The Group’s liabilities arising from its trade or borrowings such as accounts payable and accrued expenses (excluding statutory payables), finance lease liabilities and long-term debt are included under this category (Notes 7, 16, 17 and 26).

#### Embedded Derivatives

The Group assesses whether embedded derivatives are required to be separated from the host contracts when the Group becomes a party to the contract.

An embedded derivative is separated from the host contract and accounted for as a derivative if all of the following conditions are met: a) the economic characteristics and risks of the embedded derivative are not 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 or combined instrument is not recognized as at FVPL. 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.

#### Derecognition of Financial Assets and Financial Liabilities

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

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

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the Group continues to recognize the transferred asset to the extent of the Group’s continuing involvement. In that case, the Group also recognizes the associated liability. The transferred asset and the associated liability are measured on the basis that reflects the rights and obligations that the Group has retained.

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

#### Impairment of Financial Assets

The Group assesses, at the reporting date, whether there is objective evidence that 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 have 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.

*Assets Carried at Amortized Cost.* For financial assets carried at amortized cost such as loans and receivables, the Group first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If no objective evidence of impairment has been identified for a particular financial asset that was individually assessed, the Group includes the asset as part of a group of financial assets with similar credit risk characteristics and collectively assesses the group for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in the collective impairment assessment.

Evidence of impairment for specific impairment purposes may include indications that the borrower or a group of borrowers is experiencing financial difficulty, default or delinquency in principal or interest payments, or may enter into bankruptcy or other form of financial reorganization intended to alleviate the financial condition of the borrower. For collective impairment purposes, evidence of impairment may include observable data on existing economic conditions or industry-wide developments indicating that there is a measurable decrease in the expected future cash flows of the related assets.

If there is objective evidence of impairment, the amount of 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) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). Time value is generally not considered when the effect of discounting the cash flows is not material. If a loan or receivable has a variable rate, the discount rate for measuring any impairment loss is the current effective interest rate, adjusted for the original credit risk premium. For collective impairment purposes, impairment loss is computed based on their respective default and historical loss experience.

The carrying amount of the asset shall be reduced either directly or through the use of an allowance account. The impairment loss for the period shall be recognized in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. Any subsequent reversal of an impairment loss is recognized in profit or loss, to the extent that the carrying amount of the asset does not exceed its amortized cost at the reversal date.

*AFS Financial Assets.* For equity instruments carried at fair value, the Group assesses, at each reporting date, whether objective evidence of impairment exists. Objective evidence of impairment includes a significant or prolonged decline in the fair value of an equity instrument below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' is evaluated against the period in which the fair value has been below its original cost. The Group generally regards fair value decline as being significant when decline exceeds 25%. A decline in a quoted market price that persists for 12 months is generally considered to be prolonged.

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

In the case of an unquoted equity instrument or of a derivative asset linked to and must be settled by delivery of an unquoted equity instrument, for which its fair value cannot be reliably measured, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of expected future cash flows from the asset discounted using the historical effective rate of return on the asset.

#### Classification of Financial Instruments between Debt and Equity

From the perspective of the issuer, a financial instrument is classified as debt instrument if it provides for a contractual obligation to:

- deliver cash or another financial asset to another entity;
- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Group; or
- satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares

If the Group does not have an unconditional right to avoid delivering cash or another financial asset to settle its contractual obligation, the obligation meets the definition of a financial liability.

#### Debt Issue Costs

Debt issue costs are considered as an adjustment to the effective yield of the related debt and are deferred and amortized using the effective interest method. When a loan is paid, the related unamortized debt issue costs at the date of repayment are recognized in profit or loss.

#### Offsetting Financial Instruments

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

### Inventories

Inventories are measured at the lower of cost and net realizable value. Cost is determined using first-in-first-out method for materials and supplies, specific identification method or moving average method for coal inventories and moving average method for fuel oil and other consumables. Net realizable value is the current replacement cost.

### Business Combination

Business combinations are accounted for using the acquisition method as of the acquisition date. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interests in the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree at fair value or at proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

When the Group acquires a business, it assesses the financial assets and financial liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured at the acquisition date fair values and any resulting gain or loss is recognized in profit or loss.

The Group measures goodwill at the acquisition date as: a) the fair value of the consideration transferred; plus b) the recognized amount of any non-controlling interests in the acquiree; plus c) if the business combination is achieved in stages, the fair value of the existing equity interest in the acquiree; less d) the net recognized amount (generally fair value) of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognized immediately in profit or loss. Subsequently, goodwill is measured at cost less any accumulated impairment in value. Goodwill is reviewed for impairment, annually or more frequently, if events or changes in circumstances indicate that the carrying amount may be impaired.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognized in profit or loss. Costs related to acquisition, other than those associated with the issue of debt or equity securities that the Group incurs in connection with a business combination, are expensed as incurred. Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognized in profit or loss.

#### ▪ *Goodwill in a Business Combination*

Goodwill acquired in a business combination is, from the acquisition date, allocated to each of the cash-generating units, or groups of cash-generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than an operating segment determined in accordance with PFRS 8.

Impairment is determined 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, an impairment loss is recognized. Where goodwill forms part of a cash-generating unit or group of cash-generating units 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 this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained. An impairment loss with respect to goodwill is not reversed.

▪ *Intangible Asset Acquired in a Business Combination*

The cost of an intangible asset acquired in a business combination is the fair value as of the date of acquisition, determined using discounted cash flows as a result of the asset being owned.

Following initial recognition, intangible asset is carried at cost less accumulated amortization and any impairment losses. The useful life of intangible asset is assessed to be either finite or indefinite.

An intangible asset with finite life is amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each reporting date. A change in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for as a change in accounting estimates. The amortization expense on intangible asset with finite life is recognized in profit or loss.

▪ *Loss of Control*

On the loss of control, the Group derecognizes the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognized in profit or loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently, it is accounted for as an equity-accounted investee or as an AFS financial asset depending on the level of influence retained.

Transactions under Common Control

Transactions under common control entered into in contemplation of each other and business combination under common control designed to achieve an overall commercial effect are treated as a single transaction.

Transfers of assets between commonly controlled entities are accounted for using book value accounting.

Non-controlling Interests

The acquisitions of non-controlling interests are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognized as a result of such transactions. Any difference between the purchase price and the net assets of acquired entity is recognized in equity. The adjustments to non-controlling interests are based on a proportionate amount of the identifiable net assets of the subsidiary.

### Investments in an Associate and Joint Venture

An associate is an entity in which the Group has significant influence. Significant influence is the power to participate in the financial and operating policies of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The considerations made in determining significant influence or joint control is similar to those necessary to determine control over subsidiaries.

The Group's investments in an associate and joint venture are accounted for using the equity method.

Under the equity method, the investment in an associate or joint venture is initially recognized at cost. The carrying amount of the investment is adjusted to recognize the changes in the Group's share of net assets of the associate or joint venture since the acquisition date. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortized nor individually tested for impairment.

The Group's share in the profit or loss of the associate or joint venture is recognized as "Equity in net earnings (losses) of associates and joint ventures - net" account in the consolidated statements of income. Adjustments to the carrying amount may also be necessary for changes in the Group's proportionate interest in the associate or joint venture arising from the changes in the associate or joint venture's other comprehensive income. The Group's share of those changes is recognized as "Share in other comprehensive income of an associate" account in the consolidated statements of comprehensive income. Unrealized gains and losses resulting from transactions between the Group and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.

After application of the equity method, the Group determines whether it is necessary to recognize an impairment loss with respect to the Group's net investment in the associate or joint venture. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate or joint venture is impaired. If there is such evidence, the Group recalculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying amount. Such impairment loss is recognized as part of "Equity in net earnings (losses) of associates and joint ventures - net" account in the consolidated statements of income.

Upon loss of significant influence over the associate or joint control over the joint venture, the Group measures and recognizes any retained investment at fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control, and the fair value of the retained investment and proceeds from disposal is recognized in profit or loss.

The financial statements of the associate or joint venture are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

### Property, Plant and Equipment

Property, plant and equipment are measured at cost less accumulated depreciation and amortization, and any accumulated impairment in value. Such cost includes the cost of replacing part of the property, plant and equipment at the time that cost is incurred, if the recognition criteria are met, and excludes the costs of day-to-day servicing.

The initial cost of property, plant and equipment comprises of its construction cost or purchase price, including import duties, taxes and any directly attributable costs in bringing the asset to its working condition and location for its intended use. Cost also includes any related asset retirement obligation (ARO). Expenditures incurred after the asset has been put into operation, such as repairs, maintenance and overhaul costs, are normally recognized as expense in the period the costs are incurred. Major repairs are capitalized as part of property, plant and equipment only when it is probable that future economic benefits associated with the items will flow to the Group and the cost of the items can be measured reliably.

Construction in progress (CIP) represents structures under construction and is stated at cost. This includes the costs of construction and other direct costs. Borrowing costs that are directly attributable to the construction of plant and equipment are capitalized during the construction period. CIP is not depreciated until such time that the relevant assets are ready for use.

Depreciation and amortization, which commences when the assets are available for their intended use, are computed using the straight-line method over the following estimated useful lives of the assets:

|                        | Number of Years                              |
|------------------------|----------------------------------------------|
| Power plants           | 10 - 43                                      |
| Building               | 15 - 25                                      |
| Other equipment        | 2 - 15                                       |
| Leasehold improvements | 5 - 10                                       |
|                        | or term of the lease<br>whichever is shorter |

The remaining useful lives, residual values, and depreciation and amortization methods are reviewed and adjusted periodically, if appropriate, to ensure that such periods and method of depreciation and amortization are consistent with the expected pattern of economic benefits from the items of property, plant and equipment.

The carrying amount of property, plant and equipment is reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

Fully depreciated assets are retained in the accounts until they are no longer in use.

An item of property, plant and equipment is derecognized when either it has been disposed of or when it is permanently withdrawn from use and no future economic benefits are expected from its use or disposal. Any gain or loss arising from the retirement and disposal of an item of property, plant and equipment (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period of retirement and disposal.

### Intangible Assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is its fair value as at the date of acquisition. Subsequently, intangible assets are measured at cost less accumulated amortization and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditures are recognized in profit or loss in the year in which the related expenditures are incurred. The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortized over the useful life and assessed for impairment whenever there is an indication that the intangible assets may be impaired. The amortization period and the amortization method used 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 pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimate. The amortization expense on intangible assets with finite lives is recognized in profit or loss consistent with the function of the intangible asset.

|                                | Number of Years |
|--------------------------------|-----------------|
| Concession right               | 25              |
| Computer software and licenses | 2 - 8           |

Gains or losses arising from the disposal 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 profit or loss when the asset is derecognized.

### *Intangible Asset - Power Concession Right*

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

The Interpretation applies to both: (a) infrastructure that the entities in the Group constructs or acquires from a third party for the purpose of the service arrangement; and (b) existing infrastructure to which the grantor gives the entity in the Group access for the purpose of the service agreement.

Infrastructures within the scope of the Interpretation are not recognized as property, plant and equipment of the Group. Under the terms of the contractual arrangements within the scope of the Interpretation, an entity (the company created by the Concession Agreement) acts as a service provider. An entity constructs or upgrades infrastructure (construction or upgrade services) used to provide a public service and operates and maintains that infrastructure (operation services) for a specified period of time.

The useful lives of power concession right are assessed to be either finite or indefinite. Power concession right arising from a service concession arrangement is amortized using straight-line method over the concession period, which is 25 years from the first day of the commencement of operations, or the estimated useful lives of the infrastructure, whichever is lower, and assessed for impairment whenever there is an indication that the asset may be impaired. The amortization period and the amortization method are reviewed annually. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the concession assets are treated as changes in accounting estimates. The amortization expense is recognized in profit or loss in the expense category consistent with the function of the concession assets.

The power concession right is derecognized on disposal or when no further economic benefits are expected from its use or disposal. Gains or losses arising from derecognition of concession assets are recognized in profit or loss and measured as the difference between the net disposal proceeds and the carrying amount of the concession assets.

The Group's power concession right pertains to the right granted by the Government to the Parent Company to operate the Albay Electric Cooperative, Inc. (ALECO). The power concession right is carried at cost less accumulated amortization and any accumulated impairment losses.

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

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

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

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

In accordance with PAS 23, *Borrowing Costs*, borrowing costs attributable to the arrangement are recognized as an expense in the period in which they are incurred unless the applicable entities have a contractual right to receive an intangible asset (a right to charge users of the public service). In this case, borrowing costs attributable to the arrangement are capitalized during the construction phase of the arrangement.

### *Intangible Assets - Mining Rights*

The Group's mining rights that are acquired by the Group and have finite lives are measured at costs less accumulated amortization and any accumulated impairment losses.

Subsequent expenditures are capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditures are recognized in profit or loss as incurred.

Amortization of mining rights is recognized in profit or loss on a straight-line basis over the estimated useful lives. The estimated useful lives of mining rights pertain the period from commercial operations to the end of the operating contract. Amortization method and useful lives are reviewed at each reporting date and adjusted as appropriate.

Gains or loss from derecognition of mining rights are measured as the difference between the net disposal proceeds and the carrying amount of the asset, and is recognized in profit or loss.

### Deferred Exploration and Development Costs

Deferred exploration and development costs comprise of expenditures which are directly attributable to:

- Researching and analyzing existing exploration data;
- Conducting geological studies, exploratory drilling and sampling;
- Examining and testing extraction and treatment methods; and
- Compiling pre-feasibility and feasibility studies.

Deferred exploration and development costs also include expenditures incurred in acquiring mining rights, entry premiums paid to gain access to areas of interest and amounts payable to third parties to acquire interests in existing projects.

Exploration assets are reassessed on a regular basis and tested for impairment provided that at least one of the following conditions is met:

- the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned;
- such costs are expected to be recouped in full through successful development and exploration of the area of interest or alternatively, by its sale; or
- exploration and evaluation activities in the area of interest have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active and significant operations in relation to the area are continuing, or planned for the future.

If the project proceeds to development stage, the amounts included within deferred exploration and development costs are transferred to property, plant and equipment under mine development costs.

#### Impairment of Non-financial Assets

The carrying amounts of property, plant and equipment, investments and advances, deferred exploration and development costs and goodwill and other intangible assets with finite useful lives reviewed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable. If any such indication exists, and if the carrying amount exceeds the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amounts. The recoverable amount of the asset is the greater of fair value less costs of disposal and value in use. The fair value less costs of disposal is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less costs of disposal. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. 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 that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation and amortization, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss. After such a reversal, the depreciation and amortization charge 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.

#### Concession Payable

Concession payable is recognized at the date of inception of the concession agreement. Fixed concession fees are recognized at present value using the discount rate at the inception date. This account is debited upon payment of fixed fees and such payments are apportioned between interest payment and payment of the principal. Interest arising from the accretion of concession payable is presented under "Interest expense and other financing charges" account in the consolidated statements of income.

Concession payable that are expected to be settled within 12 months after the reporting date are classified as current liabilities. Otherwise, these are classified as noncurrent liabilities.

#### Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or most advantageous market must be accessible to the Group.

The fair value of an asset or liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their best economic interest.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

For assets and liabilities that are recognized in the consolidated financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing the categorization at the end of each reporting period.

For purposes of the fair value disclosure, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of fair value hierarchy, as explained above.

#### Provisions

Provisions are recognized when: (a) the Group has a present obligation (legal or constructive) as a result of past events; (b) it is probable (i.e., more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessment of the time value of money and the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as interest expense. Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset. The amount recognized for the reimbursement shall not exceed the amount of the provision. Provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

#### Share Capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares are recognized as a deduction from equity, net of any tax effects.

#### Undated Subordinated Capital Securities

Undated subordinated capital securities are classified as equity when there is no contractual obligation to deliver cash or other financial assets to another person or entity or to exchange financial assets or financial liabilities with another person or entity that is potentially unfavorable to the issuer.

Incremental costs directly attributable to the issuance of undated subordinated capital securities are recognized as a deduction from equity, net of tax. The proceeds received net of any directly attributable transaction costs are credited to undated subordinated capital securities.

#### Revenue Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the amount of the revenue can be reliably measured. Revenues are stated at amounts invoiced to customers, inclusive of pass-through charges, net of value-added tax (VAT) and other taxes. The following specific recognition criteria must also be met before revenue is recognized:

*Sale of Power.* Revenue from power generation is recognized in the period when actual power or capacity is generated, transmitted or/and made available to the customers, net of related discounts.

*Sale of Electricity.* Revenues are recognized upon the supply of power to the customers. The Uniform Filing Requirements (UFR) on the rate unbundling released by the Energy Regulatory Commission (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 I and II, where applicable and (h) interclass and life subsidies. VAT, local franchise tax and universal charges are billed and collected on behalf of the national and local government and do not form part of the Group's revenue. Generation, transmission and system loss charges, which are part of revenues, are pass-through charges.

*Interest Income.* Revenue is recognized as the interest accrues, taking into account the effective yield on the asset.

*Dividend.* Dividend income is recognized when the Group's right as a shareholder to receive the payment is established.

