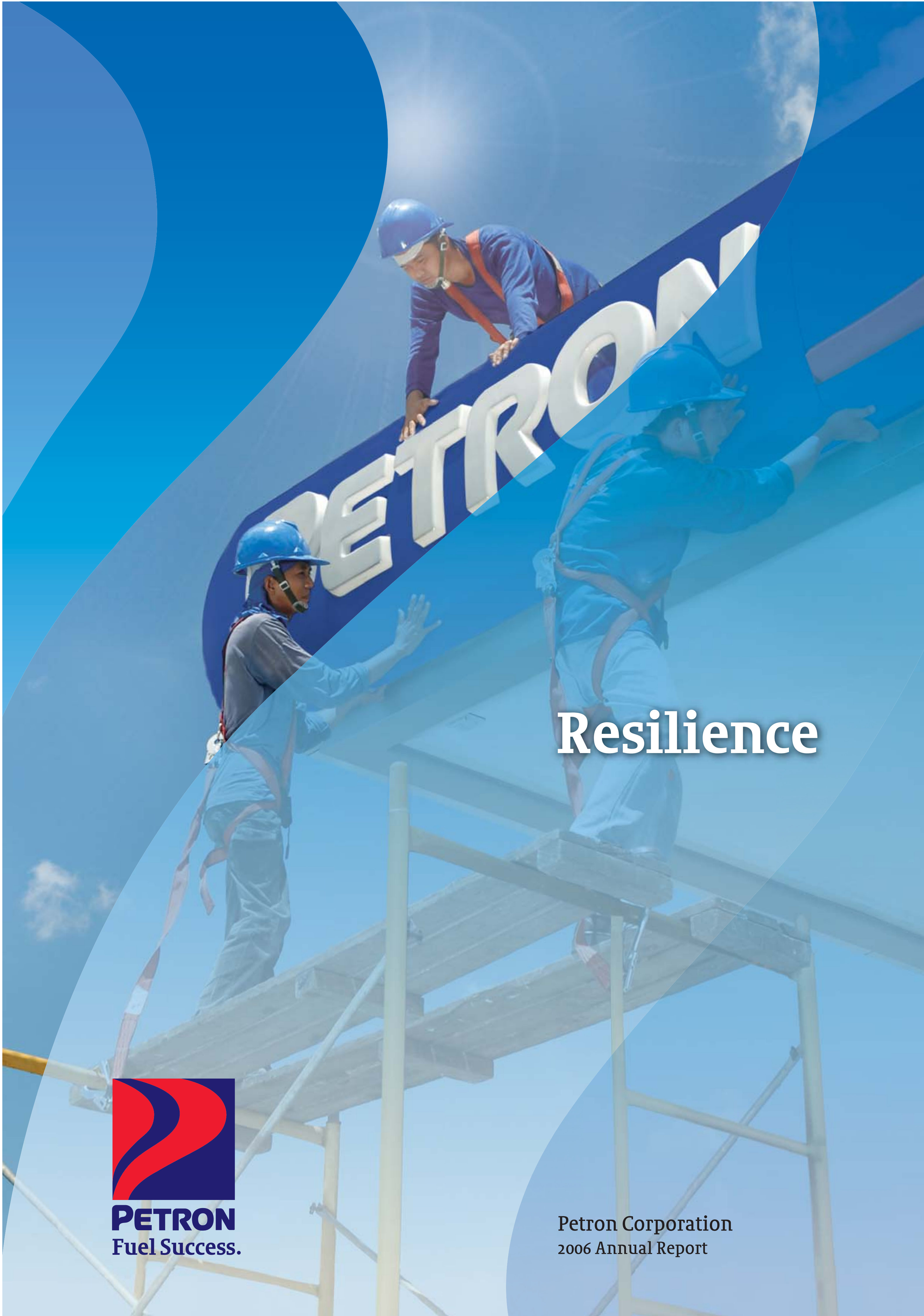

Resilience

Petron Corporation
2006 Annual Report

PETRON
Fuel Success.

Company Profile

Petron Corporation is the largest oil refining and marketing company in the Philippines. Supplying nearly 40% of the country's oil requirements, our world-class products and quality services fuel the lives of millions of Filipinos. We are dedicated and passionate about our vision to be the leading provider of total customer solutions in the energy sector and its derivative businesses.

We operate a refinery in Limay, Bataan, with a rated capacity of 180,000 barrels a day. Our ISO-14001-certified refinery processes crude oil into a full range of petroleum products including LPG, gasoline, diesel, jet fuel, kerosene, industrial fuel oil, solvents, asphalts, and mixed xylene.

From the refinery, we move our products mainly by sea to 31 depots and terminals situated all over the country. Through this nationwide network, we supply fuel oil, diesel, and LPG to various industrial customers. The power sector is our largest customer.

We also supply jet fuel at key airports to international and domestic carriers.

Through more than 1,200 service stations, we retail gasoline, diesel and kerosene to motorists and public transport operators. We also sell our LPG brand Gasul to households and other consumers through an extensive dealership network.

We operate a world-class lube oil blending plant at our Pandacan Terminal, where we manufacture lubes and greases. These are also sold through service stations and sales centers.

We are expanding our non-fuel businesses which include our convenience store brand "Treats." We have partnered with major food chains and other consumer services to give our customers a one-stop full service experience. We are also putting up additional company-owned and operated service stations in strategic locations.

We are publicly-listed. The Philippine National Oil Company and the Aramco Overseas Company B.V. each owns a 40% share of equity. The remaining 20% is held by close to 200,000 individual stockholders.

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Vision Mission Values

To be the Leading Provider of Total Customer Solutions in the Energy Sector and its Derivative Businesses. We will achieve this by:

- **Being an integral part of our customers' lives, delivering a consistent customer experience thru innovative products and services;**
- **Developing strategic partnerships in pursuit of growth and opportunity;**
- **Leveraging our refining assets to achieve competitive advantage;**
- **Fostering an entrepreneurial culture that encourages teamwork, innovation and excellence;**
- **Caring for our community and environment;**
- **Conducting ourselves with professionalism, integrity and fairness;**
- **Promoting the best interest of all our stakeholders.**

Message to Our
Stockholders

NICASIO I. ALCANTARA
Chairman and Chief Executive Officer

KHALID D. AL-FADDAGH
President

We believe that a culture of resilience underlies our capacity to cope with the adverse developments that came our way in 2006, and is one major reason for our continued success in a changing market. The organizational norms that account for this resilient performance include focus, determination, astuteness, optimization, forward-thinking, and compassion. It is from this perspective that we present our accomplishments for the year.

Resilience Amidst Trying Times

We are pleased to report that in spite of extraordinary challenges that we faced in 2006, your company achieved a net income of ₱6.02 billion, which approximately matches our income in 2005. This attests to the resilience of the company and our drive to sustain the record-breaking performance that we attained in 2005.

We achieved this in an environment of volatile crude prices, where Dubai averaged at $61.50 per barrel or more than $12.00 higher than the 2005 figure of $49.30. By the middle of 2006, we were actually on track to surpass our earnings for the previous year. However, crude prices fell steeply in September after reaching record highs in July-August, and as a result, we incurred inventory losses amounting to ₱1.6 billion.

The pressure on our income in the third quarter spurred us to work harder to reach our annual targets. Through aggressive marketing campaigns, our domestic sales grew in the fourth quarter despite continued weakness in domestic demand.

We ended the year with an overall market share of 38.8%, up by 0.7 percentage points compared to 2005. We also widened our edge over our nearest competitor to 7.4 percentage points from 6.5 in 2005. Our full-year domestic sales declined in line with the industry trend, but we managed to contain the drop to 5.8% compared to the 7.5% contraction in local oil demand reported by the Department of Energy. Overall, our sales volume increased by 0.8%, aided by a robust growth of 37.1% in our exports.

We also focused on improving operating efficiency, with the result that our operating expense was about 1% lower than the previous year's figure.

An Unusual Test: Guimaras

Our steady business performance in 2006 amidst a very tough business environment was remarkable. That we had to deal with one of the most difficult challenges ever to confront the company made it even more so.

On August 11, 2006, a tanker that we contracted to haul fuel oil to a customer in Mindanao sank in heavy seas off the coast of Guimaras Island in the Visayas. Most of its fuel oil cargo of two million liters spilled into the sea and landed in the southern coastline of Guimaras. Our response was immediate as we took charge of the oil spill clean-up, undertook relief operations for the affected communities, and committed to the rehabilitation of these areas. We worked with government, NGOs, the academe, and the International Oil Pollution Compensation Fund to ensure an organized and expert approach to the problem. And at any given time, up to about 10% of our workforce was involved as employees volunteered to assist in the operations.

Message to Our
Stockholders

Despite our best efforts to address the consequences of the oil spill, the incident spawned a number of issues that were played up in media. Thus, while we were financially covered through our participation in the International Oil Pollution Compensation Fund, the threat to our reputation was significant as hostile environment advocates and other groups rode the bandwagon of publicity in the weeks following the event.

To present the facts to you, our stockholders, we have prepared a report on Guimaras which we are including as a special section in this annual report.

Our Strengths

We believe that a *culture of resilience* underlies our capacity to cope with the adverse developments that came our way in 2006, and is one major reason for our continued success in a changing market. The organizational norms that account for our resilient performance include *focus, determination, astuteness, optimization, forward-thinking,* and *compassion.* It is from this perspective that we present our accomplishments for the year.

Focus is evident in how we have developed our products and services around the needs of our customers. Last year, we continued to introduce new products as well as new product formulations for both the fuels and lubes markets, all aimed at enhancing engine efficiency, fuel economy, and thus customer satisfaction. We also continued to construct more service stations in strategic locations, including company-operated stations with convenience stores and other non-fuel offerings.

Determination marks our drive to protect our leadership in an increasingly competitive industry. In the hotly contested retail market, we remained No.1 and our market share even improved to 34.8% versus 33.7% in 2005. Determination also shows in our unrelenting pursuit of operational improvements, reflected in new ISO certifications and unbroken safety records at our facilities across the country.

Astuteness shows in our financial decisions - from managing foreign exchange risk to securing low-cost financing for our major refinery investments - and is reflected in our having secured the highest possible rating for creditworthiness from PhilRatings, the Philippines' pioneer credit rating agency.

Forward-thinking is about anticipating change and discerning opportunities for growth. Our $300 million Refinery Masterplan – the group of refinery projects now under construction and due for commissioning in 2008 – is a product of this. As we aim to meet the product requirements of the mature fuels market more efficiently, we draw on refinery synergies to diversify into profitable petrochemicals. Likewise, our partnership with Innospec, the leading global additives supplier, will open up new markets for our lubricants in the Asia-Pacific region.

Optimization is seen in our efforts to reduce costs and raise productivity. Examples include a number of successful initiatives to improve energy efficiency at the refinery. We also introduced process improvements in the area of information technology, using our home-grown IT experts to upgrade our online, real-time enterprise-wide information software called SAP and thereby saving the company millions of pesos.

Last but not least, **Compassion** fuels our drive for sustainable development. By subscribing to a larger cause that aims for the long-term well-being of society, we reinforce our stake in the viability of the company. Thus, our continuing Corporate Social Responsibility programs for child education (*Tulong Aral* and the Petron Schools) as well as for the environment (Coastal Management) are an integral part of our corporate culture. Our response to the Guimaras incident was only part of a broader commitment to assist disaster-stricken communities.

Our Rewards

Petron's culture of resilience is borne out by the company's historical performance; rebounding from a ₱2.5 billion loss in 2000, Petron's income grew from ₱1.2 billion in 2001 to ₱4.1 in 2004, and then to over ₱6 billion in 2005 and 2006. Remarkable as this performance is for a company in a mature industry, we expect this to be surpassed in the years ahead as our diversification and market expansion strategies are rewarded.

Our drive to excel, however, is not confined to the bottom line. This is affirmed by the recognition that we received last year from various respected organizations.

For the second straight year, Petron was named by the prestigious, internationally-recognized Institute of Corporate Directors (ICD) as one of the Best-Governed Listed Companies in the Philippines, particularly in the areas of shareholders' rights, equity of shareholders, role of stakeholders, disclosure and transparency, and board responsibility. Our good governance practices are discussed in more detail in a section that we are introducing in this annual report.

We also received recognition for various business communication programs, as we garnered seven *Gold Quill* awards from IABC (International Association of Business Communicators) Philippines. *ArtPetron*, our six year-old annual competition for art students, has consistently won awards and has become established as a regular artistic venue for celebrating Filipino cultural themes.

Even at the international level, we have received affirmation for our initiatives. Our advertising campaign for our most popular gasoline brand, *Petron Xtra Unleaded*, won the Bronze in the "Best Ideas" category of the Asian Marketing Effectiveness Awards.

Likewise, the Bataan Coastal Care Foundation, where Petron Foundation has a leading role, was cited by the Partnership for the Seas of East Asia (PEMSEA) for its excellence in promoting public-private partnerships in coastal and marine management.

All of these achievements – both tangible and intangible - should eventually be reflected in the market's valuation of your company. The stock price of Petron already showed some improvement in 2006, averaging at ₱4.25 versus ₱3.53 in 2005. Its highest closing price in 2006 was ₱5.00, compared to ₱4.65 in 2005. The emerging trend in 2007 is for an even stronger stock price, and we have already seen this reach a high of ₱5.70.

As our on-going investments raise the company to a new level of profitability, we can only expect Petron's value to grow further.

NICASIO I. ALCANTARA
Chairman and Chief Executive Officer

KHALID D. AL-FADDAGH
President

Operational Highlights

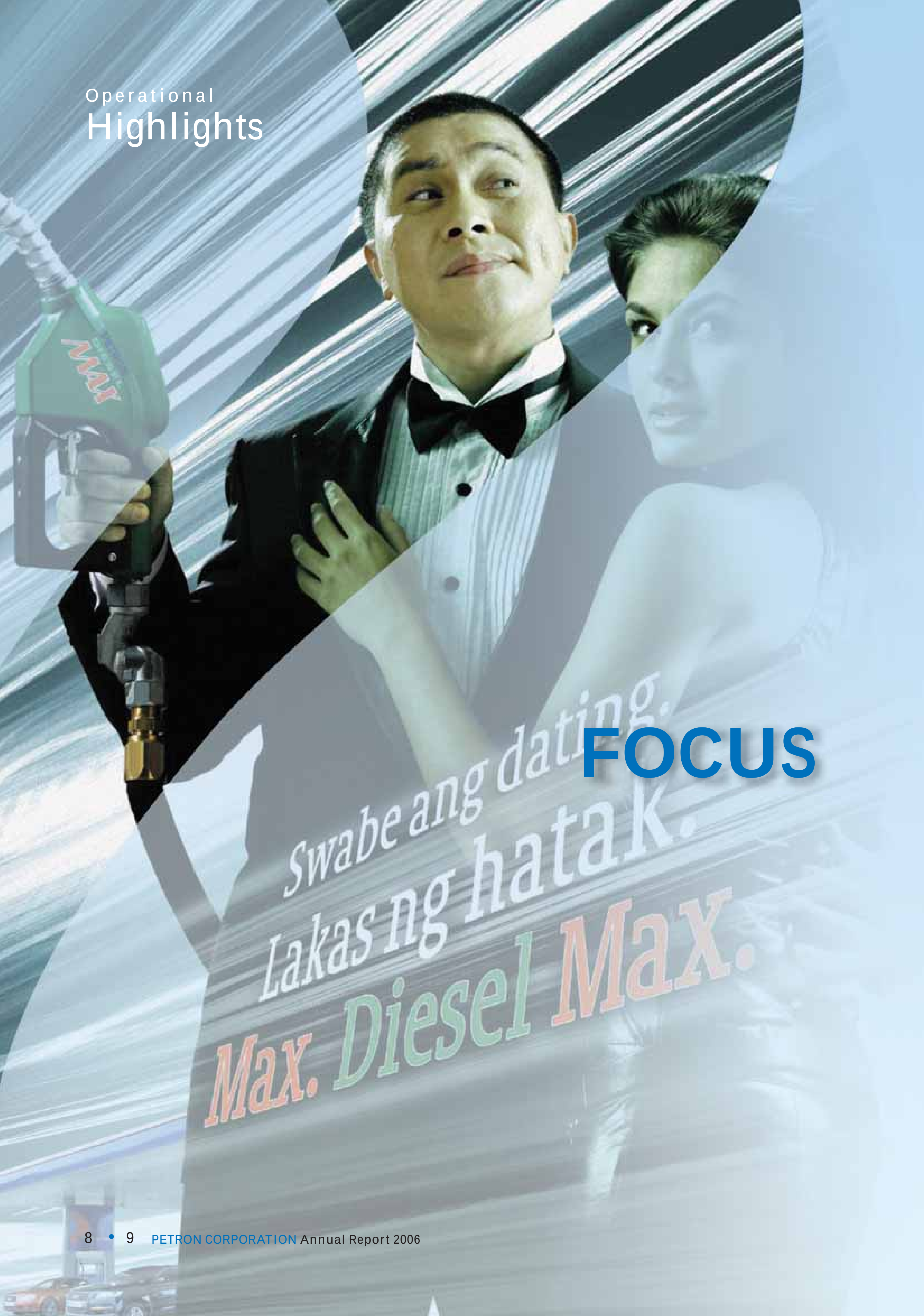
A culture of RESILIENCE

Decades of operating in the ever-dynamic petroleum industry has instilled a culture of resilience in Petron. This culture, which has become one of our greatest strengths, consists of a set of attitudes or behavioral norms that include focus, determination, astuteness, optimization, forward-thinking, and compassion.

It is this very nature of our organization that allowed us to bounce back—and move forward—despite the serious challenges that we saw in 2006.


PETRON

Operational
Highlights



FOCUS

We are focused in exceeding
our customers' expectations

Better Products

We continued to introduce superior products to the market such as the Petron Carbon Flush, a revolutionary product that has been proven to significantly reduce emissions in diesel engines by as much as 70% and improve fuel efficiency, resulting in fuel savings of about 10%.

Moreover, we enhanced the quality of our diesel fuel to accurately match the performance requirements of the latest diesel-powered vehicles, giving birth to the New Generation Petron Diesel Max. This product's new formulation makes it robust and stable enough to withstand the severe operating conditions that come with new diesel engine designs. It protects the fuel system against corrosion, provides better torque, boosts power, and reduces exhaust emissions for both old and new diesel engines.

More Services

More of our service stations are now complemented by our Treats convenience stores as we added 8 more in 2006, bringing the total count to 43. Combined revenues from these projects more than doubled to ₱2.3 billion in 2006. Likewise, with the addition of 4 more company-owned and operated service stations to our network, the number of locators such as fast-food restaurants also increased from 61 to 86.

Customer-oriented Programs

To further ensure service excellence, we launched the Fuel X Mystery Shopper Program so our service stations constantly deliver a delightful customer experience. This continuing initiative engages Petron employees to pose as ordinary customers at our outlets in order to evaluate and make recommendations on improving service quality.

We also launched two dealer programs called the REAP & RULE (Retail Excellence Achievement Program) and Volume Incentive Program (VIP). REAP and RULE encouraged our dealers to further improve the quality of service and housekeeping in our stations, while VIP motivated them to support our drive for bigger sales volumes through rebates.

Our drive for higher volumes was also supported by an increase in the number of cardholders for Petron Fleet Card—powered by microchip technology—and the Petron-BPI Mastercard. Nearly 100,000 cardholders now enjoy various privileges and advantages through these unique products.

Market Share Performance

Our total market share increased to 38.8% from 38.1% in 2005 amidst contracting oil demand. While domestic oil demand went down by 7.5% in 2006, we were able to post a better performance with only a 5.8% decline.

We remained No. 1 in the major industry trades.

We held on to the much-coveted top slot in the Retail Trade, successfully fending off the competition as we increased our market share to 34.8% from 33.7% in 2005.

In the Industrial Trade, we likewise remained the leader with a market share of 43.2%. We grew our aviation sales by 13%, setting a new record in our jet fuel sales at the Manila International Airport with a monthly average volume of 50.6 million liters. We were also able to defend our 100% share of the military's fuel supply.

In the LPG Trade, Gasul's market share increased to 29.1% in 2006 from 27.6% in 2005. We remain the biggest player in this sector.

Operational
Highlights

DETERMINATION

We are determined to protect
our market leadership

Stronger Marketing Network

Our strong marketing and supply chain infrastructure, together with our product and service innovations, helped to reinforce our overall market leadership.

We made strides in making the Petron experience accessible to more motorists. We constructed 28 more service stations nationwide, bringing our count to 1,246 outlets as of end 2006. Out of this number, 9 are company-owned, company-operated stations that serve as flagship outlets in their respective areas. These investments have helped us maintain the distinction of having the largest retail network in the country with a market share of 30%.

Our automotive liquefied petroleum gas (LPG) Xtend has become a popular alternative fuel since it is cost-efficient and environment-friendly. To meet the increasing demand for the fuel from motorists, especially taxi fleets, we opened 5 additional Xtend Autogas facilities. We will be putting in similar facilities over the coming years, including provincial areas.

Meanwhile, the country's most preferred cooking gas brand Gasul has become more accessible as we added 70 branch stores. Our reliability as an LPG supplier was likewise further affirmed as we acquired the centralized requirements of SM and Ayala Land malls.