*Gain or Loss on Sale of Investments in Shares of Stock.* Gain or loss is recognized if the Group disposes of its investments in a subsidiary, associate or joint venture. Gain or loss is computed as the difference between the proceeds of the disposed investment and its carrying amount, including the carrying amount of goodwill, if any.

#### Cost and Expense Recognition

*Costs and Expenses.* Costs and expenses are recognized upon receipt of goods, utilization of services or at the date they are incurred. Cost of power sold is debited for the direct costs related to power generation, retail and distribution of electricity, or/and trading.

*Interest Expense and Other Financing Charges.* Interest expense and other financing charges comprise finance charges on finance lease liabilities, loans, concession payable and other borrowings. Finance charges on finance lease liabilities, loans and concession payable are recognized in profit or loss using the effective interest method.

*Short-term Employee Benefits.* Short-term employee benefits are expensed as the related service is provided. A liability is recognized for the amount expected to be paid if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

### Share-based Payment Transactions

Under SMC's Employee Stock Purchase Plan (ESPP), employees of the Group receive remuneration in the form of share-based payment transactions, whereby the employees render services as consideration for equity instruments of SMC. Such transactions are handled centrally by SMC.

Share-based transactions in which SMC grants option rights to its equity instruments direct to the Group's employees are accounted for as equity-settled transactions. SMC charges the Group for the costs related to such transactions with its employees. The amount is charged to operations by the Group.

The cost of ESPP is measured by reference to the market price at the time of the grant less subscription price. The cumulative expense recognized for share-based transactions at each reporting date until the date when the relevant employees become fully entitled to the award (the "vesting date") reflects the extent to which the vesting period has expired and SMC's best estimate of the number of equity instruments that will ultimately vest.

Where the terms of a share-based award are modified, as a minimum, an expense is recognized as if the terms had not been modified. In addition, an expense is recognized for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification. Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award.

### Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset. A reassessment is made after the inception of the lease only if one of the following applies:

- (a) there is a change in contractual terms, other than a renewal or extension of the arrangement;
- (b) a renewal option is exercised or an extension granted, unless the term of the renewal or extension was initially included in the lease term;
- (c) there is a change in the determination of whether fulfillment is dependent on a specific asset; or
- (d) there is a substantial change to the asset.

Where a reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gives rise to the reassessment for scenarios (a), (c) or (d), and at the date of renewal or extension period for scenario (b) above.

#### *Finance Lease*

Finance leases, which transfer to the Group substantially all the risks and rewards incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Obligations arising from plant assets under finance lease agreement are classified in the consolidated statements of financial position as finance lease liabilities.

Lease payments are apportioned between the financing charges and reduction of the lease liabilities so as to achieve a constant rate of interest on the remaining balance of the liabilities. Financing charges are recognized in profit or loss.

Capitalized leased assets are depreciated over the estimated useful lives of the assets when there is reasonable certainty that the Group will obtain ownership by the end of the lease term.

#### Operating Lease

*Group as Lessee.* Leases which do not transfer to the Group substantially all the risks and rewards of ownership of the assets are classified as operating leases. Operating lease payments are recognized as an expense in profit or loss on a straight-line basis over the lease term. Associated costs such as maintenance and insurance are expensed as incurred.

*Group as Lessor.* Leases where the Group does not transfer substantially all the risks and rewards of ownership of the assets are classified as operating leases. Rent income from operating lease is recognized as income on a straight-line basis over the lease term. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized as an expense over the lease term on the same basis as rent income. Contingent rents are recognized as income in the period in which they are earned.

#### Borrowing Costs

Borrowing costs are capitalized if they are directly attributable to the acquisition or construction of a qualifying asset. Capitalization of borrowing costs commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Borrowing costs are capitalized until the assets are substantially ready for their intended use.

#### Foreign Currency Translations

Transactions in foreign currencies are translated to the functional currency of the Group at exchange rates at the dates of the transactions. Monetary assets and monetary liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortized cost in foreign currency translated at the exchange rate at the reporting date.

#### Taxes

*Current Tax.* Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

*Deferred Tax.* Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- with respect to taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, carryforward benefits of unused tax credits - Minimum Corporate Income Tax (MCIT) and unused tax losses - Net Operating Loss Carry Over (NOLCO), to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward benefits of MCIT and NOLCO can be utilized, except:

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

The carrying amount of deferred tax assets is reviewed at each 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 tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

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

In determining the amount of current and deferred tax, the Group takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretation of tax laws and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Group to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact tax expense in the period that such a determination is made.

Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

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

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

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

The net amount of tax recoverable from, or payable to, the taxation authority is included as part of “Prepaid expenses and other current assets”, “Other noncurrent assets” or “Accounts payable and accrued expenses” accounts in the consolidated statements of financial position.

#### Related Parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control and significant influence. Related parties may be individuals or corporate entities. Transactions between related parties are on an arm’s length basis in a manner similar to transactions with non-related parties.

#### Basic and Diluted Earnings Per Share (EPS)

Basic EPS is computed by dividing the net income for the period attributable to equity holders of the Parent Company by the weighted-average number of issued and outstanding common shares during the period.

For the purpose of computing diluted EPS, the net income for the period attributable to equity holders of the Parent Company and the weighted-average number of issued and outstanding common shares are adjusted for the effects of all potential dilutive instruments.

As at December 31, 2014 and 2013, the Group has no dilutive equity instruments as disclosed in Note 24 to the consolidated financial statements.

#### Operating Segments

The Group’s operating segments are organized and managed separately based on the fuel source of the power plants, with each segment representing a strategic business unit that has different economic characteristic and activities. The BOD (the chief operating decision maker; CODM) reviews management reports on a regular basis.

The measurement policies the Group used for segment reporting under PFRS 8 are the same as those used in its consolidated financial statements. There have been no changes in the measurement methods used to determine reported segment profit or loss from prior periods. All inter-segment transfers are carried out at arm’s length prices.

Segment revenues, expenses and performance include sales and purchases between business segments. Such sales and purchases are eliminated in consolidation.

#### Contingencies

Contingent liabilities are not recognized in the consolidated financial statements. They are disclosed in the notes to the consolidated financial statements unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the consolidated financial statements but are disclosed in the notes to the 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 Group's financial position at the reporting date (adjusting events) are reflected in the consolidated financial statements. Post year-end events that are not adjusting events are disclosed in the notes to the consolidated financial statements when material.

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### **4. Significant Accounting Judgments, Estimates and Assumptions**

The preparation of the consolidated financial statements in accordance with PFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the amounts of assets, liabilities, income and expenses reported in the consolidated financial statements at the reporting date. However, uncertainty about these judgments, estimates and assumptions could result in an outcome that could require a material adjustment to the carrying amount of the affected asset or liability in the future.

Judgments and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions are recognized in the period in which the judgments and estimates are revised and in any future period affected.

#### Judgments

In the process of applying the Group's accounting policies, management has made the following judgments, apart from those involving estimations, which have the most significant effect on the amounts recognized in the consolidated financial statements:

*Finance Lease - Group as Lessee.* In accounting for its Independent Power Producer Administration (IPPA) Agreements with Power Sector Assets and Liabilities Management Corporation (PSALM), the Group's management has made a judgment that the IPPA Agreements are agreements that contain a lease.

The Group's management has made a judgment that it has substantially acquired all the risks and rewards incidental to the ownership of the power plants. Accordingly, the Group accounted for the agreements as a finance lease and recognized the power plants and finance lease liabilities at the present value of the agreed monthly payments to PSALM (Notes 7 and 12).

Finance lease liabilities recognized in the consolidated statements of financial position amounted to P186,303,745 and P195,002,721 as of December 31, 2014 and 2013, respectively (Note 7).

The combined carrying amounts of power plants under finance lease amounted to P188,132,700 and P193,319,103 as of December 31, 2014 and 2013, respectively (Note 12).

*Operating Lease Commitments - Group as Lessor/Lessee.* The Group has entered into various lease agreements either as a lessor or a lessee. The Group has determined that it retains all the significant risks and rewards of ownership of the property leased out on operating leases while the significant risks and rewards for property leased from third parties are retained by the lessors (Note 7).

Rent income recognized in the consolidated statements of income amounted to P18,434 and nil in 2014 and 2013, respectively.

Rent expense recognized in the consolidated statements of income amounted to P115,849 and P24,167 in 2014 and 2013, respectively (Note 20).

*Applicability of Philippine Interpretation IFRIC 12 - Concession Right.* In accounting for the Group's transactions in connection with its Concession Agreement with ALECO, significant judgment was applied to determine the most appropriate accounting policy to use.

Management used Philippine Interpretation IFRIC 12 as guide and determined that the Concession Agreement is within the scope of the Interpretation and should be accounted for under the intangible asset model (Notes 3, 7 and 14).

*Contingencies.* The Group is currently involved in various pending claims and cases which could be decided in favor of or against the Group. The Group's estimate of the probable costs for the resolution of these pending claims and cases has been developed in consultation with in-house as well as outside legal counsel handling the prosecution and defense of these matters and is based on an analysis of potential results. The Group's management and legal counsels currently do not believe that these pending claims and cases will have a material adverse effect on its financial position and financial performance. It is possible, however, that future financial performance could be materially affected by the changes in the estimates or in the effectiveness of strategies relating to these proceedings (Note 27).

#### Estimates and Assumptions

The key estimates and assumptions used in the consolidated financial statements are based upon management's evaluation of relevant facts and circumstances as of the date of the consolidated financial statements. Actual results could differ from such estimates.

*Fair Value Measurements.* A number of the Group's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Group has an established control framework with respect to the measurement of fair values. This includes a valuation team that has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values. The valuation team regularly reviews significant unobservable inputs and valuation adjustments. If third party information is used to measure fair values, then the valuation team assesses the evidence obtained to support the conclusion that such valuations meet the requirements of PFRS, including the level in the fair value hierarchy in which such valuations should be classified.

The Group uses market observable data when measuring the fair value of an asset or liability. Fair values are categorized into different levels in a fair value hierarchy based on the inputs used in the valuation techniques (Note 3).

If the inputs used to measure the fair value of an asset or a liability may be categorized in different levels of the fair value hierarchy, then the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy based on the lowest level input that is significant to the entire measurement.

The Group recognizes transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

The methods and assumptions used to estimate the fair values for both financial and non-financial assets and liabilities are discussed in Note 26.

The Group has no financial asset or financial liability carried at fair values as of December 31, 2014 and 2013.

*Allowance for Impairment Losses on Trade and Other Receivables.* Provisions are made for specific and groups of accounts, where objective evidence of impairment exists. The Group evaluates these accounts on the basis of factors that affect the collectibility of the accounts. These factors include, but are not limited to, the length of the Group's relationship with the customers and counterparties, the customers' current credit status based on third party credit reports and known market forces, average age of accounts, collection experience and historical loss experience. The amount and timing of the recorded expenses for any period would differ if the Group made different judgments or utilized different methodologies. An increase in allowance for impairment losses would increase the recorded operating expenses and decrease current assets.

The allowance for impairment losses on trade and other receivables amounted to P866,686 and P722,293 as of December 31, 2014 and 2013, respectively. The carrying amount of trade and other receivables amounted to P18,208,339 and P31,540,444 as of December 31, 2014 and 2013, respectively (Note 9).

*Write-down of Inventory.* The Group writes-down the cost of inventory to its net realizable value whenever net realizable value becomes lower than cost due to damage, physical deterioration, obsolescence, changes in price levels or other causes.

Estimates of net realizable value are based on the most reliable evidence available at the time the estimates are made of the amount the inventories are expected to be realized. These estimates take into consideration fluctuations of price or cost directly relating to events occurring after the reporting date to the extent that such events confirm conditions existing at the reporting date.

The Group assessed that no write-down of inventories to reduce inventories to net realizable value is necessary as of December 31, 2014 and 2013.

The carrying amount of inventories amounted to P1,365,033 and P1,499,135 as of December 31, 2014 and 2013, respectively (Note 10).

*Estimated Useful Lives of Property, Plant and Equipment.* The Group estimates the useful lives of property, plant and equipment based on the period over which the assets are expected to be available for use. The estimated useful lives of property, plant and equipment are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the assets.

In addition, estimation of the useful lives of property, plant and equipment is based on collective assessment of industry practice, internal technical evaluation and experience with similar assets. It is possible, however, that future financial performance could be materially affected by changes in estimates brought about by changes in factors mentioned above. 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 property, plant and equipment would increase the recorded cost and expenses and decrease noncurrent assets.

Property, plant and equipment, net of accumulated depreciation and amortization amounted to P228,133,323 and P217,021,519 as of December 31, 2014 and 2013, respectively. Accumulated depreciation and amortization of property, plant and equipment amounted to P27,404,427 and P21,233,181 as of December 31, 2014 and 2013, respectively (Note 12).

*Estimated Useful Lives of Intangible Assets.* The useful lives of intangible assets are assessed at the individual asset level as having either a finite or indefinite life. Intangible assets are regarded to have an indefinite useful life when, based on analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the Group.

Intangible assets with finite useful lives amounted to P2,313,375 and P1,719,726 as of December 31, 2014 and 2013, respectively (Note 14).

*Impairment of Goodwill.* The Group determines whether the goodwill acquired in business combination are impaired at least annually. This requires the estimation of value in use of the cash-generating units to which the goodwill is allocated. Estimating value in use requires management to make an estimate of the expected future cash flows from the cash-generating unit and to choose a suitable discount rate to calculate the present value of those cash flows.

The carrying amount of goodwill amounted to P8,866 as of December 31, 2014 and 2013 (Note 14).

*Acquisition Accounting.* The Group accounts for acquired businesses using the acquisition method of accounting which requires that the assets acquired and the liabilities assumed be recognized at the date of acquisition based on their respective fair values.

The application of the acquisition method requires certain estimates and assumptions especially concerning the determination of the fair values of acquired property, plant and equipment and intangible assets as well as liabilities assumed at the acquisition date. Moreover, the useful lives of the acquired property, plant and equipment and intangible assets have to be determined. Accordingly, for significant acquisitions, the Group obtains assistance from valuation specialists. The valuations are based on information available at the acquisition date.

*Recoverability of Deferred Exploration and Development Costs.* A valuation allowance is provided for estimated unrecoverable deferred exploration and development costs based on the Group's assessment of the future prospects of the mining properties, which are primarily dependent on the presence of economically recoverable reserves in those properties.

The Group's mining activities are all in the exploratory stages as of December 31, 2014. All related costs and expenses from exploration are currently deferred as exploration and development costs to be amortized upon commencement of commercial operations. The Group has not identified any facts and circumstances which suggest that the carrying amount of the deferred exploration and development costs exceeded the recoverable amounts as of December 31, 2014 and 2013.

Deferred exploration and development costs amounted to P671,783 and P525,999 as of December 31, 2014 and 2013, respectively (Note 6).

*Realizability of Deferred Tax Assets.* The Group reviews its deferred tax assets at each reporting date and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilized. The Group's assessment on the recognition of deferred tax assets on deductible temporary difference and carryforward benefits of MCIT and NOLCO is based on the projected taxable income in the following periods.

Deferred tax assets arising from MCIT and NOLCO have not been recognized because the management believes that it is not probable that future taxable income will be available against which the Group can utilize the benefits therefrom (Note 22).

Deferred tax assets from temporary differences amounted to P2,779,380 and P2,909,105 as of December 31, 2014 and 2013, respectively (Note 22).

*Impairment of Non-financial Assets.* PFRS requires that an impairment review be performed on property, plant and equipment, investments and advances, deferred exploration and development costs and goodwill and other intangible assets with finite useful lives when events or changes in circumstances indicate that the carrying amounts may not be recoverable. Determining the recoverable amount of these assets requires the estimation of cash flows expected to be generated from the continued use and ultimate disposition of such assets. While it is believed that the assumptions used in the estimation of fair values reflected in the consolidated financial statements are appropriate and reasonable, significant changes in these assumptions may materially affect the assessment of recoverable amounts and any resulting impairment loss could have a material adverse impact on the financial performance.

The Group assessed that its non-financial assets are not impaired as of December 31, 2014 and 2013.

The combined carrying amounts of property, plant and equipment, investments and advances, deferred exploration and development costs and other intangible assets with finite useful lives amounted to P241,730,758 and P225,279,043 as of December 31, 2014 and 2013, respectively (Notes 6, 12, 13 and 14).

*Asset Retirement Obligation.* Determining ARO requires estimation of the cost of dismantling property, plant and equipment and other costs of restoring the leased properties to their original condition. The Group determined that there are no ARO as of December 31, 2014 and 2013.

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## 5. Segment Information

### Operating Segments

The Group's operations are segmented based on fuel source of the power plants consistent with the reports prepared internally for use by the Group's CODM in reviewing the business performance of the operating segments. The differing economic characteristics and activities of these power plants make it more useful to users of the consolidated financial statements to have information about each component of the Group's profit or loss, assets and liabilities.

The coal mining companies, which were acquired in 2010, have not yet started commercial operations and are in the exploratory stage of mining activities (Note 6). The mining companies' total assets do not exceed 10% of the combined assets of all operating segments. Accordingly, management believes that as of December 31, 2014 and 2013, the information about this component of the Group would not be useful to the users of the consolidated financial statements.