More Efficient Supply Chain

Our supply chain also plays a vital role in ensuring that our world-class products get to our consumers in a reliable and environment-friendly manner. The Environmental Management Systems of our depots in Mandaue, Zamboanga, Davao, Jimenez, and Tagoloan were certified as ISO-14001-compliant in 2006 by renowned auditing firms Bureau Veritas Certification and Moody International Certification. This achievement affirms that our people promote and implement only international-standard environmental practices in these outports.

Moreover, our depots in Davao and Roxas were able to secure the maximum possible period of 5 years for International Ship and Port Facility Security certifications from the Department of Transportation and Communications - Office for Transport Security. This achievement verifies the excellent security measures we implement at our port facilities.

Meanwhile, our Mandaue Terminal now holds the distinction of having the largest LPG containment facility in the Visayas-Mindanao area with the completion of an additional 2,000 metric-ton LPG sphere. This development reduces freight and operating costs for our company while ensuring a more stable LPG supply in the VisMin region.

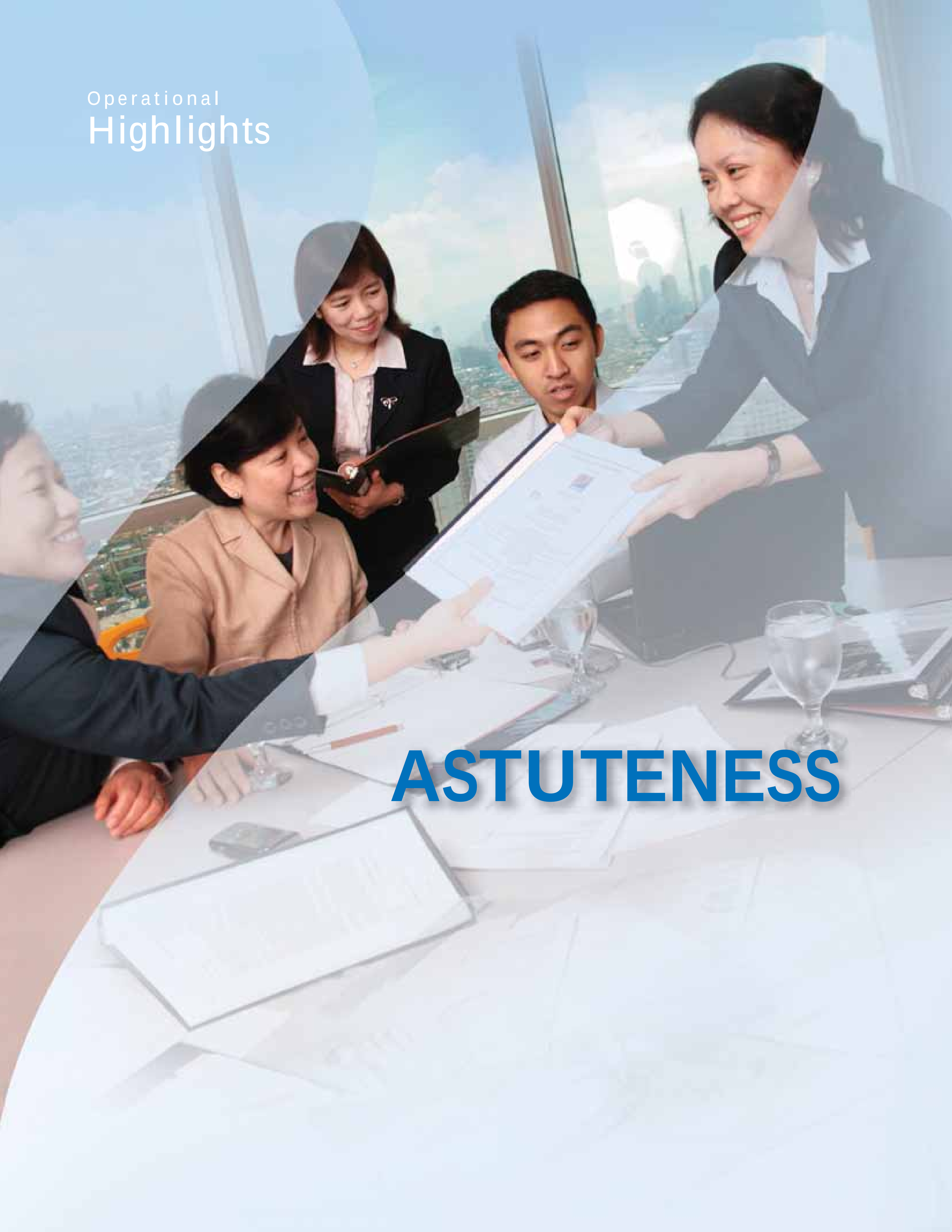
Further demonstrating our efforts to provide quality fuel products across the archipelago in a faster and more efficient manner was the arrival of MMM Ashton, the first of the modern tankers we procured under the Shipping Business Alliance Project. This program, which has been in place since 2004, paves way for the commissioning of 9 larger double-hull, double-bottom oil tankers for our inter-island shipping requirements by 2008.

Safety Across the Supply Chain

While we place a great importance on operational efficiency, safety and environmental compliance is also a primary consideration throughout our supply chain. We conduct regular safety audits to ensure compliance with international and governmental standards. In 2006, we achieved a combined record of 10.7 million man-hours without lost time injury in all our facilities including major depots such as our Pandacan Terminal.

We also implemented our Contractor Safety Management (CSM) program which requires all our contractors to comply with safety and health requirements prior to any work activities performed within our facilities. The program also offers safety orientation courses to instill in our contractors our safety management principles.

We also provided oil spill response and fire-fighting training to our various industrial accounts such as Coca-Cola and Philippine Airlines.



ASTUTENESS

We are astute in
managing our finances

Highest Credit Rating

Unstable foreign exchange rates, extreme volatilities in world crude prices, and the start of our major refinery investments in 2006 demanded prudence and forethought in managing financing costs, securing additional working capital, and obtaining long-term investment funding.

To sustain our fiscal strength and stability amid these developments, we leveraged our historically sound financial stature to secure the highest possible rating for credit-worthiness from the Philippine Rating Services—the PRS Aaa. The PRS Aaa rating underscores our strong capacity to meet financial commitments relative to that of other Philippine corporations.

Successful Notes Issue

Armed with this bill of financial health, we tapped the domestic debt capital market with the issuance of a ₱6.3 billion, five-year Fixed Rate Corporate Note. This raised a major portion of the funding we need for our ongoing Refinery Masterplan.

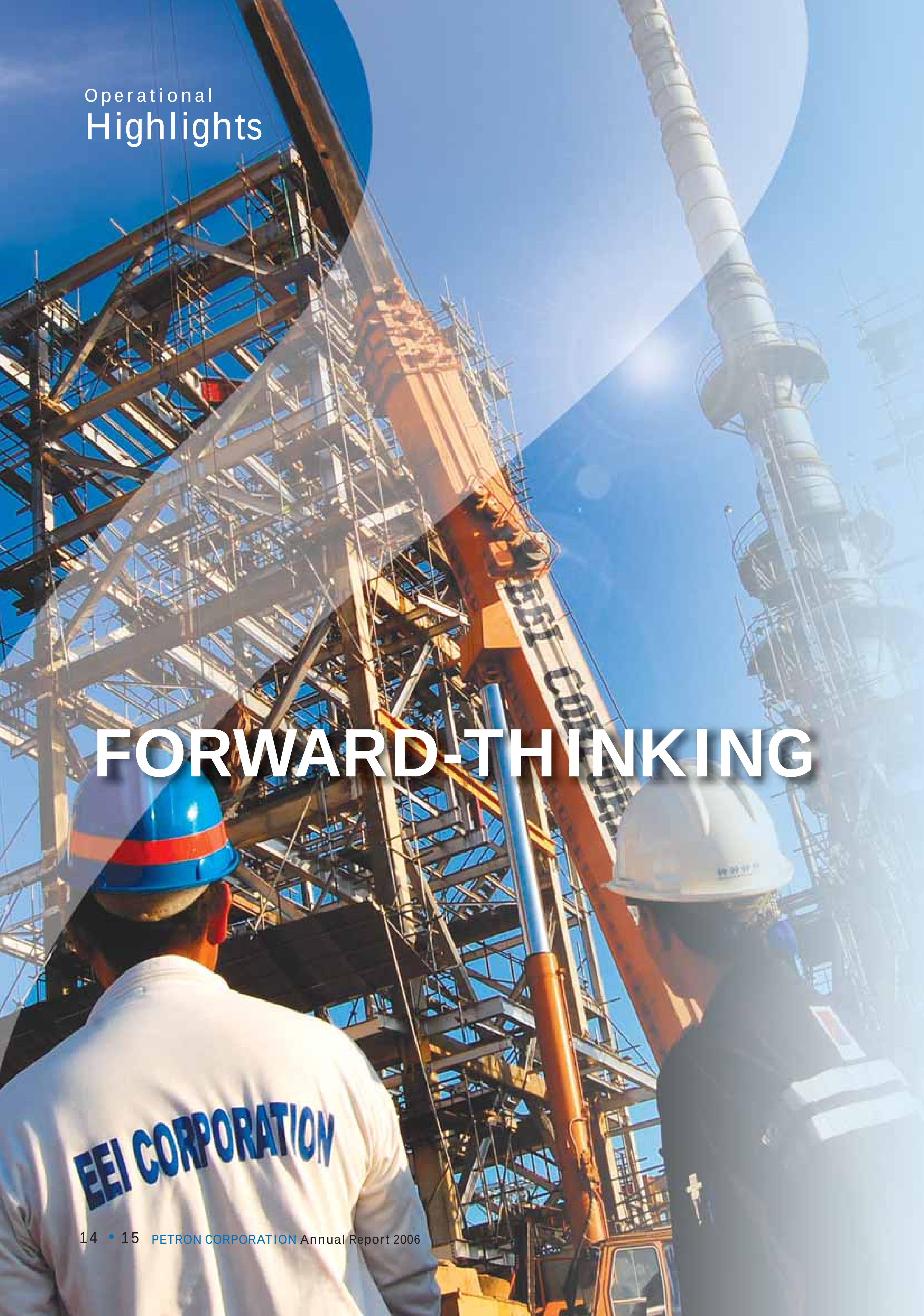
At the time, Petron's successful Notes issue held the distinction of being the largest peso-denominated private placement for Philippine corporates, and was a resounding vote of confidence in our performance and prospects by the banking community.

The PRS Aaa rating was also advantageous in swiftly securing low-cost, short-term borrowings to finance our increased working capital requirement due to higher crude prices.

Sound Hedging Decisions

Meanwhile, we were also successful in utilizing the Value-at-Risk (VAR) technology in managing our foreign exchange exposure. VAR is a business solution software that measures the value of our assets and liabilities affected by forex market volatilities. This allowed us to make sound hedging decisions which significantly contributed to lowering our total financing cost in 2006.

Operational
Highlights



FORWARD-THINKING

We are forward-thinking in discerning
opportunities for growth

Diversifying into Profitable Petrochemicals

We set out on the path to strategic transformation as we pushed forward our $300 million Refinery Masterplan. This is centered on leveraging our existing refinery assets to produce high-value petrochemicals such as propylene, benzene, toluene, and mixed xylene. This will result in a substantial increase in our profitability and serve as a cushion against the volatility of margins in our core business.

As of end 2006, the Engineering, Procurement, and Construction (EPC) of our Petro Fluidized Catalytic Cracker (Petro-FCC) and its accompanying Propylene Recovery Unit (PRU) was 44.6% complete. These are the major components of our Refinery Masterplan. The Petro-FCC and PRU will allow us to produce more high-value or white products, such as diesel and LPG, and extract propylene from our refinery streams by the first quarter of 2008.

A Benzene-Toluene-Xylene (BTX) extraction unit, another major component of the MasterPlan, should be operational by the last quarter of 2008. This unit will double our mixed xylene production and allow us to extract more petrochemicals from our refinery streams.

Expansion of Market Base

Our desire to serve more customers goes beyond local boundaries; we increased our exports of Petron-branded lubricants and other specialty products to the Kingdom of Cambodia. Our successful entry into the Cambodian lubes market points to more opportunities to serve the rest of the regional market, and so we are now exploring similar deals in other countries such as China and Indonesia.

We continued to look for market opportunities abroad as we increased our export sales of straight run fuel oil, diesel and mixed xylene. Our export volumes amounted to around 11 million barrels in 2006, equivalent to a 37% increase from 2005.

Partnering with Global Players

In line with our efforts to increase our non-traditional revenue sources, we expanded our strategic partnership with the leading global fuel additives supplier, Innospec. Under the agreement, we will construct and operate a $2.5 million blending plant in Subic Bay that will supply Innospec's customers in the Asia-Pacific region. This should also enable us to tap into Innospec's customers in the region, thus broadening the market base for our lubricants.

Operational
Highlights

OPTIMIZATION

We continually search for ways to reduce costs and improve productivity

Higher Energy Efficiency

At our 180,000 barrel per day Bataan refinery, we placed special focus on energy efficiency and reliability. These were further improved with the enhancement of our heat recovery due to better furnaces insulation.

Our power rationalization projects contributed to energy efficiency as we availed of more economical power from the grid instead of relying on self-generation. To increase reliability, we replaced a 7 MVA transformer and the construction of a 230 KV substation.

We also acquired new instruments that help eliminate flaring and heat loss. An acoustic detector and fugitive emission sniffer help in the reduction of flaring while the portable flue gas analyzer allows us to increase furnace and boiler efficiency.

Leveraging Information Technology

We also made process improvements in the area of information technology or IT. We managed to upgrade our online, real-time information system called SAP to its latest version, called ECC 6.0, facilitated almost entirely by our homegrown IT experts with very minimal consultation with the technology's owner, SAP Germany. This feat not only testified to Petron's exceptional IT expertise, but also saved our company millions of pesos in consultancy fees. With the latest version of SAP in place, we are now assured of more efficient management of our people, processes, and technology. This also gives Petron the distinction of being one of the first few companies in the world to implement this version.

To further streamline our procurement process, we implemented the Materials Procurement Optimization System (MPOS) which enables our suppliers to interact with us via the web. This is aimed at reducing the procurement cycle time and produce real savings.

An additional 21 service stations were outfitted with the Point-of-Sale (POS) system which automates many processes at the service station level. We can now efficiently monitor the sales and inventory of 51 Petron stations from our head office.

People Development

We continuously implemented programs for the professional and personal development of our employees to enhance their job satisfaction and productivity.

We continued to hold regular "An Hour With A Champion" seminars where we invite successful entrepreneurs and executives from various organizations to relate their success stories, thereby helping expand the business perspectives of our own executives and supervisors. This initiative has in fact won for Petron the 2006 Gold Quill Merit Award for Employee Communication Skills.

We also helped our employees make more informed workplace decisions by keeping them abreast of events, projects, and issues relevant to our business through PETRONews, our official newsletter which also won for Petron the 2006 Gold Quill Merit Award for Publication Skills.

Alongside these personnel development initiatives were various recreational activities such as flower arrangement seminars, painting sessions, and sportsfests that promote work-life balance.

Operational
Highlights

We believe that our concern for society is key to enduring success

Active Support for Child and Youth Education

Through Tulong Aral ng Petron, we continued to send poor children to elementary schools in Metro Manila and Mindanao. As of end-2006, there were 5,139 children enjoying the program's benefits, including the provision of books, school supplies, uniforms and meal allowances. The program also includes training for teachers and capability building seminars as well as livelihood projects for parents. This initiative is recognized by the Department of Social Welfare and Development as the only partnership with the private sector that has been sustained.

It is heartening to note that at the end of school year 2005-2006, a total of 413 of our scholars were rated outstanding and 55 were awarded first honors.

In addition to Tulong Aral, we have been supporting the Department of Education's Adopt-A-School program by putting up school buildings in communities where these are badly needed. In 2006, five Petron Schools were built in various locations in Mindanao, bringing the total to 19 schools established since 2002.

We likewise sustained our contributions to education in the secondary and tertiary levels through the YIELD (Youth in Entrepreneurship and Leadership) Program and our employee volunteers' regular mentoring in the Junior Achievement Philippines and WIWAG Business Week programs.

These initiatives are under our Fuel H.O.P.E. (Helping Filipino Children and the Youth Overcome Poverty through Education) banner program, which remains the centerpiece of our CSR.

Helping the Victims of Disasters

The landslide in Southern Leyte and the oil spill off Guimaras Strait also saw our company at the forefront of relief and rehabilitation efforts and taking a lead role in coordinating with government agencies and other concerned organizations.

We helped in the relief of the affected communities in Southern Leyte as we played an active role in managing the Tulong Kapwa Center. We spearheaded a consortium of companies in the energy sector to construct the Tulong Kapwa-GK Energy Village in Liloan, Southern Leyte.

In the Guimaras oil spill, we immediately took the responsibility for restoring the island to its condition prior to the incident. We led a "Cash-for-Work" program under the banner of Ligtas Guimaras to clean the affected shorelines. Beyond the clean-up, we also established several livelihood programs to help the people of Guimaras. Months after the incident, our commitment to help the people of Guimaras continues.

Indeed, the principles we have embraced throughout the years that have helped develop our organizational resilience prove that your investment is in good hands with the Petron family.

Corporate Governance

In line with its commitment to promote the best interest of its stakeholders, Petron has embraced a practice of good corporate governance—fostering transparency that goes beyond compliance. The core of the company's governance principles and practices is embodied in its Articles of Incorporation and By-Laws. In 2003, Petron further affirmed its commitment to these practices by adopting a Corporate Governance Manual.

The Board of Directors

Petron's Board of Directors is composed of ten members, two of whom are Independent Directors. The Board is responsible for overseeing management of the company and pursuing its growth. The Board conducts itself with utmost honesty and integrity in the discharge of its duties, functions and responsibilities.

Directors sign Conflict-of-Interest Statements, disclosing their respective business interests, to ensure that these are not in competition with the business of Petron. The schedule of board meetings for the entire year is fixed at the start of the year.

Pursuant to the company's By-Laws, the Board of Directors has instituted the following Committees:

1. NOMINATION

The Nomination Committee's main responsibility is to pre-screen and shortlist candidates proposed to become members of the Board of Directors. It ensures that the members of the Board of Directors have complied with the appropriate qualifications as prescribed in the Corporate Governance Manual.

2. COMPENSATION

The Compensation Committee considers and approves the salary structure as well as the promotion of Division Heads/Vice Presidents. It likewise evaluates other compensation policies such as the corporate benefit plans.

3. AUDIT

The Audit Committee, on the other hand, assesses the effectiveness of the company's internal control system. It reviews the activities of the Internal Audit Manager as well as the External Auditor.

We are implementing a performance evaluation system to promote higher awareness among Directors for the competent and responsible performance of their duties and functions. Essentially, the performance evaluation is made among the Directors. Evaluation forms are required to be accomplished wherein the Directors assess the performance of the Chairman and the President; the Chairman and the President assess the performance of the Directors; and the Board Committee Members assess the performance of their respective Board Committee Chairmen.

Corporate Governance Manual

Implemented in January 2003, this Manual guides the company in its pursuit of sound business practices as it competes in a continually evolving business environment. It sets out clear and specific guidelines—from the nomination of members of the Board of Directors and the functions of various committees, to the benefits accruing to shareholders.

Key internal control measures are highlighted in this Manual:

- The Board of Directors ensures that the company is appropriately and effectively managed and controlled;
- Management actively manages and operates the company in a sound and prudent manner under the direction of the Board;
- Organizational and procedural controls are supported by an effective management information system and risk management reporting system;
- Independent audit mechanisms are in place for monitoring the adequacy and effectiveness of the company's governance and overall operations.

Transparency

Periodic financial and other reports are submitted to the Securities and Exchage Commission and Philippine Stock Exchange. Relevant corporate developments are likewise submitted to these regulatory agencies in the form of press releases and official disclosures.

The company's Management also utilizes its corporate website—www.petron.com—as a venue to disclose new corporate developments and reportorial requirements.

In July 2006, the corporate website underwent re-imaging not only to reflect its new brand features but also to enhance content and transparency. A section under the Investor Relations site is now dedicated to feature all disclosures. On the other hand, other corporate developments through press releases are also posted in the website's Newsroom Section.

With almost 10,000 hits per week, the website has become one of the most effective and expeditious means to disseminate corporate information to the public.

Recognition

Petron has received recognition from the internationally known Institute of Corporate Directors (ICD) for its corporate governance practices. For the last two years, the ICD has named Petron as one of the country's Best Governed Listed Companies on the basis of rights and equity of shareholders, role of stakeholders, disclosure & transparency, and board responsibility.

This has only strengthened the company's resolve to institute and implement programs and policies in line with good corporate stewardship.

Moving forward, we are committed to continually look for ways to enhance our good governance practices in order to serve the best interests of our stakeholders.

Audit Committee Report

The Board of Directors
Petron Corporation

The Audit Committee assists the Board of Directors in its oversight function with respect to the adequacy and effectiveness of internal control environment, compliance with corporate policies and regulations, integrity of the financial statements, the independence and overall direction of the internal audit function, and the selection and performance of the external auditor.

In the performance of our responsibilities, we report that in 2006:

- We reviewed and discussed with Controllers management the quarterly and annual financial statements of Petron Corporation and Subsidiaries and endorsed these for approval by the Board.

- The independent auditors, SGV and Co., presented to and discussed with the Committee the scope and timing of their annual audit plan and focus areas related to their review of the financial statements.