The Group's inter-segment sales of power are accounted for based on contracts entered into by the parties and are eliminated in the consolidation. Segment assets do not include investments and advances, goodwill and other intangible assets and deferred tax assets. The investment in Manila Electric Company (Meralco) and subsequent transactions affecting investment in Meralco are presented under "Others". Segment liabilities do not include long-term debt, deferred tax liabilities and income tax payable. Capital expenditures consist of additions to property, plant and equipment of each reportable segment.

The Group operates only in the Philippines which is treated as a single geographical segment.

### Major Customers

The Group sells, retails and distributes power, through power supply agreements, retail supply agreements, concession agreement and other power related service agreements (Note 7), either directly to customers (other generators, distribution utilities, electric cooperatives and industrial customers) or through the Philippine Wholesale Electricity Spot Market (WESM). Sale, retail and/or distribution of power to individual external customers that represents 10% or more of the Group's total revenues is as follows:

| Customers | 2014               | 2013        |
|-----------|--------------------|-------------|
| Meralco   | <b>P47,233,747</b> | P46,952,999 |
| WESM      | <b>9,622,839</b>   | 10,770,643  |

For management reporting purposes, the Group's operating segments are organized and managed separately as follows:

### Operating Segments

Financial information about reportable segments follows:

|                                                                        | For the Years Ended December 31 |             |                                                    |          |                          |          |                  |           |                    |             |                     |              |
|------------------------------------------------------------------------|---------------------------------|-------------|----------------------------------------------------|----------|--------------------------|----------|------------------|-----------|--------------------|-------------|---------------------|--------------|
|                                                                        | Power Generation                |             | Retail and Other Power<br>Related Service Provider |          | Coal Mining<br>Companies |          | Others           |           | Eliminations       |             | Consolidated        |              |
|                                                                        | 2014                            | 2013        | 2014                                               | 2013     | 2014                     | 2013     | 2014             | 2013      | 2014               | 2013        | 2014                | 2013         |
| <b>Sale of Power</b>                                                   |                                 |             |                                                    |          |                          |          |                  |           |                    |             |                     |              |
| External                                                               | <b>P80,080,157</b>              | P73,882,922 | <b>P4,213,433</b>                                  | P160,865 | <b>P -</b>               | P -      | <b>P -</b>       | P -       | <b>P -</b>         | P -         | <b>P84,293,590</b>  | P74,043,787  |
| Inter-segment                                                          | <b>4,872,675</b>                | 2,103,653   | -                                                  | -        | -                        | -        | -                | -         | <b>(4,872,675)</b> | (2,103,653) | -                   | -            |
|                                                                        | <b>84,952,832</b>               | 75,986,575  | <b>4,213,433</b>                                   | 160,865  | -                        | -        | -                | -         | <b>(4,872,675)</b> | (2,103,653) | <b>84,293,590</b>   | 74,043,787   |
| <b>Cost and Expenses</b>                                               |                                 |             |                                                    |          |                          |          |                  |           |                    |             |                     |              |
| Cost of power sold                                                     | <b>56,304,969</b>               | 53,919,111  | <b>4,053,848</b>                                   | 139,164  | -                        | -        | -                | -         | <b>(4,872,675)</b> | (2,103,653) | <b>55,486,142</b>   | 51,954,622   |
| Operating expenses                                                     | <b>2,610,578</b>                | 1,635,443   | <b>37,204</b>                                      | 7,951    | <b>23,919</b>            | 15,345   | <b>855,229</b>   | 504,093   | <b>(615,000)</b>   | (615,082)   | <b>2,911,930</b>    | 1,547,750    |
|                                                                        | <b>58,915,547</b>               | 55,554,554  | <b>4,091,052</b>                                   | 147,115  | <b>23,919</b>            | 15,345   | <b>855,229</b>   | 504,093   | <b>(5,487,675)</b> | (2,718,735) | <b>58,398,072</b>   | 53,502,372   |
| <b>Segment Result</b>                                                  | <b>26,037,285</b>               | 20,432,021  | <b>122,381</b>                                     | 13,750   | <b>(23,919)</b>          | (15,345) | <b>(855,229)</b> | (504,093) | <b>615,000</b>     | 615,082     | <b>25,895,518</b>   | 20,541,415   |
| Gain on sale of investment                                             |                                 |             |                                                    |          |                          |          |                  |           |                    |             | -                   | 2,587,044    |
| Equity in net earnings (losses) of associates and joint ventures - net |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>(22,345)</b>     | 795,004      |
| Interest income                                                        |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>549,977</b>      | 447,843      |
| Interest expense and other financing charges                           |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>(13,168,470)</b> | (12,673,891) |
| Other income (charges) - net                                           |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>68,225</b>       | (8,491,062)  |
| Income tax benefit (expense)                                           |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>(2,693,423)</b>  | 836,302      |
| <b>Consolidated Net Income</b>                                         |                                 |             |                                                    |          |                          |          |                  |           |                    |             | <b>P10,629,482</b>  | P4,042,655   |

| For the Years Ended December 31                                                      |                     |              |                                                    |            |                          |          |                    |             |                      |              |                     |              |
|--------------------------------------------------------------------------------------|---------------------|--------------|----------------------------------------------------|------------|--------------------------|----------|--------------------|-------------|----------------------|--------------|---------------------|--------------|
|                                                                                      | Power Generation    |              | Retail and Other Power<br>Related Service Provider |            | Coal Mining<br>Companies |          | Others             |             | Eliminations         |              | Consolidated        |              |
|                                                                                      | 2014                | 2013         | 2014                                               | 2013       | 2014                     | 2013     | 2014               | 2013        | 2014                 | 2013         | 2014                | 2013         |
| <b>Other Information</b>                                                             |                     |              |                                                    |            |                          |          |                    |             |                      |              |                     |              |
| Segment assets                                                                       | <b>P249,910,569</b> | P253,043,075 | <b>P2,419,373</b>                                  | P392,316   | <b>P683,275</b>          | P623,242 | <b>P54,959,742</b> | P38,419,420 | <b>(P9,937,570)</b>  | (P2,024,583) | <b>P298,035,389</b> | P290,453,470 |
| Investments and advances                                                             | <b>157,146</b>      | 136,669      | <b>191,549</b>                                     | 259,834    | -                        | -        | <b>10,263,582</b>  | 5,615,296   | -                    | -            | <b>10,612,277</b>   | 6,011,799    |
| Intangible assets and goodwill                                                       |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>2,322,241</b>    | 1,728,592    |
| Deferred tax assets                                                                  |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>2,779,380</b>    | 2,909,105    |
| <b>Consolidated Total Assets</b>                                                     |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>P313,749,287</b> | P301,102,966 |
| Segment liabilities                                                                  | <b>P213,093,977</b> | P218,575,799 | <b>P2,081,602</b>                                  | P79,249    | <b>P74,665</b>           | P65,238  | <b>P9,878,869</b>  | P1,255,091  | <b>(P10,037,078)</b> | (P2,000,723) | <b>P215,092,035</b> | P217,974,654 |
| Long-term debt                                                                       |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>48,713,245</b>   | 47,088,885   |
| Income tax payable                                                                   |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>151,360</b>      | 218,519      |
| Deferred tax liabilities                                                             |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>3,043,470</b>    | 2,088,065    |
| <b>Consolidated Total Liabilities</b>                                                |                     |              |                                                    |            |                          |          |                    |             |                      |              | <b>P267,000,110</b> | P267,370,123 |
| Capital expenditures                                                                 | <b>P38,878</b>      | P121,438     | <b>P -</b>                                         | <b>P -</b> | <b>P15,087</b>           | P52,425  | <b>P17,425,124</b> | P18,948,668 | <b>P -</b>           | <b>P -</b>   | <b>P17,479,089</b>  | P19,122,531  |
| Depreciation and amortization of property, plant and equipment and intangible assets | <b>6,143,959</b>    | 5,382,435    | <b>14,686</b>                                      | 75         | <b>18,098</b>            | 9,139    | <b>10,897</b>      | 6,125       | -                    | -            | <b>6,187,640</b>    | 5,397,774    |
| Noncash items other than depreciation*                                               | <b>1,027,398</b>    | 7,976,155    | <b>11,074</b>                                      | 41,373     | <b>(23)</b>              | -        | <b>87,776</b>      | 1,491,555   | -                    | -            | <b>1,126,225</b>    | 9,509,083    |

\*Noncash items other than depreciation and amortization include unrealized foreign exchange gain/losses, impairment losses on receivables and equity in net earnings of associates.

## 6. Deferred Exploration and Development Costs

The movement in deferred exploration and development costs is as follows:

|                              | 2014            | 2013     |
|------------------------------|-----------------|----------|
| Balance at beginning of year | <b>P525,999</b> | P325,219 |
| Additions                    | <b>145,784</b>  | 200,780  |
| Balance at end of year       | <b>P671,783</b> | P525,999 |

SMEC acquired DAMI, SEPC and BERI in 2010 resulting in the recognition of mining rights of P1,719,726 (Note 14).

DAMI's coal property covered by Coal Operating Contract (COC) No. 126, issued by the Department of Energy (DOE), is located in South Cotabato and consists of two (2) coal blocks with a total area of two thousand (2,000) hectares, more or less, and has an In-situ coal resources (measured plus indicative coal resources) of about ninety-four (94) million metric tons as of December 31, 2014.

SEPC has a coal mining property and right over an aggregate area of seven thousand (7,000) hectares, more or less, composed of seven (7) coal blocks located in South Cotabato and Sultan Kudarat. As of December 31, 2014, COC No. 134 has an In-situ coal resources (measured plus indicative coal resources) of about thirty-five (35) million metric tons.

BERI's COC No. 138, issued by the DOE is located in Sarangani Province and South Cotabato consisting of eight (8) coal blocks with a total area of eight thousand (8,000) hectares, more or less, and has an In-situ coal resources (measured plus indicative coal resources) of about twenty three (23) million metric tons as of December 31, 2014.

### Status of Operations

In 2008 and 2009, the DOE approved the conversion of the COC for Exploration to COC for Development and Production of DAMI, SEPC and BERI, respectively, effective on the following dates:

| Subsidiary | COC No. | Effective Date    | Term*    |
|------------|---------|-------------------|----------|
| DAMI       | 126     | November 19, 2008 | 10 years |
| SEPC       | 134     | February 23, 2009 | 10 years |
| BERI       | 138     | May 26, 2009      | 10 years |

\* The term is followed by another 10-year extension, and thereafter, renewable for a series of 3 year periods not exceeding 12 years under such terms and conditions as may be agreed upon with the DOE.

In May 2011, DAMI, SEPC and BERI separately requested to the DOE for a moratorium on suspension of the implementation of the production timetable as specified in the Five-Year Development and Productive Work Progress of COC Nos. 126, 134 and 138 due to the newly enacted Environment Code of South Cotabato which prohibits open pit mining and other related activities, hence, constrained these companies into implementing the production timetable without violating this local ordinance. On April 27, 2012, the DOE granted DAMI, SEPC and BERI's request for a moratorium on their work commitments from the effective dates of their respective COCs when these were converted to Development/Production Phase until December 31, 2012.

On December 27, 2012, DAMI, SEPC and BERI submitted separately their Five-Year Work Program (WP) to the DOE. The DOE, however, imposed certain requirements before it can further process the WP. On August 8, 2013, DAMI, SEPC and BERI resubmitted the Five-Year WP incorporating additional requirements of the DOE.

On April 29, 2014, DAMI, SEPC and BERI requested for a suspension of their work commitments under their respective COCs until December 31, 2016 or until the ban on open-pit mining pursuant to the Environment Code of South Cotabato has been lifted, whichever comes first. On January 26, 2015, the DOE granted the request.

As of December 31, 2014, DAMI, SEPC and BERI are in the exploratory stages of their mining activities. All related costs and expenses from exploration are currently deferred as exploration and development costs and will be amortized upon commencement of their commercial operations.

The Group has not identified any facts and circumstances which suggest that the carrying amount of the deferred exploration and development costs exceeded recoverable amount as of December 31, 2014 and 2013.

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## 7. Agreements

### a. Independent Power Producer (IPP) Administration (IPPA) Agreements

As a result of the biddings conducted by PSALM for the Appointment of the IPP Administrator for the Contracted Capacity of the following power plants, the Group was declared the winning bidder and act as IPP Administrator through the following appointed subsidiaries:

| Subsidiary | Power Plant                                                                | Location                       |
|------------|----------------------------------------------------------------------------|--------------------------------|
| SMEC       | Sual Coal - Fired Power Station (Sual Power Plant)                         | Sual, Pangasinan Province      |
| SPDC       | San Roque Hydroelectric Power Plant (San Roque Power Plant)                | San Roque, Pangasinan Province |
| SPPC       | Ilijan Natural Gas - Fired Combined Cycle Power Plant (Ilijan Power Plant) | Ilijan, Batangas Province      |

The IPPA Agreements are with the conformity of National Power Corporation (NPC), a government-owned and controlled corporation created by virtue of Republic Act (R.A.) No. 6395, as amended, whereby NPC confirms, acknowledges, approves and agrees to the terms of the IPPA Agreements and further confirms that for so long as it remains the counterparty of the IPP it will comply with its obligations and exercise its rights and remedies under the original agreement with the IPP at the request and instruction of PSALM.

The IPPA Agreements include, among others, the following common salient rights and obligations:

- i. The right and obligation to manage and control the contracted capacity of the power plant for its own account and at its own cost and risks;

- ii. The right to trade, sell or otherwise deal with the capacity (whether pursuant to the spot market, bilateral contracts with third parties or otherwise) and contract for or offer related ancillary services, in all cases for its own account and at its own risk and cost. Such rights shall carry the rights to receive revenues arising from such activities without obligation to account therefore to PSALM or any third party;
- iii. The right to receive a transfer of the power plant upon termination of the IPPA Agreement at the end of the cooperation period or in case of buy-out;
- iv. For SMEC and SPPC, the right to receive an assignment of NPC's interest to existing short-term bilateral power supply contracts;
- v. The obligation to supply and deliver, at its own cost, fuel required by the IPP and necessary for the Sual Power Plant to generate the electricity required to be produced by the IPP;
- vi. Maintain the performance bond in full force and effect with a qualified bank; and
- vii. The obligation to pay PSALM the monthly payments and energy fees in respect of all electricity generated from the capacity, net of outages.

Relative to the IPPA Agreements, SMEC, SPDC and SPPC have to pay PSALM monthly payments for fifteen (15) years until October 1, 2024, eighteen (18) years until April 26, 2028 and twelve (12) years until June 26, 2022, respectively. Energy fees for 2014 and 2013 amounted to P30,775,896 and P31,269,293, respectively. SMEC, SPDC and SPPC renewed their performance bonds in United States dollar (US\$) amounting to US\$58,187, US\$20,305 and US\$60,000 which will expire on November 3, 2015, January 25, 2015 and June 16, 2015, respectively. Subsequently, the performance bond of SPDC was renewed up to January 25, 2016.

The finance lease liabilities are carried at amortized cost using the US dollar and Philippine peso discount rates as follows:

|      | US Dollar | Philippine Peso |
|------|-----------|-----------------|
| SMEC | 3.89%     | 8.16%           |
| SPPC | 3.85%     | 8.05%           |
| SPDC | 3.30%     | 7.90%           |

The discount determined at inception of the agreement is amortized over the period of the IPPA Agreement and recognized as part of "Interest expense and other financing charges" account in the consolidated statements of income. Interest expense in 2014 and 2013 amounted to P10,717,606 and P10,983,520, respectively.