- SGV and Co. briefed the members of the Audit Committee on the new accounting standards that were adopted by Petron in 2005 and their impact on the financial statements. Similarly, new accounting standards for adoption in 2006 and their possible effect on the financial statements were also presented.

- The Audit Committee reviewed with SGV and Co. the external auditors' audit observations and recommendations on the Company's internal controls and management's response to the issues raised.

- The Committee reviewed with the Internal Audit Manager and approved the annual internal audit plan and satisfied itself to the independence of the internal audit function.

- We reviewed on a quarterly basis Internal Audit's report on the adequacy and effectiveness of the internal control environment in the areas covered during the period.

- Based on a review of the external auditors' performance, the Committee recommended to the Board and the Shareholders the reappointment of SGV and Co. as Petron's independent auditor for 2006.

- The Committee reviewed and approved the engagement of services and related fees of other audit service providers.

All the four members of the Audit Committee, two of whom are independent directors, are satisfied with the scope and appropriateness of the Committee's mandate and that the Committee substantially met its mandate in 2006.

Emilia T. Boncodin
Chairperson
Independent Director

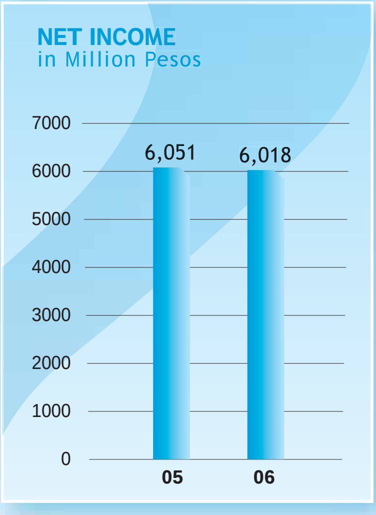
Douhan H. Al-Douhan
Independent Director

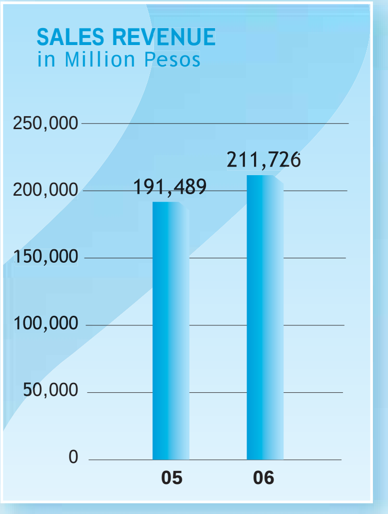
Herminio S. Aquino

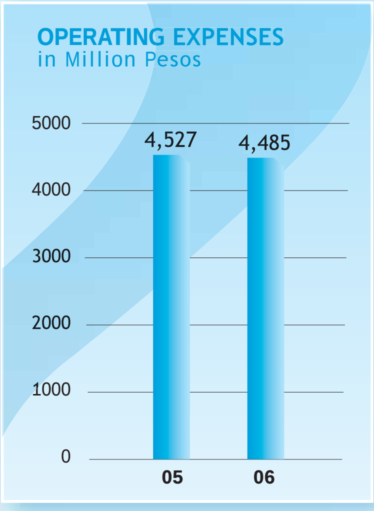
Basil A. Abul-Hamayel

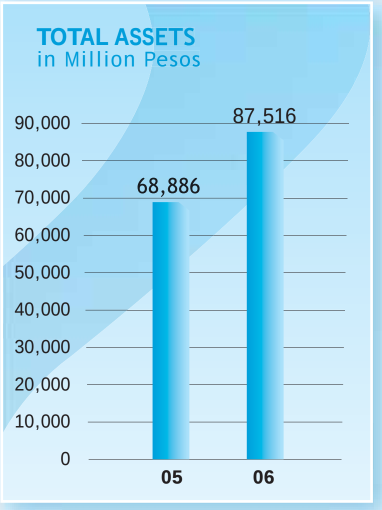
FINANCIAL HIGHLIGHTS

In Million Pesos, Except Per Share Amount	**2006**	2005
SALES	**211,726**	191,489
NET INCOME (LOSS)	**6,018**	6,051
OPERATING EXPENSES	**4,485**	4,527
INCOME FROM OPERATIONS	**9,727**	9,752
PLANT, PROPERTY & EQUIPMENT	**25,153**	22,570
TOTAL ASSETS	**87,516**	68,886
TOTAL EQUITY	**32,253**	27,615
(In Pesos Per Share)		
EARNINGS PER SHARE	**0.64**	0.64
CASH DIVIDEND DECLARED	**0.10**	0.10









FINANCIAL HIGHLIGHTS

RESILIENCY IN THE FACE OF CHANGE AND SETBACKS

Your company realized after tax income of ₱6.02 billion, net of the ₱1.6 billion inventory losses incurred in the second half of 2006, driven mainly by the collapse in crude prices towards the end of the third quarter. Despite the inventory losses, 2006 net income almost matched 2005 net earnings of ₱6.05 billion, reflecting improved operating efficiency. Consequently, earnings per share was constant at 64 centavos.

	2004	2005	**2006**
Net Income (in Million Pesos)	4,101	6,051	**6,018**
Earnings Per Share (in Peso/Share)	0.44	0.64	**0.64**

Total equity reached ₱32.25 billion or ₱3.44 per share as of end-2006, 17% higher than end-2005 book value of ₱27.62 billion or ₱2.95 per share.

	2004	2005	**2006**
Total Equity (in Million Pesos)	22,323	27,615	**32,253**
Book Value Per Share (in Peso/Share)	2.38	2.95	**3.44**

IMPROVED OPERATING EFFICIENCY

Earnings before interest, taxes, depreciation and amortization (EBITDA) was slightly higher at ₱12.21 billion.

(in Million Pesos)	2004	2005	**2006**
EBITDA	8,967	12,087	**12,209**
Income from Operations	7,150	9,752	**9,727**

Factors contributing to this improvement are:

- Aggregate sales volume was higher at 52.22 million barrels, as exports increased by 37% or 2.96 million barrels from 2005 level to compensate for the 6% or 2.43 million barrels decline in domestic sales. Notwithstanding the slump in domestic sales performance, your company's market share improved by 0.8 percentage points to 38.8%, as the drop in its domestic sales volume was slower than the 7.5% contraction in total domestic demand, as reported by the Department of Energy.

  Coupled with the increase in both regional and domestic prices, net revenues of ₱211.7 billion grew by 11% compared to the year before. Meanwhile, revenue contribution of export sales increased by 4 percentage points to 16% of total revenues.

	2004	2005	**2006**
Net Revenues (in Million Pesos)	147,425	191,489	**211,726**
Sales Volume (in Thousand Barrels)	52,758	51,695	**52,220**

- Cost of goods sold rose by 12% to ₱197.51 billion due to the 25% increase in cost of Dubai (2006 FOB/barrel average: $61.50 vs. 2005 FOB/barrel average: $49.30). This was aggravated by inventory losses incurred during the second half of 2006 because of the sudden drop in crude and regional product prices.

  Hence, gross margin rate declined by 0.8 percentage points to 6.7% resulting in a slightly lower gross profit of ₱14.22 billion (vs. 2005 level of ₱14.28 billion).

- In contrast, your company reflected improved operating efficiency as it spent less on selling and administrative expenses (2006**:** ₱4.49 billion vs. 2005: ₱4.53 billion). Together with the growth in aggregate sales volume, unit cost was 2% lower at 54 centavos. The positive variance was essentially because of the reduction in employee-related costs, advertising expenses, and materials and supplies.

Operating Expenses	2004	2005	**2006**
In Million Pesos	4,877	4,527	**4,485**
In Peso Per Liter Sold	0.58	0.55	**0.54**

- On the other hand, net interest and other charges went up by 13% to ₱1.82 billion. The increment was caused by the hike in interest expense resulting from increased short-term borrowings to fund more expensive crude oil imports.

- Effective tax rate for 2006 was at 24%, 8% better than the 26% registered in 2005, even as the statutory corporate income tax rate was increased to 35% effective November 1, 2005. The lower tax provision and its difference from the statutory rate was attributable to the income tax holiday granted to the company's mixed xylene, as well as its isomerization and gasoil hydrotreater operations.

  The income tax holiday for mixed xylene lapsed in December 2006.

	2004	2005	**2006**
Provision for Income Tax (in Million Pesos)	1,323	2,091	**1,886**
Effective Tax Rate (in %)	24%	26%	**24%**

HEALTHY CASH GENERATION

With healthy cash flows, your company was able to fund its investments during the year amounting to ₱9.08 billion from 2005 level of ₱2.63 billion, as well as return cash totaling ₱0.93 billion (or 10 centavos per share) to shareholders. The bulk of its investments was for its various capital projects, mainly consisting of construction costs for its Petro Fluidized Catalytic Cracker (PetroFCC) as well as an additional refinery facility that would extract other petrochemicals (BTX unit). The PetroFCC, which includes a new Propylene Recovery Unit (PRU) will allow the company to produce more high-value white products and extract the petrochemical grade propylene. The BTX unit will produce aromatics such as benzene and toluene and expand the company's mixed xylene production capacity.

Net cash inflow from operations more than doubled year-on-year. From the 2005 level of ₱1.96 billion, the amount reached ₱4.43 billion in 2006, as incremental requirements for working capital was 33% lower than the previous year's level. Higher cash earnings (by 3%) and lower tax payments (by 21%) augmented the impact of the more efficient and effective working capital management implemented by your company.

	2004	2005	**2006**
Net Operating Cash (in Million Pesos)	191	1,963	**4,428**

The growth in net operating cash was supplemented by long-term loan availment, which net of repayments amounted to ₱12.48 billion, a hefty increase from the ₱0.52 billion net level in 2005. Your company successfully auctioned a five-year ₱6.3 billion Fixed Rate Corporate Notes Issuance (FXCN), specifically to finance its various refinery projects.

ROBUST AND LIQUID FINANCIAL CONDITION

Your company's financial condition is robust. Total resources grew by 27% to ₱87.52 billion as of end-2006.

Year-on-year, current assets increased by 37% to ₱60.99 billion, reflecting better liquidity ratios. Average cash cycle improved by 12% as turnover rates for both receivables and inventory were faster, especially towards the last quarter of 2006.

	2004	2005	**2006**
Net Operating Cash (in Million Pesos)	191	1,963	**4,428**
Current Ratio	1.24 : 1	1.31 : 1	**1.47 : 1**
Acid Test Ratio	0.50 : 1	0.48 : 1	**0.67 : 1**

Property, plant and equipment, net of depreciation, grew by 11% to ₱25.15 billion. Nonetheless, your company managed its assets better, as turnover ratio for its fixed assets improved by 24%.

On the other hand, current liabilities increased by 22% to ₱41.49 billion, mainly due to higher short-term loans used to finance more expensive crude. Similarly, noncurrent liabilities almost doubled to ₱13.77 billion, as your company issued ₱6.3 billion worth of Fixed Rate Corporate Notes. Despite the increase in total liabilities, debt-equity ratio of 1.7 times was well within the creditor banks' limit.

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The management of Petron Corporation is responsible for all information and representations contained in the consolidated balance sheets as of December 31, 2006 and 2005, and the related consolidated statements of income, recognized income and expense and cash flows for the years ended December 31, 2006, 2005 and 2004. The financial statements have been prepared in conformity with generally accepted accounting principles in the Philippines and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration to materiality.

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

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

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

MA. CONCEPCION F. DE CLARO
Controller

NICASIO I. ALCANTARA
Chairman

INDEPENDENT AUDITORS' REPORT

SGV & Co

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1226 Makati City
Philippines

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The Stockholders and the Board of Directors
Petron Corporation
Petron MegaPlaza
358 Sen. Gil Puyat Avenue
Makati City

We have audited the accompanying financial statements of Petron Corporation and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2006 and 2005, and the consolidated statements of income, consolidated statements of recognized income and expense and consolidated statements of cash flows for each of the three years in the period ended December 31, 2006, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Philippine Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Petron Corporation and Subsidiaries as of December 31, 2006 and 2005, and their financial performance and their cash flows for each of the three years in the period ended December 31, 2006 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VALAYO & CO.

Wilson P. Tan

Wilson P. Tan
Partner
CPA Certificate No. 76737
SEC Accreditation No. 0100-AR-1
Tax Identification No. 102-098-469
PTR No. 0267394, January 2, 2007, Makati City

CONSOLIDATED BALANCE SHEETS
(Amounts in Millions)

	December 31	
	2006	**2005**
ASSETS		
Current Assets		
Cash and cash equivalents (Note 4)	**₱11,735**	₱3,940
Financial assets at fair value through profit or loss (Note 5)	**180**	116
Available-for-sale investments (Note 6)	**103**	259
Receivables - net (Note 7)	**15,629**	11,863
Inventories - net (Notes 8, 23 and 26)	**26,289**	27,018
Other current assets - net (Note 30)	**7,054**	1,297
Total Current Assets	**60,990**	44,493
Noncurrent Assets		
Available-for-sale investments (Note 6)	**529**	327
Property, plant and equipment - net (Note 9)	**25,153**	22,570
Investment properties - net (Note 10)	**222**	235
Other noncurrent assets - net (Notes 11, 22 and 25)	**622**	1,261
Total Noncurrent Assets	**26,526**	24,393
	₱87,516	₱68,886
LIABILITIES AND EQUITY		
Current Liabilities		
Short-term loans (Note 12)	**₱28,135**	₱21,407
Liabilities for crude oil and petroleum product importation (Note 23)	**7,541**	7,911
Accounts payable and accrued expenses (Notes 13 and 30)	**3,731**	2,626
Income tax payable	**452**	183
Current portion of long-term debt - net (Note 14)	**1,633**	1,906
Total Current Liabilities	**41,492**	34,033
Noncurrent Liabilities		
Long-term debt - net of current portion (Note 14)	**11,279**	5,025
Deferred income tax liabilities - net (Note 22)	**1,443**	1,516
Other noncurrent liabilities (Note 15)	**1,049**	697
Total Noncurrent Liabilities	**13,771**	7,238
Equity Attributable to Equity Holders of the Parent (Note 16)		
Capital stock	**9,375**	9,375
Retained earnings:		
Appropriated	**17,021**	11,652
Unappropriated	**6,232**	6,352
Other reserves	**(490)**	128
Equity Attributable to Equity Holders of the Parent	**32,138**	27,507
Minority Interest (Note 16)	**115**	108
Total Equity	**32,253**	27,615
	₱87,516	₱68,886

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

(Amounts in Millions, Except Per Share Amounts)

	Years Ended December 31		
	2006	2005	2004
SALES (Notes 26 and 32)	**₱211,726**	₱191,489	₱147,425
COST OF GOODS SOLD (Notes 8, 17, 19, 20, 23, 25 and 26)	**197,514**	177,210	135,398
GROSS PROFIT	**14,212**	14,279	12,027
SELLING AND ADMINISTRATIVE			
EXPENSES (Notes 18, 19, 20, 23, 25 and 33)	**(4,485)**	(4,527)	(4,877)
INTEREST EXPENSE (Notes 12, 14, 15 and 21)	**(2,684)**	(2,091)	(1,675)
INTEREST INCOME (Note 21)	**362**	317	344
OTHERS - Net (Notes 5, 15, 21, 23 and 30)	**499**	164	(395)
INCOME BEFORE INCOME TAX	**7,904**	8,142	5,424
PROVISION FOR (BENEFIT FROM)			
INCOME TAX (Notes 22 and 31)			
Current	**1,723**	2,057	1,339
Deferred	**163**	34	(16)
	1,886	2,091	1,323
NET INCOME (Note 16)	**6,018**	₱6,051	₱4,101
Attributable to:			
Equity holders of the parent (Note 27)	**₱6,011**	₱6,044	₱4,094
Minority interest	**7**	7	7
	₱6,018	₱6,051	₱4,101
BASIC EARNINGS PER SHARE			
ATTRIBUTABLE TO EQUITY			
HOLDERS OF THE PARENT (Note 27)	**₱0.64**	₱0.64	₱0.44

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF RECOGNIZED INCOME AND EXPENSE

(Amounts in Millions)

	Years Ended December 31		
	2006	2005	2004
Actuarial gain (loss) on defined pension plan (Note 25)	**(₱699)**	₱356	₱286
Tax effect	**242**	(133)	(92)
Net actuarial gain (loss) on defined pension plan	**(457)**	223	194
Actuarial loss (gain) due to limit on recognized plan assets [net of tax effects of ₱93, ₱212 and ₱53 in 2006, 2005 and 2004, respectively (Notes 16 and 25)]	**(176)**	(408)	115
	(633)	(185)	309
Unrealized fair value gain on available-for-sale investments [net of tax effects of ₱8 and ₱4 in 2006 and 2005, respectively (Note 6)]	**15**	4	–
NET INCOME (LOSS) RECOGNIZED DIRECTLY IN EQUITY	**(618)**	(181)	309
NET INCOME FOR THE YEAR (Note 16)	**6,018**	6,051	4,101
TOTAL RECOGNIZED INCOME AND EXPENSE FOR THE YEAR	**₱5,400**	₱5,870	₱4,410
Attributable to:			
Equity holders of the parent	**₱5,393**	₱5,863	₱4,403
Minority interest	**7**	7	7
	₱5,400	₱5,870	₱4,410

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in Millions)

	Years Ended December 31		
	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES			
Income before income tax	**₱7,904**	₱8,142	₱5,424
Adjustments for:			
Interest expense (Note 21)	**2,684**	2,091	1,675
Depreciation and amortization (Notes 9, 10 and 20)	**2,482**	2,335	1,856
Unrealized foreign exchange loss (gain) - net	**(382)**	(270)	48
Interest income (Note 21)	**(362)**	(317)	(344)
Others	**(131)**	(111)	–
Operating income before working capital changes	**12,195**	11,870	8,659
Changes in operating assets and liabilities (Note 28)	**(4,282)**	(6,326)	(6,093)
Interest paid	**(2,383)**	(2,047)	(1,643)
Income taxes paid	**(1,454)**	(1,850)	(1,075)
Interest received	**352**	316	343
Net cash provided by operating activities	**4,428**	1,963	191
CASH FLOWS FROM INVESTING ACTIVITIES			
Additions to:			
Property, plant and equipment (Note 9)	**(5,052)**	(2,313)	(5,463)
Investment properties (Note 10)	**-**	(16)	–
Decrease (increase) in:			
Other receivables	**(3,943)**	9	209
Other noncurrent assets	**(61)**	(67)	(182)
Reductions from (additions to):			
Financial assets at fair value through profit or loss	**1**	2	–
Available-for-sale investments	**(24)**	(249)	–
Short-term investments	**-**	–	19
Net cash used in investing activities	**(9,079)**	(2,634)	(5,417)
CASH FLOWS FROM FINANCING ACTIVITIES			
Availments of loans	**157,460**	78,246	80,854
Payments of:			
Loans	**(144,433)**	(76,879)	(72,949)
Cash dividends	**(928)**	(925)	(1,846)
Others	**378**	78	101
Net cash provided by financing activities	**12,477**	520	6,160
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	**(31)**	(13)	(28)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**7,795**	(164)	906
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**3,940**	4,104	3,198
CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 4)	**₱11,735**	₱3,940	₱4,140

See accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

1. Corporate Information

Petron Corporation (the Parent Company or Petron) was incorporated under the laws of the Republic of the Philippines and registered with the Philippine Securities and Exchange Commission (SEC) on December 15, 1966. Petron is the largest oil refining and marketing company in the Philippines, supplying more than one-third of the country's oil requirements. The Company is dedicated and passionate about its vision to be the leading provider of total customer solutions in the energy sector and its derivative businesses.

Petron operates a refinery in Limay, Bataan, with a rated capacity of 180,000 barrels a day. Petron's International Standards Organization (ISO)-14001 - certified refinery processes crude oil into a full range of petroleum products including LPG, gasoline, diesel, jet fuel, kerosene, industrial fuel oil, solvents, asphalts, and mixed xylene. From the refinery, Petron moves its products mainly by sea to Petron's 32 depots and terminals situated all over the country. Through this nationwide network, Petron supplies fuel oil, diesel, and LPG to various industrial customers. The power sector is Petron's largest customer. Petron also supplies jet fuel at key airports to international and domestic carriers.

Through more than 1,200 service stations, the largest in the country, Petron retails gasoline, diesel and kerosene to motorists and public transport operators. Petron also sells its LPG brand "Gasul" to households and other consumers through an extensive dealership network.

Petron operates a state-of-the-art lube oil blending plant at Pandacan Oil Terminals, where it manufactures lubes and greases. These are also sold through Petron's service stations and sales centers.

Petron is expanding its non-fuel businesses which include its convenience store brand "Treats." Petron has partnered with major fast-food chains, coffee shops, and other consumer services to give its customers a one-stop full service experience. Petron is also putting up additional company-owned and company-operated (COCO) service stations in strategic locations.

In line with Petron's efforts to increase its presence in the regional market, it exports various petroleum products to Asia-Pacific countries such as Cambodia, Korea, China and Australia.

Petron is a public company under Section 17.2 of the Securities Regulation Code. The Philippine National Oil Company (PNOC) and the Aramco Overseas Company B.V. each owns a 40% share of equity. The remaining 20% is held by close to 200,000 stockholders.

The principal activities of the subsidiaries are described in Note 2 under "Basis of Consolidation."

The registered office address of Petron and its Philippine-based subsidiaries is Petron MegaPlaza, 358 Sen. Gil Puyat Avenue, Makati City.