The future minimum lease payments for each of the following periods are as follows:

| <b>2014</b>                                               | <b>US Dollar<br/>Payments</b> | <b>Peso<br/>Equivalent of<br/>US Dollar<br/>Payments</b> | <b>Peso<br/>Payments</b> | <b>Total</b> |
|-----------------------------------------------------------|-------------------------------|----------------------------------------------------------|--------------------------|--------------|
| Not later than one year                                   | US\$238,557                   | P10,668,258                                              | P11,423,146              | P22,091,404  |
| More than one year and not later than five years          | 1,027,007                     | 45,927,750                                               | 49,178,287               | 95,106,037   |
| Later than five years                                     | 1,413,789                     | 63,224,641                                               | 67,753,365               | 130,978,006  |
|                                                           | 2,679,353                     | 119,820,649                                              | 128,354,798              | 248,175,447  |
| Less: Future finance charges on finance lease liabilities | 462,375                       | 20,677,383                                               | 41,194,319               | 61,871,702   |
| Present values of finance lease liabilities               | US\$2,216,978                 | P99,143,266                                              | P87,160,479              | P186,303,745 |

| <b>2013</b>                                               | <b>US Dollar<br/>Payments</b> | <b>Peso<br/>Equivalent of<br/>US Dollar<br/>Payments</b> | <b>Peso<br/>Payments</b> | <b>Total</b> |
|-----------------------------------------------------------|-------------------------------|----------------------------------------------------------|--------------------------|--------------|
| Not later than one year                                   | US\$218,026                   | P9,679,245                                               | P10,437,649              | P20,116,894  |
| More than one year and not later than five years          | 997,500                       | 44,283,990                                               | 47,765,439               | 92,049,429   |
| Later than five years                                     | 1,681,853                     | 74,665,869                                               | 80,589,359               | 155,255,228  |
|                                                           | 2,897,379                     | 128,629,104                                              | 138,792,447              | 267,421,551  |
| Less: Future finance charges on finance lease liabilities | 546,958                       | 24,282,163                                               | 48,136,667               | 72,418,830   |
| Present values of finance lease liabilities               | US\$2,350,421                 | P104,346,941                                             | P90,655,780              | P195,002,721 |

The present values of minimum lease payments for each of the following periods are as follows:

| <b>2014</b>                                      | <b>US Dollar<br/>Payments</b> | <b>Peso<br/>Equivalent<br/>of US Dollar<br/>Payments</b> | <b>Peso<br/>Payments</b> | <b>Total</b> |
|--------------------------------------------------|-------------------------------|----------------------------------------------------------|--------------------------|--------------|
| Not later than one year                          | US\$194,970                   | P8,719,059                                               | P7,486,165               | P16,205,224  |
| More than one year and not later than five years | 764,915                       | 34,206,990                                               | 26,604,935               | 60,811,925   |
| Later than five years                            | 1,257,093                     | 56,217,217                                               | 53,069,379               | 109,286,596  |
|                                                  | US\$2,216,978                 | P99,143,266                                              | P87,160,479              | P186,303,745 |

| 2013                                                   | US Dollar<br>Payments | Peso<br>Equivalent<br>of US Dollar<br>Payments | Peso<br>Payments | Total        |
|--------------------------------------------------------|-----------------------|------------------------------------------------|------------------|--------------|
| Not later than one<br>year                             | US\$185,176           | P8,220,890                                     | P7,409,540       | P15,630,430  |
| More than one year<br>and not later than<br>five years | 771,027               | 34,229,759                                     | 27,918,504       | 62,148,263   |
| Later than five years                                  | 1,394,218             | 61,896,292                                     | 55,327,736       | 117,224,028  |
|                                                        | US\$2,350,421         | P104,346,941                                   | P90,655,780      | P195,002,721 |

b. Market Participation Agreements (MPA)

SMEC, SPDC and SPPC entered into a MPA with the Philippine Electricity Market Corporation (PEMC) to satisfy the conditions contained in the Philippine WESM Rules on WESM membership and to set forth the rights and obligations of a WESM member. Under the WESM Rules, the cost of administering and operating the WESM shall be recovered through a charge imposed on all WESM members or transactions, as approved by the Energy Regulatory Commission (ERC). For the years ended December 31, 2014 and 2013, PEMC's market fees charged to SMEC, SPDC and SPPC amounted to P233,701 and P246,591, respectively (Note 20).

In March 2013, SMELC entered into a MPA for Supplier as Direct WESM Member - Customer Trading Participant Category with the PEMC to satisfy the conditions contained in the Philippine WESM Rules on WESM membership and to set forth the rights and obligations of a WESM member. SMELC has a standby letter of credit, expiring on December 26, 2015, to secure the full and prompt performance of obligations for its transactions as a Direct Member and trading participant in the WESM.

c. Power Supply Agreements

SMEC, SPPC, SPDC, SMELC and SPI have Power Supply Agreements with various counterparties, including related parties, to sell electricity produced by the power plants. All agreements provide for renewals or extensions subject to mutually agreed terms and conditions by the parties.

Certain customers like electric cooperatives are billed based on the time-of-use (TOU) per kilowatt hour (kWh) while others are billed at capacity-based rate. However, as stipulated in the contracts, each TOU-based customer has to pay the minimum charge based on the contracted power using the basic energy charge and/or adjustments if customer has not fully taken or failed to consume the contracted power. For capacity-based contracts, the customers are charged with the capacity fees based on the contracted capacity even if there is no associated energy taken during the month.

SMEC, SPPC, SPDC and APEC purchase power from WESM and other power generation companies during periods when the power generated from the power plant is not sufficient to meet customers' power requirements.

d. Coal Supply Agreements

SMEC and SPI have supply agreements with various coal suppliers for their power plants' coal requirements.

e. Operations and Maintenance (O&M) Services Agreement

In exchange for the O&M services rendered by Petron Corporation (Petron), SPI pays for all the documented costs and expenses incurred in relation to the operation, maintenance and repair of the power plant. The agreement is effective for 25 years from September 2013 until 2038.

f. Retail Supply Agreements

SMELC has retail supply agreements with customers to supply or sell electricity purchased from related parties and WESM. All agreements provide for renewals or extensions subject to terms and conditions mutually agreed by the parties.

The customers are billed based on the capacity charge and associated energy charge. However, as stipulated in the contracts, each customer has to pay the capacity charge based on the contracted capacity using the capacity fee and associated energy with adjustments if customer has not fully taken or failed to consume the contracted capacity.

g. Lease Agreements

- i. The Group has operating lease agreements with San Miguel Properties, Inc. (SMPI), a related party under common control, for a period of 1 to 6 years which is renewable annually or upon agreement between parties.
- ii. SPI subleases its plant premises from New Ventures Realty Corporation (NVRC), a related party under common control. The existing lease agreement is for 25-year period up to September 30, 2038, subject to renewal. The yearly rental is subject to an automatic 3% escalation rate for the 4 years following the negotiation under the lease terms.
- iii. SMEC has operating lease agreement with Challenger Aero Air Corporation (Challenger), a related party under common control, for a period of 1 year commencing in October 2014 and expiring in September 2015.

Relative to the lease agreements with SMPI and Challenger, the Group was required to pay advance rental and security deposits which are included under "Trade and other receivables - net" or "Prepaid expenses and other current assets" accounts in the consolidated statements of financial position (Notes 9 and 11).

Future minimum lease payments under the non-cancellable operating lease agreements are as follows:

|                                             | 2014           | 2013    |
|---------------------------------------------|----------------|---------|
| Within one year                             | <b>P24,361</b> | P23,270 |
| After one year but not more than five years | <b>37,928</b>  | 62,289  |
|                                             | <b>P62,289</b> | P85,559 |

Rent expense recognized in the consolidated statements of income amounted to P115,849 and P24,167 in 2014 and 2013, respectively (Note 20).

- iv. During the year, the Parent Company has an operating sub-lease agreement with Clariden Holdings, Inc. a related party under common control, for a period of 2 years which is renewable upon agreement between the parties.

Future minimum lease receivables under the non-cancellable operating sub-lease is as follows:

|                                             | <b>2014</b>    |
|---------------------------------------------|----------------|
| Within one year                             | <b>P7,120</b>  |
| After one year but not more than five years | <b>3,957</b>   |
|                                             | <b>P11,077</b> |

Rent income recognized in the consolidated statements of income amounted to P18,434 and nil in 2014 and 2013, respectively.

#### h. Concession Agreement

The Parent Company entered into a 25-year Concession Agreement with ALECO on October 29, 2013. It became effective upon confirmation of the National Electrification Administration on November 7, 2013.

The Concession Agreement include, among others, the following rights and obligations: i) the Parent Company, through Albay Power and Energy Corp. (APEC), assumed all the rights and interests and perform the obligations under the Concession Agreement effective on January 3, 2014; ii) as Concession Fee, the Concessionaire shall pay to ALECO: (a) separation pay of ALECO employees in accordance with the Concession Agreement; (b) the amount of P2,100 every quarter for the upkeep of residual ALECO (fixed concession fees); iii) if the net cash flow of APEC is positive within five (5) years or earlier from date of signing of the Concession Agreement, 50% of the Net Cash Flow each month shall be deposited in an escrow account until the cumulative nominal sum reaches P4,048,529; iv) on the 20<sup>th</sup> anniversary of the Concession Agreement, the concession period may be extended by mutual agreement between ALECO and APEC; and v) at the end of the concession period, all assets and system, as defined in the Concession Agreement, shall be returned by APEC to ALECO in good and usable condition. Additions and improvements to the system shall likewise be transferred to ALECO. In this regard, APEC shall provide services within the franchise area and shall be allowed to collect fees and charges, as approved by the ERC. ALECO turned over the operations to APEC on February 26, 2014.

Part of the separation pay under “ii (a)” above in the amount of P80,000 has been paid to ALECO on December 19, 2013. The payment was recognized as part of “Other noncurrent assets” account in the consolidated statements of financial position pending assumption by APEC of the Concession Agreement.

The Group recognized as intangible asset all costs directly related to the Concession Agreement. The intangible asset consist of: a) concession rights, which include fixed concession fees and separation pay of ALECO employees amounting to P384,317. Fixed concession fees are recognized at present value using the discount rate at the inception date with a corresponding concession payable recognized; and b) infrastructure, which includes the costs of structures and improvements, distribution system and equipment. Cost of infrastructure amounted to P111,995 and nil as of December 31, 2014 and 2013, respectively. Interest expense on concession payable recognized in profit or loss amounted to P4,769 and nil for the years ended December 31, 2014 and 2013, respectively. Amortization of concession assets recognized in profit or loss in 2014 and 2013 amounted to P14,610 and nil, respectively.

Maturities of the carrying amount of concession payable are as follows:

|                                              | <b>2014</b>     |
|----------------------------------------------|-----------------|
| Not later than 1 year                        | <b>P2,146</b>   |
| Later than 1 year but not later than 5 years | <b>9,929</b>    |
| More than 5 years                            | <b>96,969</b>   |
| Ending balance                               | <b>P109,044</b> |

The movements in concession asset relating to the Concession Agreement are as follows:

|                                 | <i>Note</i> | <b>2014</b>     |
|---------------------------------|-------------|-----------------|
| <b>Cost</b>                     |             |                 |
| Balance at beginning of year    |             | <b>P -</b>      |
| Additions                       |             | <b>496,312</b>  |
| Balance at end of year          |             | <b>496,312</b>  |
| <b>Accumulated amortization</b> |             |                 |
| Balance at beginning of year    |             | <b>-</b>        |
| Amortization                    |             | <b>14,610</b>   |
| Balance at end of year          |             | <b>14,610</b>   |
| <b>Net carrying amount</b>      | <b>14</b>   | <b>P481,702</b> |

i. MOA with San Roque Power Corporation (SRPC)

On December 6, 2012, SPDC entered into a 5-year MOA with SRPC to sell a portion of the capacity of the San Roque Power Plant. Under the MOA, i) SRPC shall purchase a portion of the capacity sourced from the San Roque Power Plant; ii) SRPC shall pay a settlement amount to SPDC for the capacity; and iii) the MOA may be earlier terminated or extended subject to terms and mutual agreement of the parties.

Revenue from sale of capacity of the San Roque Power Plant amounted to P1,488,437 and P577,192 as of December 31, 2014 and 2013, respectively, and was recognized as part of "Sale of power" account in the consolidated statements of income.

## 8. Cash and Cash Equivalents

Cash and cash equivalents consist of:

|                           | <i>Note</i> | <b>2014</b>        | 2013        |
|---------------------------|-------------|--------------------|-------------|
| Cash in banks and on hand |             | <b>P9,043,630</b>  | P13,330,802 |
| Short-term investments    |             | <b>29,260,664</b>  | 15,794,369  |
|                           | 25, 26      | <b>P38,304,294</b> | P29,125,171 |

Cash in banks earns interest at the respective bank deposit rates. Short-term investments are made for varying periods of up to three months depending on the immediate cash requirements of the Group and earn interest at the respective short-term investment rates.

## 9. Trade and Other Receivables

Trade and other receivables consist of:

|                                      | <i>Note</i> | <b>2014</b>        | 2013        |
|--------------------------------------|-------------|--------------------|-------------|
| Trade                                | 18          | <b>P13,195,630</b> | P12,753,539 |
| Other receivables                    | 18          | <b>5,879,395</b>   | 19,509,198  |
|                                      |             | <b>19,075,025</b>  | 32,262,737  |
| Less allowance for impairment losses |             | <b>866,686</b>     | 722,293     |
|                                      |             | <b>P18,208,339</b> | P31,540,444 |

Trade and other receivables are non-interest bearing, unsecured and are generally on a 30-day term or an agreed collection period. The balance of trade receivables is inclusive of VAT on the sale of power collectible from customers.

The movements in the allowance for impairment losses are as follows:

|                              | <i>Note</i> | <b>2014</b>     | 2013     |
|------------------------------|-------------|-----------------|----------|
| Balance at beginning of year |             | <b>P722,293</b> | P689,443 |
| Charges for the year         | 20          | <b>144,393</b>  | 32,850   |
| Balance at end of year       |             | <b>P866,686</b> | P722,293 |

As of December 31, the aging of trade receivables is as follows:

|                   | <b>2014</b>        | 2013        |
|-------------------|--------------------|-------------|
| Current           | <b>P6,703,992</b>  | P6,625,563  |
| Past due          |                    |             |
| Less than 30 days | <b>1,125,712</b>   | 2,574,000   |
| 30-60 days        | <b>574,608</b>     | 437,877     |
| 61-90 days        | <b>194,855</b>     | 144,861     |
| Over 90 days      | <b>4,596,463</b>   | 2,971,238   |
|                   | <b>P13,195,630</b> | P12,753,539 |

The Group believes that the unimpaired amounts that are past due by more than 30 days are still collectible based on historical payment behavior and analyses of the underlying customer credit ratings. There are no significant changes in their credit quality. There were no write-offs or reversals in 2014 and 2013.

Other receivables include the following:

- a. The Parent Company's receivable from the sale of investment in an associate amounting to P16,228,991. The Parent Company collected the receivable from J.G. Summit Holdings, Inc. (J.G. Summit) in 2014 (Note 13).
- b. Advances to suppliers pertain to the deposits made to certain suppliers for the ongoing construction of two (2) x 150 Mega Watt (MW) Coal-Fired Power Plant.
- c. On June 16, 2011, SMEC entered into a MOA with Hardrock Coal Mining Pty Ltd. (HCML) and Caason Investments Pty Ltd. (Caason), companies registered in Australia, for the acquisition of shares in HCML. SMEC paid to Caason Australian dollar (AUD) 12,000 (equivalent to P550,000), for an option to subscribe to the shares in HCML (the "Deposit") with further option for SMEC to decide not to pursue its investment in HCML, which will result in the return of the Deposit to SMEC plus interest. In a letter dated July 15, 2011, SMEC notified Caason and HCML that it shall not pursue said investment and therefore asked Caason and HCML for the return of the Deposit with corresponding interest (the "Amount Due"), pursuant to the terms of the MOA.

On September 2, 2014, SMEC, HCML and Caason agreed to a schedule of payment of the outstanding Amount Due to SMEC. As of December 31, 2014, HCML and Caason has paid a total amount of P119,841, inclusive of interest and other payments, such as legal costs and expenses. Interest income amounted to P118,824 and P25,015 as of December 31, 2014 and 2013, respectively. As of December 31, 2014 and 2013, total outstanding receivables from HCML amounted to P566,155 and P562,041, respectively.

- d. Pursuant to the MOA in respect of excess capacity of Sual Power Station, SMEC has receivables from Team Philippines Energy Corp. (TPEC) and Team Sual Corporation (TSC) for their share in fuel, market fees, coal and other charges related to the operation of the Sual Power Plant amounting to P59,871 and P30,267 as of December 31, 2014 and 2013, respectively. Likewise, SMEC has receivables from WESM for the account of TPEC amounting to P926,583 and P444,463 as of December 31, 2014 and 2013, respectively.
- e. As of December 31, 2014 and 2013, the outstanding claims from PSALM due to monthly payments reduction amounted to nil and P355,175, respectively (Note 7).
- f. The balance mainly pertains to receivables from customers related to power rate adjustments which will be remitted to the Government upon collection.

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**10. Inventories**

Inventories at cost consist of:

|                        | <i>Note</i> | <b>2014</b>       | 2013       |
|------------------------|-------------|-------------------|------------|
| Coal                   | 7, 18       | <b>P1,179,585</b> | P1,381,589 |
| Fuel oil               | 18          | <b>93,402</b>     | 114,356    |
| Materials and supplies |             | <b>86,242</b>     | -          |
| Other consumables      |             | <b>5,804</b>      | 3,190      |
|                        |             | <b>P1,365,033</b> | P1,499,135 |

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There were no inventory write-downs to net realizable value for the years ended December 31, 2014 and 2013. Inventories charged to cost of power sold amounted to P11,945,280 and P11,179,322 in 2014 and 2013, respectively.

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**11. Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets consist of:

|                         | <i>Note</i> | <b>2014</b>       | 2013       |
|-------------------------|-------------|-------------------|------------|
| Input VAT               |             | <b>P7,389,026</b> | P6,058,256 |
| Prepaid tax             |             | <b>1,296,666</b>  | 933,774    |
| Prepaid rent and others | 7, 18       | <b>451,510</b>    | 242,862    |
|                         |             | <b>P9,137,202</b> | P7,234,892 |

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Input VAT consists of current and deferred Input VAT on purchases and can be offset against the output VAT payable (Note 16).

Prepaid tax consists of creditable withholding taxes and excess tax credits of the Group from prior years.

## 12. Property, Plant and Equipment

Property, plant and equipment consist of:

|                                                      | <b>Power Plants</b><br>(Note 7) | <b>Building</b>   | <b>Leasehold<br/>Improvements</b> | <b>Other<br/>Equipment</b> | <b>Construction<br/>in Progress</b> | <b>Total</b>        |
|------------------------------------------------------|---------------------------------|-------------------|-----------------------------------|----------------------------|-------------------------------------|---------------------|
| <b>Cost</b>                                          |                                 |                   |                                   |                            |                                     |                     |
| January 1, 2013                                      | P214,319,759                    | P -               | P -                               | P43,275                    | P4,769,135                          | P219,132,169        |
| Additions                                            | 7,441,107                       | 3,480,934         | 332,251                           | 917,483                    | 6,950,756                           | 19,122,531          |
| Reclassifications                                    | -                               | -                 | 14,351                            | -                          | (14,351)                            | -                   |
| December 31, 2013                                    | 221,760,866                     | 3,480,934         | 346,602                           | 960,758                    | 11,705,540                          | 238,254,700         |
| Additions                                            | -                               | -                 | 46                                | 98,542                     | 17,380,501                          | 17,479,089          |
| Disposals                                            | -                               | -                 | -                                 | -                          | (82,420)                            | (82,420)            |
| Reclassifications                                    | 5,027,966                       | 2,350,163         | -                                 | 98,776                     | (7,590,524)                         | (113,619)           |
| <b>December 31, 2014</b>                             | <b>226,788,832</b>              | <b>5,831,097</b>  | <b>346,648</b>                    | <b>1,158,076</b>           | <b>21,413,097</b>                   | <b>255,537,750</b>  |
| <b>Accumulated Depreciation and<br/>Amortization</b> |                                 |                   |                                   |                            |                                     |                     |
| January 1, 2013                                      | 15,814,253                      | -                 | -                                 | 14,744                     | -                                   | 15,828,997          |
| Additions                                            | 5,312,454                       | 45,193            | 9,750                             | 36,787                     | -                                   | 5,404,184           |
| December 31, 2013                                    | 21,126,707                      | 45,193            | 9,750                             | 51,531                     | -                                   | 21,233,181          |
| Additions                                            | 5,803,956                       | 220,638           | 36,481                            | 110,171                    | -                                   | 6,171,246           |
| <b>December 31, 2014</b>                             | <b>26,930,663</b>               | <b>265,831</b>    | <b>46,231</b>                     | <b>161,702</b>             | <b>-</b>                            | <b>27,404,427</b>   |
| <b>Carrying Amount</b>                               |                                 |                   |                                   |                            |                                     |                     |
| December 31, 2013                                    | P200,634,159                    | P3,435,741        | P336,852                          | P909,227                   | P11,705,540                         | P217,021,519        |
| <b>December 31, 2014</b>                             | <b>P199,858,169</b>             | <b>P5,565,266</b> | <b>P300,417</b>                   | <b>P996,374</b>            | <b>P21,413,097</b>                  | <b>P228,133,323</b> |

On September 23, 2013, SPI acquired from Petron a 2 x 35 MW Co-Generation Solid Fuel-Fired Power Plant and all other pertinent machinery, equipment, facilities and structures being constructed and installed which comprise the additional 2 x 35 MW Co-Generation Solid Fuel-Fired Power Plant in Bataan, for a total consideration of P16,800,000, inclusive of tax (Note 18). The power plant is used as collateral in securing a loan obtained by SPI from syndicated banks (Note 17).

Construction in progress pertains to the following:

- a. Power plant project of SMCP and SCPC for the construction of Coal-Fired Power Plants in Davao and Bataan, respectively;
- b. Construction of limestone pulverizing plant and petcoke handling facility of SPI.

SMEC, as IPP Administrator, and TSC, as IPP and operator of the Sual Power Plant, intend to improve the coal receiving and unloading capability of the Sual Power Plant as well as increase the coal shipment deliveries thereto (Note 7).

On September 9, 2014, SMEC agreed to provide an additional coal unloader (the “Third Unloader”) to the Sual Power Plant while TSC agreed to install, operate and maintain the same during the life of the Sual IPPA Agreement or until 2024. Considering however, that TSC is not allowed to accept and install any equipment in the Sual Power Plant that it does not own, SMEC agreed to donate the same in order to implement the parties’ intention to improve unloading capability and increase coal shipment deliveries. The Third Unloader will be part of the assets to be turned over to SMEC at the end of the Sual IPPA Agreement or until 2024 and is recognized under “Donations” account in the consolidated statements of income (Note 20).

Computer and system installations, and upgrades and implementation of accounting system recognized as part of capital projects in progress were reclassified to “Intangible assets” in 2014 (Note 14).

Depreciation and amortization are recognized in profit or loss as follows:

|                    | <i>Note</i> | <b>2014</b>       | 2013       |
|--------------------|-------------|-------------------|------------|
| Cost of power sold |             | <b>P6,143,866</b> | P5,382,435 |
| Operating expenses | 20          | <b>43,774</b>     | 21,749     |
|                    |             | <b>P6,187,640</b> | P5,404,184 |

Total depreciation and amortization recognized in profit or loss include annual amortization of capitalized interest amounting to P4,453 and nil in 2014 and 2013, respectively.

The Group has interest amounting to P254,539 and P84,367 which was capitalized in 2014 and 2013, respectively. The capitalization rates used to determine the amount of interest eligible for capitalization range from 6.0606% to 6.5446% and 6.3131% in 2014 and 2013, respectively. The unamortized capitalized borrowing costs amounted to P349,498 and P87,462 as of December 31, 2014 and 2013, respectively.

The combined carrying amounts of power plants under finance lease amounted to P188,132,700 and P193,319,103 as of December 31, 2014 and 2013, respectively.

### 13. Investments and Advances

Investments and advances consist of:

|                                                        | <i>Note</i> | <b>2014</b>        | <b>2013</b>  |
|--------------------------------------------------------|-------------|--------------------|--------------|
| <b>Cost</b>                                            |             |                    |              |
| Balance at beginning of year                           |             | <b>P301,208</b>    | P12,824,356  |
| Additions                                              |             | <b>1,830,054</b>   | 301,208      |
| Disposal                                               |             | -                  | (12,824,356) |
| Adjustment to subscription receivable                  |             | <b>(57,211)</b>    | -            |
| Balance at end of year                                 |             | <b>2,074,051</b>   | 301,208      |
| <b>Accumulated Equity in Net Earnings<br/>(Losses)</b> |             |                    |              |
| Balance at beginning of year                           |             | <b>(41,374)</b>    | 596,598      |
| Equity in net earnings (losses) during the<br>year     |             | <b>(32,231)</b>    | 795,004      |
| Adjustment to equity in net loss prior year            |             | <b>9,886</b>       | -            |
| Share in other comprehensive income                    | 19          | -                  | 20,535       |
| Dividends                                              |             | -                  | (704,407)    |
| Disposal                                               |             | -                  | (749,104)    |
| Balance at end of year                                 |             | <b>(63,719)</b>    | (41,374)     |
|                                                        |             | <b>2,010,332</b>   | 259,834      |
| Advances                                               |             | <b>8,601,945</b>   | 5,751,965    |
|                                                        |             | <b>P10,612,277</b> | P6,011,799   |

The Group's investments pertain to the following:

a. Meralco

In 2012, investment in an associate consists of 69,059,538 quoted common stock of Meralco, representing 6.13% ownership interest. The Parent Company has determined that it has obtained significant influence over the financial and operating policies of Meralco in conjunction with SMC and subsidiaries' ownership of 32.04% interest in Meralco. Accordingly, the Parent Company applied the equity method of accounting on its investment in shares of stock of Meralco.

On September 30, 2013, the Parent Company, together with SMC and San Miguel Pure Foods Company, Inc., entered into a Share Purchase Agreement with J.G. Summit, for the sale of the Parent Company's 69,059,538 shares of stock of Meralco for P16,228,991. The sale is subject to the satisfaction of certain closing conditions, which were satisfied by all the parties on December 11, 2013. As a result of the sale, the Group recognized a gain of P2,587,044, net of expenses, included as part of "Gain on sale of investment" account in the 2013 consolidated statement of income (Note 9).

b. Olongapo Electricity Distribution Company, Inc. (OEDC)

In April 2013, SPGC and San Miguel Equity Investments, Inc. (SMEII) entered into a Deed of Assignment of Subscription Rights whereby SMEII agreed to assign 35% ownership interest in OEDC to SPGC for a consideration of P8,750.

As of December 31, 2014 and 2013, carrying amount of investment in OEDC amounted to P191,549 and P259,834, respectively. Subscription payable amounted to P28,101 and P65,625 as of December 31, 2014 and 2013, respectively (Note 16).

The table below summarizes the financial information of investment in an associate which is accounted for using the equity method:

| <b>Country of Incorporation</b>                  | <b>2014</b>                              | <b>2013</b>                            |
|--------------------------------------------------|------------------------------------------|----------------------------------------|
|                                                  | <b>(Unaudited)</b><br><b>Philippines</b> | <b>(Audited)</b><br><b>Philippines</b> |
| Current assets                                   | <b>P424,000</b>                          | P247,317                               |
| Noncurrent assets                                | <b>1,004,174</b>                         | 891,828                                |
| Current liabilities                              | <b>(916,386)</b>                         | (567,671)                              |
| Noncurrent liability                             | -                                        | (1,990)                                |
| Net assets                                       | <b>P511,788</b>                          | P569,484                               |
| Revenue                                          | <b>P1,231,297</b>                        | P656,942                               |
| Net losses / total comprehensive losses          | <b>(P59,883)</b>                         | (P92,049)                              |
| Share in net losses / total comprehensive losses | <b>(P20,959)</b>                         | (P31,488)                              |

- c. Angat Hydropower Corporation (Angat Hydro) and KWPP Holdings Corporation (KWPP)

In accordance with the agreement of the Parent Company through PVEI, a subsidiary of SMC Global, and Korea Water Resources Corporation (K-Water) to enter into a joint venture partnership for the acquisition, rehabilitation, operation and maintenance of the 218 MW Angat Hydroelectric Power Plant (Angat Power Plant) awarded by PSALM to K-Water, PVEI deposited US\$26,448 to an escrow account.

On November 18, 2014, PVEI acquired from the individual stockholders and K-Water, 2,817,270 shares or 60% of the outstanding capital stock of Angat Hydro and from the individual stockholders, 75 shares representing 60% of KWPP outstanding capital stock. Accordingly, PVEI paid K-Water and the individual stockholders a total of US\$39,236 and P15 as full payment of the share purchase price of Angat Hydro and KWPP shares, respectively. The payment was funded in part by the deposit in escrow.

In accordance with the entry of PVEI into Angat Hydro and KWPP, K-Water and PVEI are jointly in control of the management and operation of Angat Hydro and KWPP.

Further, PVEI agreed to pay K-Water a support fee amounting to 3% of the total amount of the bridge loan facility which was obtained for the acquisition by Angat Hydro of the Angat Power Plant.

#### Angat Hydro

Angat Hydro was incorporated on November 15, 2013 and was created to engage in the operations and maintenance of the Angat Power Plant and to supply power generated to power corporations, electric utilities, to import hydro-electric facilities and equipment, and to do all acts necessary and incidental thereto, in accordance with R.A. No. 9136 or otherwise known as the Electric Power Industry Reform Act of 2001 (EPIRA).

#### KWPP

KWPP was incorporated on November 27, 2013 and was established for the purpose of acquiring, holding or leasing water and flowage rights.

As of December 31, 2014, details in investments in Angat Hydro and KWPP are as follows:

|                                     | <b>Angat Hydro</b> | <b>KWPP</b> |
|-------------------------------------|--------------------|-------------|
| Acquisition cost                    | <b>P1,830,039</b>  | <b>P15</b>  |
| Equity in net losses for the period | <b>(11,257)</b>    | <b>(15)</b> |
|                                     | <b>P1,818,782</b>  | <b>P -</b>  |

The table below summarizes the financial information of investments in joint venture which is accounted for using the equity method:

|                                                                                                       | <b>Angat Hydro</b>  | <b>KWPP</b>        |
|-------------------------------------------------------------------------------------------------------|---------------------|--------------------|
| <b>Country of Incorporation</b>                                                                       | <b>Philippines</b>  | <b>Philippines</b> |
| Current assets                                                                                        | <b>P407,488</b>     | <b>P69</b>         |
| Noncurrent assets                                                                                     | <b>20,187,061</b>   | <b>17,385</b>      |
| Current liabilities                                                                                   | <b>(19,713,866)</b> | <b>(354)</b>       |
| Noncurrent liabilities                                                                                | <b>(17,421)</b>     | <b>(17,661)</b>    |
| Net assets                                                                                            | <b>P863,262</b>     | <b>(P561)</b>      |
| Revenue                                                                                               | <b>P153,772</b>     | <b>P -</b>         |
| Net losses / total comprehensive losses                                                               | <b>(P72,451)</b>    | <b>(P470)</b>      |
| Share in net losses / total comprehensive losses for the period from November 18 to December 31, 2014 | <b>(P11,257)</b>    | <b>(P15)</b>       |

#### **14. Goodwill and Other Intangible Assets**

Goodwill and other intangible assets consist of:

|                                     | <b>Note</b> | <b>2014</b>       | <b>2013</b> |
|-------------------------------------|-------------|-------------------|-------------|
| Mining rights                       | 6           | <b>P1,719,726</b> | P1,719,726  |
| Concession assets - net             | 7           | <b>481,702</b>    | -           |
| Computer software under development |             | <b>111,947</b>    | -           |
| Goodwill                            |             | <b>8,866</b>      | 8,866       |
|                                     |             | <b>P2,322,241</b> | P1,728,592  |

The goodwill is attributed to the Group's acquisition of SMEC and SPDC in 2010. Based on management's assessment of the goodwill, it is not impaired since the recoverable amount of the related net assets of SMEC and SPDC for which the goodwill was attributed still exceeds its carrying amount including goodwill as of December 31, 2014 and 2013.

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**15. Other Noncurrent Assets**

Other noncurrent assets consist of:

|                                             | <i>Note</i> | <b>2014</b>       | 2013       |
|---------------------------------------------|-------------|-------------------|------------|
| Restricted cash                             | 13, 25, 26  | <b>P1,054,801</b> | P1,800,438 |
| Deferred input VAT - net of current portion |             | <b>980,057</b>    | 1,320,591  |
| Noncurrent receivable                       | 25, 26      | <b>179,129</b>    | 305,281    |
| Advances to suppliers                       |             | <b>1,428</b>      | -          |
| Others                                      | 7           | -                 | 80,000     |
|                                             |             | <b>P2,215,415</b> | P3,506,310 |

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Restricted cash represents: (a) deposits made by PVEI in an escrow account for the acquisition, rehabilitation, operation and maintenance of the Angat Power Plant. In 2014, the amount was withdrawn and paid to the sellers (Note 13); (b) SPI's Cash Flow Waterfall accounts (Trust Fund) with a local bank as part of the provisions in SPI's Facility Agreement amounting to P1,021,163 in 2014 and P626,279 in 2013 (Note 17); and (c) APEC's collected contributions from consumers, membership fees and bill deposits in 2014 and 2013 amounted to P33,638 and nil, respectively.

The deferred input VAT mainly pertains to the input VAT on the purchase of the Limay power plant from Petron.

Noncurrent receivable represents receivable from a third party for the sale of the Parent Company's 100% ownership interest in PEI, net of current portion.

Others represent the initial amount paid by the Parent Company for the separation pay of employees of ALECO in 2013. This amount became part of the concession asset of APEC when it assumed the Concession Agreement (Note 7).

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**16. Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses consist of:

|                      | <i>Note</i> | <b>2014</b>        | 2013        |
|----------------------|-------------|--------------------|-------------|
| Trade                | 7, 18       | <b>P12,621,078</b> | P12,750,570 |
| Accrued expenses     |             | <b>8,851,501</b>   | 1,837,417   |
| Output VAT           |             | <b>4,623,037</b>   | 5,364,899   |
| Non-trade            |             | <b>1,354,760</b>   | 2,287,743   |
| Accrued interest     | 7, 17       | <b>487,997</b>     | 494,755     |
| Subscription payable | 13          | <b>28,101</b>      | 65,625      |
| Withholding taxes    |             | <b>151,330</b>     | 170,924     |
|                      | 25, 26      | <b>P28,117,804</b> | P22,971,933 |

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Output VAT consists of current and deferred output VAT payable. Deferred output VAT represents the VAT on sale of power which will be remitted to the Government only upon collection from the customers (Note 9).

Accrued expenses consist of payables related to power rate adjustments and other payables to the Government other than output VAT and withholding taxes.

Non-trade payables mainly pertain to the liability relating to the power rate adjustments in November and December 2013 sale of power to WESM amounting to P1,916,196 and P2,119,181 as of December 31, 2014 and 2013, respectively. The noncurrent portion is presented as other noncurrent liability in the statements of financial position (Note 27).