The accompanying consolidated financial statements as of December 31, 2006 and 2005 and for each of the three years in the period ended December 31, 2006 were approved and authorized for issue by the Board of Directors (BOD) on April 3, 2007.

2. Summary of Significant Accounting Policies

<u>Basis of Preparation</u>
The accompanying consolidated financial statements of Petron and subsidiaries (collectively referred to as "the Company") have been prepared on the historical cost basis, except for financial assets at fair value through profit or loss (FVPL), available-for-sale (AFS) investments and derivative financial instruments, which are measured at fair value. The consolidated financial statements are presented in Philippine pesos, which is the Company's functional and presentation currency. All amounts are rounded to the nearest millions (₱000,000), except when otherwise indicated.

<u>Statement of Compliance</u>
The consolidated financial statements of the Company have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

<u>Changes in Accounting Policies</u>
The accounting policies adopted are consistent with those of previous financial year, except for the adoption of the following new and amended PFRS and Philippine Interpretations in 2006. Adoption of these new and amended standards and interpretations did not have any significant effect on the Company's consolidated financial statements. These, however, require additional disclosures on the consolidated financial statements.

- Philippine Accounting Standard (PAS) 21, Amendment - "The Effects of Changes in Foreign Exchange Rates";
- PAS 39, Amendments - "Financial Instruments: Recognition and Measurement"; and
- Philippine Interpretation IFRIC 4 - "Determining Whether an Arrangement Contains a Lease."

The Company has also earlier adopted the following Philippine Interpretations. Adoption of these interpretations did not have any significant effect on the financial position of the Company.

- Philippine Interpretation IFRIC 8 – "Scope of PFRS 2";
- Philippine Interpretation IFRIC 9 – "Reassessment of Embedded Derivatives"; and
- Philippine Interpretation IFRIC 10 – "Interim Financial Reporting and Impairment."

The following Philippine Interpretations are effective for annual periods beginning on or after January 1, 2006 but are not relevant to the Company:

- Philippine Interpretation IFRIC 5 – "Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds"; and
- Philippine Interpretation IFRIC 6 – "Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment."

The principal effects of these changes are as follows:

a. PAS 21, "The Effects of Changes in Foreign Exchange Rates." The Company adopted the amendments to PAS 21. All exchange differences arising from a monetary item that forms part of the Company's net investment in a foreign operation are recognized in a separate component of equity in the consolidated financial statements regardless of the currency in which the monetary item is denominated. This change has no significant impact on the consolidated financial statements.

b. PAS 39, "Financial Instruments: Recognition and Measurement." Amendment for financial guarantee contracts - amended the scope of PAS 39 to require financial guarantee contracts that are not considered to be insurance contracts to be recognized initially at fair value and to be remeasured at the higher of the amount determined in accordance with PAS 37, "Provisions, Contingent Liabilities and Contingent Assets," and the amount initially recognized less, when appropriate, cumulative amortization recognized in accordance with PAS 18, "Revenue." This amendment did not have an effect on the consolidated financial statements.

   Amendment for hedges of forecast intra-group transactions - amended PAS 39 to permit the foreign currency risk of a highly probable intra-group forecast transaction to qualify as the hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated statement of income. As the Company currently has no such transactions, the amendment did not have an effect on the consolidated financial statements.

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

Amendment for the fair value option - amended PAS 39 to restrict the use of the option to designate any financial asset or any financial liability to be measured at fair value through the consolidated statement of income. The Company has complied with these conditions.

c. Philippine Interpretation IFRIC 4, "Determining Whether an Arrangement Contains a Lease." This interpretation provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This change in accounting policy has no significant impact on the consolidated financial statements.

d. Philippine Interpretation IFRIC 5, "Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds." This interpretation establishes the accounting treatment for funds established to help finance decommissioning for companies assets. As the Company does not currently operate in a country where such funds exist, this interpretation has no impact on the consolidated financial statements.

e. Philippine Interpretation IFRIC 6, "Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment." This interpretation establishes the recognition date for liabilities arising from the EU Directive relating to the disposal of waste electrical and electronic equipment. This interpretation is not applicable to the Company as it has no operations in countries covered by the EU Directive.

f. Philippine Interpretation IFRIC 8, "Scope of PFRS 2." This interpretation requires PFRS 2 to be applied to any arrangements where equity instruments are issued for consideration which appears to be less than fair value. This interpretation has no impact on the financial position of the Company.

g. Philippine Interpretation IFRIC 9, "Reassessment of Embedded Derivatives." This interpretation establishes that the date to assess the existence of an embedded derivative is the date an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. The Company has assessed that adoption of this interpretation has no impact on the consolidated financial statements.

h. Philippine Interpretation IFRIC 10, "Interim Financial Reporting and Impairment." This interpretation which provides that the frequency of financial reporting does affect the amount of impairment charge to be recognized in the annual financial reporting with respect to goodwill and AFS investments. It prohibits the reversal of impairment losses on goodwill and AFS investments recognized in the interim financial reports even if impairment is no longer present at the annual balance sheet date. This interpretation has no significant impact on the consolidated financial statements of the Company.

Basis of Consolidation
The consolidated financial statements comprise the financial statements of the Parent Company and its subsidiaries as of December 31 of each year. The financial statements of the subsidiaries are prepared for the same reporting year as the Parent Company, using consistent accounting policies.

All significant intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions are eliminated in full in the consolidation.

Subsidiaries are fully consolidated from the date on which control is transferred to the Company or Parent Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Consolidation of subsidiaries ceases when control is transferred out of the Company or Parent Company.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of income from the date of acquisition or up to the date of disposal, as appropriate.

Minority Interests
Minority interests represent the portion of profit or loss and the net assets not held by the Company and are presented separately in the consolidated statement of income and within equity in the consolidated balance sheet, separately from parent shareholders' equity. Acquisitions of minority interests are accounted for using the entity concept method, whereby the difference between the consideration and the book value of the share of the net assets acquired is recognized as an equity transaction.

The consolidated subsidiaries include:

Subsidiaries	Percentage of Ownership	Country of Incorporation
Overseas Ventures Insurance Corporation (Ovincor)	100.00	Bermuda
Petrogen Insurance Corporation (Petrogen)	100.00	Philippines
Petron Freeport Corporation (PFC)	100.00	Philippines
Petron Marketing Corporation (PMC)	100.00	Philippines
New Ventures Realty Corporation (NVRC) and Subsidiary	79.95	Philippines

In the past, Petron, being partly foreign-owned, was not allowed by the Retail Trade Law to engage in direct retailing. Upon enactment of the Retail Trade Liberalization Act (RTLA) in 2000, the Philippine Board of Investments (BOI) has approved Petron's application to establish a retail enterprise, paving the way for the establishment of a direct-retailing subsidiary, PMC, on January 27, 2004. PMC operates COCO service stations. The COCO service stations will play a major part in launching market initiatives to strengthen the "Petron" brand and will give the Company the opportunity to quickly introduce innovations beyond the present services that are available in its service stations.

The primary purpose of PFC and PMC is to, among others, sell on wholesale or retail and operate service stations, retail outlets, restaurants, convenience stores and the like. NVRC's primary purpose is to acquire real estate and derive income from its sale or lease.

Petrogen and Ovincor are engaged in the business of non-life insurance and re-insurance.

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

Financial Assets and Liabilities

Accounting Policies Effective January 1, 2005

Financial assets and liabilities are recognized initially at fair value. Transaction costs are included in the initial measurement of all financial assets and liabilities, except for financial instruments measured at FVPL.

The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's-length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis and option pricing models.

The Company recognizes a financial asset or liability in the consolidated balance sheet when it becomes a party to the contractual provisions of the instrument and derecognizes a financial asset when it no longer controls the contractual rights that comprise the financial instrument, which is normally the case when the instrument is sold, or all of the cash flows attributable to the instrument are passed to an independent third party. A financial liability (or a part of a financial liability) is derecognized when the obligation is extinguished. In the case of a regular way purchase or sale of financial assets, recognition and derecognition, as applicable, is done using settlement date accounting.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, dividends, gains and losses relating to a financial instrument or a component that is a financial liability, are reported as expense or income. Distributions to the holders of financial instruments classified as equity are charged directly to equity, net of any related income tax benefits. Financial instruments are offset when there is a legally enforceable right to offset and intention to settle either on a net basis or to realize the asset and settle the liability simultaneously.

Financial assets and liabilities are further classified into the following categories: financial assets or liabilities at FVPL, loans and receivables, held-to-maturity (HTM) investments and AFS investments. Financial liabilities that do not qualify as and are not designated at FVPL are subsequently carried at amortized cost using the effective interest method. The Company determines the classification at initial recognition and, where allowed and appropriate, re-evaluates this designation at every reporting date.

a. *Financial Assets or Liabilities at FVPL.* Financial assets or liabilities are classified in this category if acquired principally for the purpose of selling or repurchasing in the near term or upon initial recognition, it is designated by the management as FVPL. Financial assets or liabilities at FVPL are designated by management on initial recognition when the following criteria are met:

   - The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognizing gains or losses on them on a different basis;

   - The assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance 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 recorded.

   Derivatives are also categorized as held at FVPL, except those derivatives designated and considered as effective hedging instruments.

   Financial assets and liabilities at FVPL are recorded in the consolidated balance sheet at fair value. Changes in fair value are accounted for in the consolidated statement of income. Interest earned or incurred is recorded as interest income or expense, respectively. Dividend income is recorded as other income according to the terms of the contract, or when the right of the payment has been established.

   Classified as financial assets at FVPL are the Company's investments in marketable equity securities and proprietary membership shares (see Note 5). The Company has no financial liabilities at FVPL as of December 31, 2006 and 2005.

b. *Loans and Receivables.* Loans and receivables are non-derivative financial assets with fixed or determinable payments and are not quoted in an active market. Such assets are carried at cost or amortized cost in the consolidated balance sheet. Amortization is determined using the effective interest method and is included in the "Interest income" account in the consolidated statement of income. The losses arising from impairment of such financial assets are recognized in the consolidated statement of income.

   Loans and receivables are included in current assets if maturity is within 12 months from the balance sheet date. Otherwise, these are classified as noncurrent assets.

   Classified as loans and receivables are the Company's trade and other receivables (see Note 7).

c. *HTM Investments.* HTM investments are quoted non-derivative financial assets with fixed or determinable payments and fixed maturities for which the Company's management has the positive intention and ability to hold to maturity. Where the Company sell other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS investments. After initial measurement, these investments are subsequently measured at amortized cost using the effective interest method, less any impairment in value. 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 amortization is included in "Interest income" account in the consolidated statement of income. Gains and losses are recognized in the consolidated statement of income when the HTM investments are derecognized and impaired, as well as through the amortization process. The losses arising from impairment of such investments are recognized in the consolidated statement of income. The effects of restatement on foreign currency denominated HTM investments are recognized in the consolidated statement of income.