## 17. Long-term Debt

Long term debt consists of:

|                       | <i>Note</i> | <b>2014</b>        | <b>2013</b> |
|-----------------------|-------------|--------------------|-------------|
| Bonds payable         |             | <b>P13,416,000</b> | P13,318,500 |
| Less debt issue costs |             | <b>61,955</b>      | 71,164      |
|                       |             | <b>13,354,045</b>  | 13,247,336  |
| Loans payable         |             | <b>35,966,800</b>  | 34,497,500  |
| Less debt issue costs |             | <b>607,600</b>     | 655,951     |
|                       |             | <b>35,359,200</b>  | 33,841,549  |
|                       | 25, 26      | <b>48,713,245</b>  | 47,088,885  |
| Less current portion  |             | <b>1,330,037</b>   | 142,403     |
|                       |             | <b>P47,383,208</b> | P46,946,482 |

### a. Bonds Payable

On January 28, 2011, the Parent Company carried out a US\$300,000, 7%, 5-year note (Bonds Payable) issue under Regulations of the U.S. Securities Act of 1933, as amended. The unsecured bond issue is listed in the Singapore Exchange Securities Trading Limited. The terms and conditions of the bonds contain a negative pledge provision with certain limitations on the ability of the Parent Company and its material subsidiaries to create or have outstanding any security interest upon, or with respect to, any of the present or future business, undertaking, assets or revenue (including any uncalled capital) of the Parent Company or any of its material subsidiaries to secure any indebtedness, subject to certain exceptions. Upon the occurrence of a change of control, each bondholder has the right, at its option, to require the Parent Company to repurchase all (but not some only) of its bonds, at a redemption price equal to 101.0% of the principal amount thereof plus accrued interest on the change of control put date.

The Parent Company has agreed to observe certain covenants, including, among other things, maintaining a leverage ratio, limitation on guarantees and loans, limitation on indebtedness, limitation on restricted payments, limitation on dividends and other restrictions affecting material subsidiaries, limitation on transactions with shareholders and affiliates, limitation of asset sales, consolidation, merger and sales of assets and certain other covenants. Interest is payable semi-annually in arrears on January 28 and July 28 of each year, with first interest payment on July 28, 2011. Bonds payable amounted to P13,416,000 and P13,318,500 while accrued interest amounted to P391,300 and P388,457 as of December 31, 2014 and 2013, respectively. Interest expense amounted to P1,123,679 and P1,094,846 in 2014 and 2013, respectively.

On December 5, 2013, the BOD was informed of the need to amend certain provisions of the Bonds Payable, including but not limited to, the definitions of “Asset Sale”, “Material Subsidiary”, “Non-Recourse Project Level Indebtedness”, “Permitted Security Interest” and “Project Subsidiaries” and the leverage and cross-default thresholds in order to align the provisions of the Bonds Payable with the US\$700,000 Loan Facility of the Parent Company, thereby providing flexibility to enable the Parent Company to divest its non-core assets and raise funds in line with its long term growth strategy.

The US\$300,000, 7% bond will mature on January 28, 2016.

b. Loans Payable

Parent Company

- i) On March 31, 2011, the Parent Company signed a US\$200,000, 3-year term loan with a syndicate of banks. The US\$200,000 loan was drawn down by the Parent Company on September 30, 2011. Pursuant to the Facility Agreement, the amount of the loan drawn down will bear interest at the rate of the London interbank offered rate plus a margin, payable in arrears on the last day of the agreed interest period.

The Parent Company may, by giving not less than ten (10) business days’ prior written notice to the Facility Agent, prepay the loan in whole or in part with accrued interest on the amount prepaid and subject to Break Funding Cost where the prepayment is made on a day other than the last day of an interest period, without minimum penalty.

On September 30, 2013, the Parent Company pre-terminated the US\$200,000, 3-year loan maturing in September 2014.

- ii) On September 9, 2013, the Parent Company signed a US\$650,000, 5-year term loan with a syndicate of banks. The Facility Agreement has some provisions similar to the US\$200,000, 3-year term loan entered into by the Parent Company on March 31, 2011. Subsequently, on November 15, 2013, the US\$650,000 Facility Agreement was amended extending the loan facility from US\$650,000 to US\$700,000.

Drawn amount from the Facility Agreement amounted to US\$500,000 as of December 31, 2014.

The Facility Agreement imposes a number of covenants on the part of the Parent Company including, but not limited to, maintaining a leverage ratio throughout the duration of the term of the Facility Agreement. The terms and conditions of the Facility Agreement contains a negative pledge provision with certain limitations on the ability of the Parent Company and its material subsidiaries to create or have outstanding any security interest upon or with respect to, any of the present or future business, undertaking, assets or revenue (including any uncalled capital) of the Parent Company or any of its material subsidiaries to secure any indebtedness, subject to certain exceptions.

The US\$700,000, 5-year term loan will mature in September 2018.

### SPI

On September 27, 2013, SPI has entered into a P13,800,000, 10-year loan with a syndicate of banks. Of this amount, P12,300,000 and P1,500,000 were drawn on September 30, 2013 and 2014, respectively. The loan includes amount payable to a related party amounting to P3,451,000 and P3,119,565 as of December 31, 2014 and 2013, respectively (Note 18).

Pursuant to the Facility Agreement, the amount of the loan drawn down in 2014 and 2013 will bear interest at the rate of 6.5446% and 6.3131%, respectively, as determined by the Facility Agent. Effective November 28, 2014, step-down interest rate is at 6.2921% and 6.0606% for 2014 and 2013 loans, respectively. The Facility Agreement has a final maturity date of September 2023.

SPI may, by giving not less than thirty (30) days prior written notice to the Facility Agent, prepay the loan in whole or in part with accrued interest on the amount prepaid and subject to a repayment penalty of 1% of the principal amount being paid to be applied against the outstanding amounts due in the inverse order of maturity. The repayment schedule consists of forty (40) periods on a quarterly basis. First repayment of principal started December 2014.

The annual maturities on this loan are as follows:

| <b>Year</b>         | <b>Gross Amount</b> | <b>Debt Issue Costs</b> | <b>Net</b>  |
|---------------------|---------------------|-------------------------|-------------|
| 2015                | P1,373,100          | P43,063                 | P1,330,037  |
| 2016                | 1,573,200           | 39,444                  | 1,533,756   |
| 2017                | 1,573,200           | 35,107                  | 1,538,093   |
| 2018                | 1,573,200           | 30,581                  | 1,542,619   |
| 2019                | 1,573,200           | 25,733                  | 1,547,467   |
| 2020 and thereafter | 5,940,900           | 47,207                  | 5,893,693   |
|                     | P13,606,800         | P221,135                | P13,385,665 |

The Facility Agreement imposes a number of covenants on the part of SPI, including, but not limited to, maintaining a debt-to-equity ratio and a specified debt service coverage ratio throughout the duration specified under the Facility Agreement. The terms and conditions of the Facility Agreement contains certain limitations on the ability of SPI to declare or pay any dividend, distribution or other return of capital in respect of any ownership interest to SPI and any other payment to the Parent Company or its affiliates, subject to certain exceptions.

The loan is secured by the mortgage over the power plant and pledge of shares in SPI owned by the Parent Company (Note 12).

Loans payable amounted to P35,966,800 and P34,497,500 while accrued interest amounted to P17,794 and P22,483 as of December 31, 2014 and 2013, respectively. Total interest expense and financing charges on loans payable amounted to P1,380,328 and P527,527 (inclusive of P266,655 and P87,462 capitalized in construction in progress in 2014 and 2013, respectively; Note 12) in 2014 and 2013, respectively.

The amortization of debt issue costs of P173,978 and P89,912 is included as part of "Interest expense and other financing charges" account in the consolidated statements of income in 2014 and 2013, respectively.

As of December 31, 2014 and 2013, the Group is in compliance with the covenants of the debt agreements.

The movements in debt issue costs are as follow:

|                              | 2014             | 2013     |
|------------------------------|------------------|----------|
| Balance at beginning of year | <b>P727,115</b>  | P131,071 |
| Addition                     | <b>128,535</b>   | 689,051  |
| Amortization                 | <b>(173,978)</b> | (89,912) |
| Capitalized amount           | <b>(12,117)</b>  | (3,095)  |
| Balance at end of year       | <b>P669,555</b>  | P727,115 |

Contractual terms of the Group's interest bearing loans and borrowings and exposure to interest rate, foreign currency and liquidity risks are discussed in Note 25.

## 18. Related Party Disclosures

The Group, in the normal course of business, purchases products and services from and sells products and renders services to related parties. Transactions with related parties are made at normal market prices and terms. An assessment is undertaken at each financial year by examining the financial position of the related party and the market in which the related party operates.

The following are the transactions with related parties and the outstanding balances as of December 31:

|                                             | Note      | Year | Revenue from Related Parties | Purchases from Related Parties | Amounts Owed by Related Parties | Amounts Owed to Related Parties | Terms                      | Conditions    |
|---------------------------------------------|-----------|------|------------------------------|--------------------------------|---------------------------------|---------------------------------|----------------------------|---------------|
| SMC                                         |           | 2014 | P -                          | P267,336                       | P10,557                         | P18,009                         | On demand;                 | Unsecured;    |
|                                             |           | 2013 | -                            | 412,372                        | 252                             | 140,143                         | non-interest bearing       | no impairment |
| Entities Under Common Control               | 7, 12, 20 | 2014 | 7,814,823                    | 2,208,319                      | 852,839                         | 418,116                         | On demand;                 | Unsecured;    |
|                                             |           | 2013 | 1,831,882                    | 17,993,545                     | 522,697                         | 524,268                         | non-interest bearing       | no impairment |
| Associate                                   | 13        | 2014 | 878,650                      | -                              | 77,816                          | -                               | On demand;                 | Unsecured;    |
|                                             |           | 2013 | 167,550                      | -                              | 81,546                          | -                               | non-interest bearing       | no impairment |
| Associate of an Entity Under Common Control | 17        | 2014 | -                            | -                              | -                               | 3,451,000                       | 10 years; interest bearing | Secured       |
|                                             |           | 2013 | -                            | -                              | -                               | 3,119,565                       |                            |               |
|                                             |           | 2014 | P8,693,473                   | P2,475,655                     | P941,212                        | P3,887,125                      |                            |               |
|                                             |           | 2013 | P1,999,432                   | P18,405,917                    | P604,495                        | P3,783,976                      |                            |               |

- Amounts owed by related parties consist of trade and other receivables and security deposits.
- Amounts owed to related parties consist of trade payables, management fees, purchases of fuel, reimbursement of expenses, rent, insurance and services rendered by related parties.

- c. The amount owed to associate of an entity under common control consists of interest bearing loan obtained from Bank of Commerce included as part of “Long-term debt” account in the consolidated statements of financial position.
- d. The compensation of key management personnel of the Group amounted to P32,604 and P30,702 for the years ended December 31, 2014 and 2013, respectively.
- e. SMC offers shares of stock to employees of SMC and its subsidiaries under the ESPP. Under the ESPP, all permanent Philippine-based employees of SMC and its subsidiaries who have been employed for a continuous period of one year prior to the subscription period will be allowed to subscribe at a price equal to weighted average daily closing prices for three months prior to the offer period less 15% discount. A participating employee may acquire at least 100 shares of stock up to a maximum of 20,000 shares, subject to certain conditions, through payroll deductions (Note 3).

The ESPP requires the subscribed shares and stock dividends accruing thereto to be pledged to SMC until the subscription is fully-paid. The right to subscribe under the ESPP cannot be assigned or transferred. A participant may sell his shares after the second year from exercise date. The ESPP also allows subsequent withdrawal and cancellation of participant’s subscriptions under certain terms and conditions.

As of December 31, 2014 and 2013, the expenses related to ESPP amounted to nil and P505, respectively.

- f. The Group does not provide yet post-employment benefits to its employees. Management believes that the retirement expense is not significant based on the employees’ average age and years of service to the Group, and payroll costs as of December 31, 2014 and 2013.

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## 19. Equity

### Capital Stock

As of December 31, 2014 and 2013, the Parent Company’s authorized capital stock is P2,000,000, divided into 2,000,000,000 shares with par value of P1 per share.

Capital stock consists of:

|                              | 2014              | 2013       |
|------------------------------|-------------------|------------|
| Subscribed capital stock     | <b>P1,250,004</b> | P1,250,004 |
| Less subscription receivable | <b>187,500</b>    | 187,500    |
| Balance at end of year       | <b>P1,062,504</b> | P1,062,504 |

The number of shares subscribed is 1,250,003,500 shares as of December 31, 2014 and 2013.

### Reserves

Reserves consist of:

|                                                                                        | <i>Note</i> | <b>2014</b>     | <b>2013</b> |
|----------------------------------------------------------------------------------------|-------------|-----------------|-------------|
| Excess of net assets over purchase price of acquired subsidiaries under common control |             | <b>P785,279</b> | P785,279    |
| Share in other comprehensive loss of an associate - net                                |             |                 |             |
| Balance at beginning of year                                                           |             | -               | (39,306)    |
| Additions                                                                              | 13          | -               | 20,535      |
| Disposal                                                                               |             | -               | 18,771      |
| Balance at end of year                                                                 |             | -               | -           |
|                                                                                        |             | <b>P785,279</b> | P785,279    |

Excess of net assets over purchase price of acquired subsidiaries under common control pertains to the acquisitions of noncontrolling interest in SMEC and SPDC.

The share in other comprehensive loss of an associate consists of unrealized fair value gain on AFS financial assets and cumulative translation adjustments.

### Retained Earnings

The Group's unappropriated retained earnings include the Parent Company's accumulated earnings in subsidiaries and equity in net earnings of associates amounting to P427 and P12,978,115 in 2014 and 2013, respectively. Such amounts are not available for declaration as dividends until declared by the respective investees.

The Parent Company's BOD declared cash dividends as follows:

#### **December 31, 2014**

| <b>Date of Declaration</b> | <b>Stockholders of Record</b> | <b>Date Payable</b>      | <b>Dividend per share</b> | <b>Amount</b>      |
|----------------------------|-------------------------------|--------------------------|---------------------------|--------------------|
| <b>March 25, 2014</b>      | <b>March 25, 2014</b>         | <b>April 8, 2014</b>     | <b>P1.20</b>              | <b>P1,500,000</b>  |
| <b>June 3, 2014</b>        | <b>June 3, 2014</b>           | <b>June 10, 2014</b>     | <b>2.80</b>               | <b>3,500,000</b>   |
| <b>August 19, 2014</b>     | <b>August 19, 2014</b>        | <b>August 29, 2014</b>   | <b>2.00</b>               | <b>2,500,000</b>   |
| <b>November 4, 2014</b>    | <b>November 4, 2014</b>       | <b>November 11, 2014</b> | <b>2.00</b>               | <b>2,500,000</b>   |
|                            |                               |                          |                           | <b>P10,000,000</b> |

#### **December 31, 2013**

| <b>Date of Declaration</b> | <b>Stockholders of Record</b> | <b>Date Payable</b> | <b>Dividend per share</b> | <b>Amount</b>     |
|----------------------------|-------------------------------|---------------------|---------------------------|-------------------|
| February 19, 2013          | February 19, 2013             | February 28, 2013   | P0.80                     | P1,000,000        |
| May 3, 2013                | May 3, 2013                   | May 15, 2013        | 0.80                      | 1,000,000         |
| August 13, 2013            | August 13, 2013               | August 15, 2013     | 0.80                      | 1,000,000         |
| November 29, 2013          | November 29, 2013             | December 5, 2013    | 1.20                      | 1,500,000         |
|                            |                               |                     |                           | <b>P4,500,000</b> |

As of December 31, the Group's appropriated retained earnings, net of reversal are as follows:

|                | 2014               | 2013       |
|----------------|--------------------|------------|
| Parent Company | <b>P11,771,000</b> | P2,643,000 |
| SMEC           | <b>7,675,000</b>   | 1,800,000  |
| SPPC           | <b>7,352,300</b>   | 2,981,800  |
| SPDC           | <b>2,604,600</b>   | -          |
|                | <b>P29,402,900</b> | P7,424,800 |

#### Undated Subordinated Capital Securities (USCS)

On May 7, 2014, the Company issued and listed on the Singapore Stock Exchange, US\$300,000 USCS at an issue price of 100%.

The holders of the USCS are conferred a right to receive distribution on a semi-annual basis from their issue date at the rate of 7.5% per annum, subject to the step-up rate. The Company has a right to defer this distribution under certain conditions.

The USCS have no fixed redemption date and are redeemable in whole, but not in part, at the Company's option on November 7, 2019, or any distribution payment date thereafter or upon the occurrence of certain other events.

The proceeds were used by the Company to finance investments in power-related assets and other general corporate purposes.

## **20. Operating Expenses**

Operating expenses consist of:

|                                  | <i>Note</i> | 2014              | 2013       |
|----------------------------------|-------------|-------------------|------------|
| Donations                        |             | <b>P662,752</b>   | P240,060   |
| Management fees                  | 18          | <b>456,727</b>    | 409,373    |
| Taxes and licenses               |             | <b>406,979</b>    | 110,791    |
| Market fees                      | 7           | <b>233,701</b>    | 246,591    |
| Impairment losses on receivables | 9           | <b>144,393</b>    | 32,850     |
| Outside services                 |             | <b>143,492</b>    | 35,448     |
| Salaries, wages and benefits     | 18          | <b>140,128</b>    | 114,070    |
| Professional fees                |             | <b>130,019</b>    | 38,788     |
| Rent                             | 4, 7        | <b>115,849</b>    | 24,167     |
| Supplies                         |             | <b>46,451</b>     | 28,965     |
| Travel and transportation        |             | <b>45,467</b>     | 29,643     |
| Depreciation and amortization    | 12          | <b>43,774</b>     | 21,749     |
| Miscellaneous                    | 12          | <b>342,198</b>    | 215,255    |
|                                  |             | <b>P2,911,930</b> | P1,547,750 |

The Group's corporate social responsibility projects, included in the "Miscellaneous" account, amounted to P127,116 and P106,772 for the years ended December 31, 2014 and 2013, respectively.

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**21. Other Income (Charges)**

Other income (charges) consists of:

|                               | <i>Note</i> | <b>2014</b>      | 2013         |
|-------------------------------|-------------|------------------|--------------|
| PSALM monthly fees reduction  | 7           | <b>P814,565</b>  | P872,243     |
| Foreign exchange losses - net | 25          | <b>(813,621)</b> | (9,434,860)  |
| Miscellaneous income          |             | <b>67,281</b>    | 71,555       |
|                               |             | <b>P68,225</b>   | (P8,491,062) |

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**22. Income Taxes**

The components of income tax expense (benefit) are as follows:

|          | <b>2014</b>       | 2013        |
|----------|-------------------|-------------|
| Current  | <b>P1,608,293</b> | P686,311    |
| Deferred | <b>1,085,130</b>  | (1,522,613) |
|          | <b>P2,693,423</b> | (P836,302)  |

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Current income tax expense in 2014 and 2013 represents regular corporate income tax of 30% on taxable income, MCIT and final tax on interest income.

Deferred tax assets (liabilities) arise from the following:

|                                                                             | <b>2014</b>       | 2013     |
|-----------------------------------------------------------------------------|-------------------|----------|
| Difference of depreciation and other related expenses over monthly payments | <b>(P324,095)</b> | P806,712 |
| Allowance for impairment losses on receivables                              | <b>60,005</b>     | 14,328   |
|                                                                             | <b>(P264,090)</b> | P821,040 |

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The difference of depreciation and other related expenses over monthly payments represents timing difference between tax and accounting recognition of expenses.

The amounts above are reported in the consolidated statements of financial position as follows:

|                          | <b>2014</b>        | 2013        |
|--------------------------|--------------------|-------------|
| Deferred tax assets      | <b>P2,779,380</b>  | P2,909,105  |
| Deferred tax liabilities | <b>(3,043,470)</b> | (2,088,065) |
|                          | <b>(P264,090)</b>  | P821,040    |

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As of December 31, 2014, the NOLCO and MCIT of the Group that can be claimed as deduction from future taxable income and deduction from corporate income tax due, respectively, are as follows:

| <b>Year Incurred/Paid</b> | <b>Carryforward<br/>Benefits Up To</b> | <b>NOLCO</b> | <b>MCIT</b> |
|---------------------------|----------------------------------------|--------------|-------------|
| Year 2014                 | December 31, 2017                      | P2,073,953   | P14,230     |
| Year 2013                 | December 31, 2016                      | 2,187,455    | 12,766      |
| Year 2012                 | December 31, 2015                      | 1,577,233    | 7,417       |
|                           |                                        | P5,838,641   | P34,413     |

The reconciliation between the statutory income tax rate on income before income tax and the Group's effective income tax rate is as follows:

|                                                            | <b>2014</b>    | <b>2013</b> |
|------------------------------------------------------------|----------------|-------------|
| Statutory income tax rate                                  | <b>30.00%</b>  | 30.00%      |
| Increase (decrease) in the income tax rate resulting from: |                |             |
| Income subject to ITH                                      | <b>(7.87%)</b> | (76.30%)    |
| Nondeductible expenses and others                          | <b>(1.91%)</b> | 20.22%      |
| Effective income tax rate                                  | <b>20.22%</b>  | (26.08%)    |

## **23. Registrations and License**

### Registrations with the Board of Investments (BOI)

On August 21, 2007, SEPC was registered with the BOI under the Omnibus Investment Code of 1987 (Executive Order No. 226), as New Domestic Producer of Coal on a Non-pioneer Status and was entitled to certain incentives that include, among others, an Income Tax Holiday (ITH) for four years from June 2011 or date of actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration.

SMEC, SPDC and SPPC are registered with the BOI as administrator/operator of their respective power plant on a pioneer status with non-pioneer incentives and were granted ITH for four (4) years without extension beginning August 1, 2010 up to July 31, 2014, subject to compliance with certain requirements under their registrations. The ITH incentive availed was limited only to the sale of power generated from the power plants.

In 2013, SMCPC and SCPC were granted incentives by the BOI on a pioneer status for six (6) years beginning December 2015 and February 2016, respectively, or start of commercial operations whichever is earlier, subject to the representations and commitments set forth in the application for registration, the provisions of Omnibus Investments Code of 1987, the rules and regulations of the BOI and the terms and conditions prescribed. The ITH incentives shall be limited only to the revenues generated from the sale of the electricity from the power plants.

On September 3, 2013 and January 28, 2014, the BOI issued a Certificate of Authority to SMCPC and SCPC, respectively, subject to provisions and implementing rules and regulations of Executive Order No. 70, entitled “Reducing the Rates of Duty on Capital Equipment, Spare Parts and Accessories imported by BOI Registered New and Expanding Enterprises”. Authority shall be valid for one (1) year from the date of issuance. Advanced authority to import capital equipment was granted on May 21, 2013. For the subsequent year, BOI issued new Certificates of Authority dated March 6 and September 4, 2014 and February 6, 2015 to SMCPC and SCPC, respectively, both with a validity of one year from the date of issuance.

On March 4, 2014, the BOI approved the transfer of BOI Certificate of Registration Nos. 2013-047 and 2010-181 from Petron to SPI. Under the Certificates of Registration, SPI is entitled to certain incentives, including ITH incentives, for the revenue generated from the sale of electricity from the plant and sold to the grid, other entities and/or communities.

#### License Granted by the ERC

On August 22, 2011, SMELC was granted a Retail Electricity Supplier’s (RES) License by the ERC pursuant to Section 29 of the EPIRA which requires all suppliers of electricity to the contestable market to secure a license from the ERC. The term of the RES License is for a period of 5 years from the time it was granted and renewable thereafter.

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## **24. Basic and Diluted Earnings Per Share**

Basic and diluted EPS is computed as follows:

|                                                                  | <b>2014</b>        | <b>2013</b> |
|------------------------------------------------------------------|--------------------|-------------|
| Net income (a)                                                   | <b>P10,629,482</b> | P4,042,655  |
| Weighted average number of shares outstanding (in thousands) (b) | <b>1,250,004</b>   | 1,250,004   |
| Basic/diluted EPS (a/b)                                          | <b>P8.50</b>       | P3.23       |

As of December 31, 2014 and 2013, the Group has no dilutive debt or equity instruments.

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## **25. Financial Risk Management Objectives and Policies**

### Objectives and Policies

The Group has significant exposure to the following financial risks primarily from its use of financial instruments:

- Interest Rate Risk
- Foreign Currency Risk
- Liquidity Risk
- Credit Risk

This note presents information about the Group’s exposure to each of the foregoing risks, the Group’s objectives, policies and processes for measuring and managing these risks, and the Group’s management of capital.

There has been changes to the Group's exposure to the above risks or the manner in which it manages and measures the risks since prior year. The Group's overall strategy in managing its capital has likewise remained unchanged since prior year.

The Group's principal non-trade related financial instruments include cash and cash equivalents, other receivables (current and noncurrent), restricted cash, non-trade payables, and long-term debt. These financial instruments are used mainly for working capital management and investment purposes. The Group's trade-related financial assets and financial liabilities such as trade receivables, accounts payable and accrued expenses and finance lease liabilities arise directly from and are used to facilitate its daily operations.

The BOD has the overall responsibility for the establishment and oversight of the Group's risk management framework.

The BOD has established the Risk Management Committee, which is responsible for developing and monitoring the Group's risk management policies. The committee reports regularly to the BOD on its activities.

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The BOD oversees how management monitors compliance with SMC's risk management policies and procedures, and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The BOD is assisted in its oversight role by SMC's Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the BOD.

#### Interest Rate Risk

Interest rate risk is the risk that future cash flows from a financial instrument (cash flow interest rate risk) or its fair value (fair value interest rate risk) will fluctuate because of changes in market interest rates. The Group's exposure to changes in interest rates relates primarily to the Group's long-term borrowings. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. On the other hand, borrowings issued at variable rates expose the Group to cash flow interest rate risk.

Management is responsible for monitoring the prevailing market-based interest rate and ensures that the mark-up rates charged on its borrowings are optimal and benchmarked against the rates charged by other creditor banks.

On the other hand, the Group's investment policy is to maintain an adequate yield to match or reduce the net interest cost from its borrowings pending the deployment of funds to their intended use in the Group's operations and working capital management. However, the Group invests only in high-quality short-term investments and maintains the necessary diversification to avoid concentration risk.

In managing interest rate risk, the Group aims to reduce the impact of short-term fluctuations on the Group's earnings. Over the longer term, however, permanent changes in interest rates would have an impact on profit or loss.

The management of interest rate risk is also supplemented by monitoring the sensitivity of the Group's financial instruments to various standard and non-standard interest rate scenarios. Interest rate movements affect reported equity from increases or decreases in interest income or interest expense as well as fair value changes reported in profit or loss, if any.

The sensitivity to a reasonably possible 1% increase in the interest rates, with all other variables held constant, would have decreased the Group's profit before tax (through the impact on floating rate borrowings) by P6,388 and P11,893 in 2014 and 2013, respectively. A 1% decrease in the interest rate would have had the equal but opposite effect. These changes are considered to be reasonably possible given the observation of prevailing market conditions in those periods. There is no impact on the Group's equity.

#### Interest Rate Risk Table

The terms and maturity profile of the interest-bearing financial instruments, together with its gross amounts, are shown in the following tables:

| <b>December 31, 2014</b>                                       | <b>&lt;1 Year</b> | <b>1-2 Years</b>   | <b>&gt;2-3 Years</b> | <b>&gt;3-4 Years</b> | <b>&gt;4-5 Years</b> | <b>&gt;5 Years</b> | <b>Total</b>       |
|----------------------------------------------------------------|-------------------|--------------------|----------------------|----------------------|----------------------|--------------------|--------------------|
| <b>Fixed Rate</b>                                              |                   |                    |                      |                      |                      |                    |                    |
| Philippine peso-denominated                                    | P1,223,850        | P1,402,200         | P1,402,200           | P1,402,200           | P1,402,200           | P5,295,150         | P12,127,800        |
| Step-down interest rate                                        | 6.0606%           | 6.0606%            | 6.0606%              | 6.0606%              | 6.0606%              | 6.0606%            | -                  |
| Philippine peso-denominated                                    | 149,250           | 171,000            | 171,000              | 171,000              | 171,000              | 645,750            | 1,479,000          |
| Step-down interest rate                                        | 6.2921%           | 6.2921%            | 6.2921%              | 6.2921%              | 6.2921%              | 6.2921%            | -                  |
| Foreign currency-denominated<br>(expressed in Philippine peso) | -                 | 13,416,000         | -                    | -                    | -                    | -                  | 13,416,000         |
| Interest rate                                                  |                   | 7%                 |                      |                      |                      |                    |                    |
| <b>Floating Rate</b>                                           |                   |                    |                      |                      |                      |                    |                    |
| Foreign currency-denominated<br>(expressed in Philippine peso) | -                 | -                  | -                    | 22,360,000           | -                    | -                  | 22,360,000         |
| Interest rate                                                  |                   |                    |                      | LIBOR +<br>Margin    |                      |                    |                    |
|                                                                | <b>P1,373,100</b> | <b>P14,989,200</b> | <b>P1,573,200</b>    | <b>P23,933,200</b>   | <b>P1,573,200</b>    | <b>P5,940,900</b>  | <b>P49,382,800</b> |

  

| <b>December 31, 2013</b>                                       | <b>&lt;1 Year</b> | <b>1-2 Years</b>  | <b>&gt;2-3 Years</b> | <b>&gt;3-4 Years</b> | <b>&gt;4-5 Years</b> | <b>&gt;5 Years</b> | <b>Total</b>       |
|----------------------------------------------------------------|-------------------|-------------------|----------------------|----------------------|----------------------|--------------------|--------------------|
| <b>Fixed Rate</b>                                              |                   |                   |                      |                      |                      |                    |                    |
| Philippine peso-denominated                                    | P172,200          | P1,223,850        | P1,402,200           | P1,402,200           | P1,402,200           | P6,697,350         | P12,300,000        |
| Interest rate                                                  | 6.3131%           | 6.3131%           | 6.3131%              | 6.3131%              | 6.3131%              | 6.3131%            | -                  |
| Foreign currency-denominated<br>(expressed in Philippine peso) | -                 | -                 | 13,318,500           | -                    | -                    | -                  | 13,318,500         |
| Interest rate                                                  | -                 | -                 | 7%                   | -                    | -                    | -                  | -                  |
| <b>Floating Rate</b>                                           |                   |                   |                      |                      |                      |                    |                    |
| Foreign currency-denominated<br>(expressed in Philippine peso) | -                 | -                 | -                    | -                    | 22,197,500           | -                  | 22,197,500         |
| Interest rate                                                  |                   |                   |                      |                      | LIBOR +<br>margin    |                    |                    |
|                                                                | <b>P172,200</b>   | <b>P1,223,850</b> | <b>P14,720,700</b>   | <b>P1,402,200</b>    | <b>P23,599,700</b>   | <b>P6,697,350</b>  | <b>P47,816,000</b> |

#### Foreign Currency Risk

The Group's exposure to foreign currency risk results from significant movements in foreign exchange rates that adversely affect the foreign currency-denominated transactions of the Group. The Group's risk management objective with respect to foreign currency risk is to reduce or eliminate earnings volatility and any adverse impact on equity.

Information on the Group's foreign currency-denominated monetary assets and monetary liabilities and their Philippine peso equivalents as of December 31 are as follows:

|                                                       |             | 2014                 |                     | 2013          |                    |
|-------------------------------------------------------|-------------|----------------------|---------------------|---------------|--------------------|
|                                                       | <i>Note</i> | US Dollar            | Peso<br>Equivalent  | US Dollar     | Peso<br>Equivalent |
| <b>Assets</b>                                         |             |                      |                     |               |                    |
| Cash and cash equivalents                             |             | <b>US\$260,178</b>   | <b>P11,635,160</b>  | US\$299,660   | P13,303,411        |
| Trade and other receivables                           |             | <b>83,937</b>        | <b>3,753,513</b>    | 22,649        | 1,005,512          |
| Prepaid and other current assets                      |             | -                    | -                   | 26,448        | 1,174,159          |
|                                                       |             | <b>344,115</b>       | <b>15,388,673</b>   | 348,757       | 15,483,082         |
| <b>Liabilities</b>                                    |             |                      |                     |               |                    |
| Accounts payable and accrued expenses                 |             | <b>148,277</b>       | <b>6,633,727</b>    | 30,369        | 1,348,227          |
| Finance lease liabilities                             | 7           | <b>2,216,977</b>     | <b>99,143,265</b>   | 2,350,421     | 104,346,941        |
| Long-term debt                                        | 7, 17       | <b>800,000</b>       | <b>35,776,000</b>   | 800,000       | 35,516,000         |
|                                                       |             | <b>3,165,254</b>     | <b>141,552,992</b>  | 3,180,790     | 141,211,168        |
| Net foreign currency-denominated monetary liabilities |             | <b>US\$2,821,139</b> | <b>P126,164,319</b> | US\$2,832,033 | P125,728,086       |

The Group reported net unrealized foreign exchange losses amounting to P1,584,500 and P9,592,617 in 2014 and 2013, respectively, with the translation of its foreign currency-denominated assets and liabilities. These mainly resulted from the movement of the Philippine peso against US dollar as shown in the following table:

|                          | <b>US Dollar<br/>to Philippine<br/>Peso</b> |
|--------------------------|---------------------------------------------|
| <b>December 31, 2014</b> | <b>P44.720</b>                              |
| December 31, 2013        | 44.395                                      |

The management of foreign currency risk is also supplemented by monitoring the sensitivity of the Group's financial instruments to various foreign currency exchange rate scenarios. Foreign exchange movements affect reported equity from increases or decreases in unrealized and realized foreign exchange gains or losses.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and monetary liabilities) for the years ended December 31:

|                                           | 2014                                                              |                                                                   | 2013                                                   |                                                        |
|-------------------------------------------|-------------------------------------------------------------------|-------------------------------------------------------------------|--------------------------------------------------------|--------------------------------------------------------|
|                                           | <b>P1 Decrease<br/>in the US<br/>Dollar<br/>Exchange<br/>Rate</b> | <b>P1 Increase<br/>in the US<br/>Dollar<br/>Exchange<br/>Rate</b> | P1 Decrease<br>in the US<br>Dollar<br>Exchange<br>Rate | P1 Increase<br>in the US<br>Dollar<br>Exchange<br>Rate |
| Cash and cash equivalents                 | <b>(P260,178)</b>                                                 | <b>P260,178</b>                                                   | (P299,660)                                             | P299,660                                               |
| Trade and other receivables               | <b>(83,937)</b>                                                   | <b>83,937</b>                                                     | (22,649)                                               | 22,649                                                 |
| Prepaid expenses and other current assets | -                                                                 | -                                                                 | (26,448)                                               | 26,448                                                 |
|                                           | <b>(344,115)</b>                                                  | <b>344,115</b>                                                    | (348,757)                                              | 348,757                                                |
| Accounts payable and accrued expenses     | <b>148,277</b>                                                    | <b>(148,277)</b>                                                  | 30,369                                                 | (30,369)                                               |
| Finance lease liabilities                 | <b>2,216,977</b>                                                  | <b>(2,216,977)</b>                                                | 2,350,421                                              | (2,350,421)                                            |
| Long-term debt                            | <b>800,000</b>                                                    | <b>(800,000)</b>                                                  | 800,000                                                | (800,000)                                              |
|                                           | <b>3,165,254</b>                                                  | <b>(3,165,254)</b>                                                | 3,180,790                                              | (3,180,790)                                            |
|                                           | <b>P2,821,139</b>                                                 | <b>(P2,821,139)</b>                                               | P2,832,033                                             | (P2,832,033)                                           |

Exposures to foreign exchange rates vary during the year depending on the volume of foreign currency-denominated transactions. Nonetheless, the analysis above is considered to be representative of the Group's currency risk.

#### Liquidity Risk

Liquidity risk pertains to the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

The Group's objectives to manage its liquidity risk are as follows: a) to ensure that adequate funding is available at all times; b) to meet commitments as they arise without incurring unnecessary costs; c) to be able to access funding when needed at the least possible cost; and d) to maintain an adequate time spread of refinancing maturities.

The Group constantly monitors and manages its liquidity position, liquidity gaps and surplus on a daily basis. A committed standby credit facility from several local banks is also available to ensure availability of funds when necessary.

The table below summarizes the maturity profile of the Group's financial assets and financial liabilities based on contractual undiscounted receipts and payments used for liquidity management as of December 31:

| 2014                                                                     | Carrying Amount | Contractual Cash Flow | 1 Year or Less | 1 Year - 2 Years | 2 Years - 5 Years | Over 5 Years |
|--------------------------------------------------------------------------|-----------------|-----------------------|----------------|------------------|-------------------|--------------|
| <b>Financial Assets</b>                                                  |                 |                       |                |                  |                   |              |
| Cash and cash equivalents                                                | P38,304,294     | P38,304,294           | P38,304,294    | P -              | P -               | P -          |
| Trade and other receivables - net                                        | 18,208,339      | 18,208,339            | 18,208,339     | -                | -                 | -            |
| Restricted cash (included under "Other noncurrent assets" account)       | 1,054,801       | 1,054,801             | 1,054,801      | -                | -                 | -            |
| Noncurrent receivable (included under "Other noncurrent assets" account) | 179,129         | 179,129               | -              | 179,129          | -                 | -            |
| <b>Financial Liabilities</b>                                             |                 |                       |                |                  |                   |              |
| Accounts payable and accrued expenses (excluding statutory payables)     | 23,331,447      | 23,331,447            | 23,331,447     | -                | -                 | -            |
| Finance lease liabilities (including current portion)                    | 186,303,745     | 248,175,447           | 22,091,404     | 23,170,046       | 71,935,991        | 130,978,006  |
| Long-term debt - net (including current portion)                         | 48,713,245      | 49,382,800            | 1,373,100      | 14,989,200       | 27,079,600        | 5,940,900    |
| 2013                                                                     | Carrying Amount | Contractual Cash Flow | 1 Year or Less | 1 Year - 2 Years | 2 Years - 5 Years | Over 5 Years |
| <b>Financial Assets</b>                                                  |                 |                       |                |                  |                   |              |
| Cash and cash equivalents                                                | P29,125,171     | P29,125,171           | P29,125,171    | P -              | P -               | P -          |
| Trade and other receivables - net                                        | 31,540,444      | 31,540,444            | 31,540,444     | -                | -                 | -            |
| Restricted cash (included under "Other noncurrent assets" account)       | 1,800,438       | 1,800,438             | 1,800,438      | -                | -                 | -            |
| Noncurrent receivable (included under "Other noncurrent assets" account) | 305,281         | 305,281               | -              | 126,152          | 179,129           | -            |
| <b>Financial Liabilities</b>                                             |                 |                       |                |                  |                   |              |
| Accounts payable and accrued expenses (excluding statutory payables)     | 16,947,172      | 16,947,172            | 16,947,172     | -                | -                 | -            |
| Finance lease liabilities (including current portion)                    | 195,002,721     | 267,421,551           | 20,116,894     | 22,013,873       | 70,035,556        | 155,255,228  |
| Long-term debt - net (including current portion)                         | 47,088,885      | 47,816,000            | 172,200        | 1,223,850        | 39,722,600        | 6,697,350    |

### Credit Risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's trade and other receivables. The Group manages its credit risk mainly through the application of transaction limits and close risk monitoring. It is the Group's policy to enter into transactions with creditworthy customer or counterparty to mitigate any significant concentration of credit risk.

The Group has regular internal control reviews to monitor the granting of credit and management of credit exposures. Where appropriate, the Group obtains collateral or arranges master netting agreements.

### *Trade and Other Receivables*

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer or counterparty. However, management also considers the demographics of the Group's customer base, including the default risk of the industry in which customers or counterparties operate, as these factors may have an influence on the credit risk.

The Group has established a credit policy under which each new customer or counterparty is analyzed individually for creditworthiness before the Group's standard payment terms and conditions are offered. The Group ensures that sales on account are made to customers with appropriate credit history. The Group has detailed credit criteria and several layers of credit approval requirements before engaging a particular customer or counterparty. The Group's review includes external ratings, when available, and in some cases bank references. Purchase limits are established for each customer and are reviewed on a regular basis. Customers that fail to meet the Group's benchmark creditworthiness may transact with the Group only on a prepayment basis.

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in respect of trade and other receivables. The main components of this allowance include a specific loss component that relates to individually significant exposures, and, as applicable, a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

Financial information on the Group's maximum exposure to credit risk as of December 31, without considering the effects of collaterals and other risk mitigation techniques, is presented below.

|                                   | 2014               | 2013        |
|-----------------------------------|--------------------|-------------|
| Cash and cash equivalents         | <b>P38,303,999</b> | P29,125,021 |
| Trade and other receivables - net | <b>18,208,339</b>  | 31,540,444  |
| Restricted cash                   | <b>1,054,801</b>   | 1,800,438   |
| Noncurrent receivable             | <b>179,129</b>     | 305,281     |
|                                   | <b>P57,746,268</b> | P62,771,184 |

The credit risk for cash and cash equivalents is considered negligible, since the counterparties are reputable entities with high quality external credit ratings.

The Group has no significant concentration of credit risk since the Group deals with a large number of homogeneous trade customers. The Group does not execute any credit guarantee in favor of any counterparty.

#### Capital Management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its businesses and maximize shareholder value.

The Group manages its capital structure and makes adjustments, in the light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, distribution payment, pay-off existing debts, return capital to shareholders or issue new shares, subject to compliance with certain covenants of its long-term debt and USCS (Notes 17 and 19).

The Group defines capital as capital stock, additional paid-in capital, USCS and retained earnings, both appropriated and unappropriated.

The BOD has overall responsibility for monitoring capital in proportion to risk. Profiles for capital ratios are set in the light of changes in the Group's external environment and the risks underlying the Group's business, operation and industry.

The Group monitors capital on the basis of debt-to-equity ratio, which is calculated as total debt divided by total equity. Total debt is defined as total current liabilities and total noncurrent liabilities, while equity is total equity as shown in the consolidated statements of financial position.

## 26. Financial Assets and Financial Liabilities

The table below presents a comparison by category of carrying amounts and fair values of the Group's financial instruments as of December 31:

|                                                                          | 2014                |                     | 2013            |              |
|--------------------------------------------------------------------------|---------------------|---------------------|-----------------|--------------|
|                                                                          | Carrying Amount     | Fair Value          | Carrying Amount | Fair Value   |
| <b>Financial Assets</b>                                                  |                     |                     |                 |              |
| Cash and cash equivalents                                                | <b>P38,304,294</b>  | <b>P38,304,294</b>  | P29,125,171     | P29,125,171  |
| Trade and other receivables - net                                        | <b>18,208,339</b>   | <b>18,208,339</b>   | 31,540,444      | 31,540,444   |
| Restricted cash (included under "Other noncurrent assets" account)       | <b>1,054,801</b>    | <b>1,054,801</b>    | 1,800,438       | 1,800,438    |
| Noncurrent receivable (included under "Other noncurrent assets" account) | <b>179,129</b>      | <b>179,129</b>      | 305,281         | 305,281      |
|                                                                          | <b>P57,746,563</b>  | <b>P57,746,563</b>  | P62,771,334     | P62,771,334  |
| <b>Financial Liabilities</b>                                             |                     |                     |                 |              |
| Accounts payable and accrued expenses (excluding statutory payables)     | <b>P23,331,447</b>  | <b>P23,331,447</b>  | P16,947,172     | P16,947,172  |
| Finance lease liabilities (including current portion)                    | <b>186,303,745</b>  | <b>186,303,745</b>  | 195,002,721     | 195,002,721  |
| Long-term debt - net (including current portion)                         | <b>48,713,245</b>   | <b>51,311,719</b>   | 47,088,885      | 50,850,121   |
|                                                                          | <b>P258,348,437</b> | <b>P260,946,911</b> | P259,038,778    | P262,800,014 |

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:

*Cash and Cash Equivalents, Trade and Other Receivables, Restricted Cash, Noncurrent Receivable, Accounts Payable and Accrued Expenses (excluding statutory payables).* The carrying amounts of these financial assets and financial liabilities approximate fair values primarily due to the relatively short-term nature/maturities of these financial instruments. The fair value of other receivable (noncurrent) is based on the present value of expected future cash flows using applicable discount rates based on current market rates of identical or similar quoted instruments.

*Long-term Debt.* The fair value of interest-bearing fixed-rate loans is based on the discounted value of expected future cash flows using the applicable market rates for similar types of instruments as of reporting date. The discount rates used for Philippine peso-denominated loan range from 2.54% to 4.29% and from 0.49% to 3.80% as of December 31, 2014 and 2013, respectively. The discount rates used for foreign currency-denominated loans range from 0.17% to 0.63% and 0.16% to 0.56% as of December 31, 2014 and 2013, respectively. The carrying amounts of floating rate loans with quarterly interest rate repricing approximate their fair values.

The fair value of the long-term debt was categorized as Level 2 in the fair value hierarchy based on inputs other than quoted prices included within Level 1 that are observable at the reporting date. The Group has no financial instruments valued based on Level 1 and Level 3 as of December 31, 2014 and 2013. During the year, 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.

*Finance Lease Liabilities.* The fair value is based on the present value of expected cash flows using the applicable discount rates based on current market rates of similar instruments.

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## 27. Other Matters

a. Contingencies

The Company is a party to certain cases or claims filed by third parties which are either pending decision by the court/regulators or are subject to settlement agreements. The outcome of these cases or claims cannot be presently determined (Note 4).

b. Generation Payments to PSALM

SPPC disputed the claims of PSALM for energy fees. The claims arose from differing interpretations of certain provisions in the IPPA Agreement related to energy fees, the fees payable to PSALM for the generation of power to customers. SPPC's management is in discussions with PSALM to secure a common understanding through amicable means. However, management and its legal counsel assessed that SPPC's bases for the amounts due to PSALM are consistent with the terms of the Ilijan IPPA Agreement. The information usually required is not disclosed on the grounds that it may prejudice the outcome of the discussion.

c. Temporary Restraining Order (TRO) Issued to Meralco

On December 23, 2013, the Supreme Court (SC) issued a TRO, effective immediately, preventing Meralco from collecting from its customers the power rate increase pertaining to November 2013 billing. As a result, Meralco was constrained to fix its generation rate to its October 2013 level of P5.67/kWh. Claiming that since the power supplied by generators, including SMEC and SPPC is billed to Meralco's customers on a pass-through basis, Meralco deferred a portion of its payment on the ground that it was not able to collect the full amount of its generation cost. Further, on December 27, 2013, the Department of Energy (DOE), the ERC and the PEMC, acting as a tripartite committee, issued a joint resolution setting a reduced price cap on the WESM of P32/kWh. The price will be effective for 90 days until a new cap is decided upon. As of December 31, 2013, the outcome of this case cannot be determined.

On January 16, 2014, the SC granted Meralco's plea to include other power supplier and generation companies, including SMEC and SPPC, as respondents to an inquiry. On February 18, 2014, the SC extended the period of the TRO until April 22, 2014 and enjoined the respondents (PEMC and the generators) from demanding and collecting the deferred amounts.

On March 3, 2014, the ERC issued an order declaring the November and December 2013 Luzon WESM prices void and imposed the application of regulated prices. Accordingly, SMEC, SPPC and SPDC recognized a reduction in the sale of power while SMELC recognized a reduction in its power purchases. Consequently, a payable and receivable were also recognized for the portion of over-collection or over-payment. The settlement of which shall be covered by a 24-month Special Payment Arrangement (SPA) agreed with PEMC which took effect in June 2014. On June 26, 2014, SMEC, SPPC and SPDC filed with the Court of Appeals a Petition for Review of these orders.

d. Commitments

The outstanding purchase commitments of the Group as of December 31, 2014 amounted to P4,581,000.

Amount authorized but not yet disbursed for capital projects as of December 31, 2014 is approximately P39,379,030.

e. Electric Power Industry Reform Act of 2001

The EPIRA sets forth the following: (a) Section 49 created PSALM to take ownership and manage the orderly sale, disposition and privatization of all existing NPC generation assets, liabilities, IPP contracts, real estate and all other disposable assets; (b) Section 31(c) requires the transfer of the management and control of at least seventy percent (70%) of the total energy output of power plants under contract with NPC to the IPP Administrators as one of the conditions for retail competition and open access; and (c) Pursuant to Section 51(c), PSALM has the power to take title to and possession of the IPP contracts and to appoint, after a competitive, transparent and public bidding, qualified independent entities who shall act as the IPP Administrators in accordance with the EPIRA. In accordance with the bidding procedures and supplemented bid bulletins thereto to appoint an IPP Administrator relative to the capacity of the IPP contracts, PSALM has conducted a competitive, transparent and open public bidding process following which the Group was selected winning bidder of the IPPA Agreements discussed in Note 7.

The EPIRA requires generation and distribution utility (DU) companies to undergo public offering within 5 years from the effective date, and provides cross ownership restrictions between transmission and generation companies. If the holding company of generation and DU companies is already listed with the PSE, the generation company or the DU need not comply with the requirement since such listing of the holding company is deemed already as compliance with the EPIRA.

A DU is allowed to source from an associated company engaged in generation up to 50% of its demand except for contracts entered into prior to the effective date of the EPIRA. Generation companies are restricted from owning more than 30% of the installed generating capacity of a grid and/or 25% of the national installed generating capacity.

f. Subsequent Events

On March 25, 2015, the Parent Company and SMEC declared cash dividends amounting to P1,500,000 and P2,000,000, respectively, to stockholders of record on the same date which is payable on March 31, 2015.

On the same date, the BOD confirmed and ratified the Group's acquisition of 100% equity interest in Ondarre Holding Corporation and the incorporation of the following companies:

|                                        | Percentage of<br>ownership |
|----------------------------------------|----------------------------|
| <b>Parent Company</b>                  |                            |
| Limay Premiere Power Corp.             | 100                        |
| Central Luzon Premiere Power Corp.     | 100                        |
| Mariveles Power Generation Corporation | 100                        |
| Mantech Power Dynamics Services Inc.   | 100                        |
| Safetech Power Services Corp.          | 100                        |
| <b>SMEC</b>                            |                            |
| Golden Quest Investment Inc.           | 100                        |

# COVER SHEET

for  
AUDITED FINANCIAL STATEMENTS

SEC Registration Number

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Company Name

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Principal Office ( No./Street/Barangay/City/Town)Province)

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Department requiring the report

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Secondary License Type, If  
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## COMPANY INFORMATION

Company's Email Address

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Company's Telephone Number/s

667-5390

Mobile Number

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No. of Stockholders

|  |
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Annual Meeting  
Month/Day

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Fiscal Year  
Month/Day

December 31

## CONTACT PERSON INFORMATION

The designated contact person MUST be an Officer of the Corporation

Name of Contact Person

Mr. Alexander Benhur M. Simon

Email Address

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Telephone  
Number/s

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Mobile Number

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Contact Person's Address

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**Note:** In case of death, resignation or cessation of office of the officer designated as contact person, such incident shall be reported to the Commission within thirty (30) calendar days from the occurrence thereof with information and complete contact details of the new contact person designated.