   Assets under this category are classified as current assets if maturity is within 12 months from the balance sheet date and as noncurrent assets if maturity date is more than a year from the balance sheet date.

   The Company has no HTM investments as of December 31, 2006 and 2005.

d. *AFS Investments.* AFS investments are those which are designated as such or do not qualify to be classified as financial assets at FVPL, HTM investments or loans and receivables. They are purchased and held indefinitely, and may be sold in response to liquidity requirements or changes in market conditions. They may include equity investments, money market papers and other debt instruments.

   After initial measurement, AFS investments are subsequently measured at fair value. The effective yield component of AFS debt securities, as well as the impact of restatement on foreign currency-denominated AFS debt securities, are reported in the consolidated statement of income. The unrealized gains and losses arising from the fair valuation of AFS investments, net of tax, are excluded from reported earnings and are reported under "Other reserves" account in the equity section of the consolidated balance sheet, until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gains or losses previously reported in equity are included in the consolidated statement of income.

Where the Company holds more than one investment in the same security, these are deemed to be disposed of on a first-in, first-out basis. Interest earned on holding AFS investments are reported as interest income using the effective interest rate. Dividends earned on holding AFS investments are recognized in "Other income" account in the consolidated statement of income when the right of the payment has been established. The losses arising from impairment of such investments are recognized as provisions on impairment losses in the consolidated statement of income.

Classified as AFS investments are Petrogen's investments in government securities (see Note 6).

e. *Derivative Financial Instruments.* The Company uses commodity price swaps to protect its margin on industrial fuel from potential price volatility of crude oil and industrial fuel oil. It also enters into short-term forward currency contracts to hedge its currency exposure on crude oil importations. In addition, the Company has identified and bifurcated embedded foreign currency derivatives from certain non-financial contracts.

Derivative instruments are initially recognized at fair value on the date in which a derivative transaction is entered into or bifurcated, and are subsequently re-measured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. The Company has opted not to designate its derivative transactions under hedge accounting. Consequently, gains and losses from changes in fair value of these derivatives are recognized immediately in the consolidated statement of income.

The fair values of freestanding and bifurcated forward currency transactions are calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair values of commodity swaps are determined based on quotes obtained from counterparty banks.

Accounting Policies Prior to January 1, 2005

a. *Investments in Marketable Equity Securities.* Investments in marketable equity securities, shown under "Short-term investments" account in the 2004 consolidated balance sheet, were stated at the lower of aggregate cost or market value determined as of balance sheet date. The amount by which the aggregate cost exceeds market value was accounted for as a valuation allowance and changes in the valuation allowance are included in the consolidated statement of income. Realized gains or losses from the sales of current marketable equity securities were included in the consolidated statement of income. The cost of marketable equity securities used for determining the gain or loss on the sales of such securities was computed using the average method.

b. *Investments in Shares of Stock.* These investments in proprietary membership shares were carried at cost. An allowance was provided for any substantial and presumably permanent decline in the carrying values of these investments.

c. *Derivative Financial Instruments.* Gains or losses on derivative instruments, including premium amortization, were recognized in current operations simultaneous with the gains or losses on the underlying hedged transactions. No accounting recognition was given to embedded derivatives.

<u>Interest-Bearing Loans and Borrowings</u>
All loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any related issue costs, discount or premium.

Gains and losses are recognized in the consolidated statement of income when the liabilities are derecognized, as well as through the amortization process.

<u>Impairment of Financial Assets</u>

Effective January 1, 2005

The Company assesses at each balance sheet date whether a financial asset or a group of financial assets is impaired.

Loans and Receivables. If there is objective evidence that an impairment loss on loans and receivables carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognized in the consolidated statement of income.

The Company first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

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 the consolidated statement of income, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

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

<u>Derecognition of Financial Assets and Liabilities</u>

Effective January 1, 2005

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

- the rights to receive cash flows from the asset have expired;

- the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Company has transferred its rights to receive cash flows from the asset 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.

Where the Company has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Company's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

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

Offsetting Financial Instruments
Financial assets and liabilities are offset and the net amount reported in the consolidated balance sheet 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.

Impact of PAS 32 and PAS 39 Upon Initial Adoption
In 2005, as allowed by the SEC, the adoption of PAS 32 and PAS 39 did not result in the restatement of prior year consolidated financial statements. The cumulative effect of adopting these accounting standards was adjusted to January 1, 2005 equity.

Due to the adoption of PAS 32 and PAS 39, Petrogen classified its investments in government securities as AFS investments. As such, Petrogen recorded these investments at fair value resulting in the recognition of cumulative translation adjustments amounting to ₱2 (net of tax effect of ₱0.7) as of January 1, 2005. Petrogen also changed its method of amortizing bond premiums and discounts from straight-line method to effective interest method resulting in a decrease in retained earnings and investments as of January 1, 2005 by ₱0.4 and ₱0.6, respectively.

Adoption of PAS 39 has increased (decreased) the following accounts in the January 1, 2005 consolidated balance sheet:

	Amount
Receivables	(₱39)
Other current assets	1
Accounts payable and accrued expenses	(10)
Other current liabilities	32
Deferred income tax liabilities	(6)
Other noncurrent liabilities	(6)
Retained earnings	(39)
Minority interest	(9)

Inventories
Inventories are carried at the lower of cost or net realizable value. For petroleum products, crude oil and tires, batteries and accessories (TBA), the net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion, marketing and distribution. For materials and supplies, net realizable value is the current replacement cost.

For financial reporting purposes, Petron uses the first-in, first-out method in costing petroleum products (except lubes and greases, waxes and solvents), crude oil and other products.

Cost is determined using the moving-average method in costing lubes and greases, waxes and solvents, TBA and materials and supplies inventories.

For income tax reporting purposes, cost of all inventories is determined using the moving-average method.

For financial reporting purposes, duties and taxes related to the acquisition of inventories are capitalized as part of inventory cost. For income tax reporting purposes, such duties and taxes are treated as deductible expenses in the year these charges are incurred.

Interest in a Joint Venture
The Company's 33.33% joint venture interest in Pandacan Depot Services Inc. (PDSI), included under "Other noncurrent assets" account in the consolidated balance sheet, incorporated on September 29, 2004 under the laws of the Republic of the Philippines, is accounted for under equity method of accounting. The interest in joint venture is carried in the consolidated balance sheet at cost plus post-acquisition changes in the Company's share of net assets of the joint venture, less any impairment in value. The consolidated statement of income reflects the Company's share in the results of operations of the joint venture.

Property, Plant and Equipment
Property, plant and equipment, except land, are stated at cost less accumulated depreciation, amortization and any impairment in value. Land owned by NVRC is stated at cost less any impairment in value.

The initial cost of property, plant and equipment comprises its purchase price, including import duties and taxes and any directly attributable costs of bringing the assets to their working condition and location for their intended use. Cost also includes any related asset retirement obligation and interest incurred during the construction period on funds borrowed to finance the construction of the projects. Expenditures incurred after the property, plant and equipment have been put into operation, such as repairs and maintenance, are normally charged to income in the year the costs are incurred. In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment beyond its originally assessed standard of performance, the expenditures are capitalized as additional costs of property, plant and equipment. When assets are retired or otherwise disposed of, the cost and the related accumulated depreciation, amortization and impairment loss, if any, are removed from the accounts and any resulting gain or loss is credited or charged to current operations.

When each major inspection is performed, its cost is recognized in the carrying amount of the property, plant and equipment as a replacement if the recognition criteria are satisfied.

For financial reporting purposes, duties and taxes related to the acquisition of property, plant and equipment are capitalized. For income tax reporting purposes, such duties and taxes are treated as deductible expenses in the year these charges are incurred.

For financial reporting purposes, depreciation and amortization are computed using the straight-line method over the estimated useful lives of the following assets:

Buildings and related facilities	20-25 years
Refinery and plant equipment	10-16 years
Service stations and other equipment	4-10 years
Computers, office and motor equipment	2-6 years
Leasehold improvements	10 years or the term of the lease, whichever is shorter

The useful lives and depreciation and amortization method are reviewed periodically to ensure that the 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 residual value, if any, is also reviewed and adjusted if appropriate, at each balance sheet date.

For income tax reporting purposes, depreciation and amortization are computed using the double-declining balance method.

Construction in-progress represents plant and properties under construction and is stated at cost. This includes cost of construction, plant and equipment, interest and other direct costs. Construction in-progress is not depreciated until such time as the relevant assets are completed and available for operational use.

Investment Properties

Investment properties, except land, are stated at cost less accumulated depreciation and any impairment in value. Cost includes transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met and excludes the costs of day-to-day servicing of an investment property. Land is carried at cost less any impairment in value.

Investment properties are derecognized when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognized in the consolidated statement of income in the year of retirement or disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by the end of owner-occupation, commencement of an operating lease to another party or completion of construction or development. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale. These transfers are recorded using the carrying amount of the investment property at the date of the change in use.

For financial reporting purposes, depreciation on office units is computed on a straight-line basis over the estimated useful lives of the assets of 20 years. For income tax reporting purposes, depreciation is computed using the double-declining balance method.

Impairment of Non-Financial Assets

The carrying values of long-lived assets are reviewed for impairment when events or changes in circumstances indicate that the carrying values may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amounts, the assets or cash-generating units are written down to their recoverable amounts. The recoverable amount of the asset is the greater of net selling price or value in use. The net selling price is the amount obtainable from the sale of an asset in an arm's-length transaction. 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 assessment 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 smallest cash-generating unit to which the asset belongs. Impairment losses are recognized in the consolidated statement of income.

A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however, not to an amount higher than the carrying amount that would have been determined (net of any depreciation and amortization) had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is credited to current operations.

Pension Costs

The Company has a defined benefit pension plan covering all permanent, regular, full-time employees administered by trustee banks. The cost of providing benefits under the defined benefit plans is determined using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognized immediately in full in the consolidated statement of recognized income and expense. Any actuarial gains and losses and adjustments arising from the limits on asset ceiling test are taken directly to retained earnings.

The past service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested. If the benefits are already vested immediately following the introduction of, or changes to, a pension plan, past service cost is recognized immediately.

The defined benefit liability is the aggregate of the present value of the defined benefit obligation reduced by past service cost not yet recognized and the fair value of plan assets out of which the obligations are to be settled directly. If such aggregate is negative, the asset is measured at the lower of such aggregate or the aggregate of cumulative unrecognized net actuarial losses and past service cost and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

Borrowing Costs

Borrowing costs are generally expensed as incurred. For financial reporting purposes, interest on loans used to finance capital projects is capitalized as part of project costs (shown as part of “Construction in-progress” account in the consolidated balance sheet) during construction period. Capitalization of interest commences when the activities to prepare the asset are in progress and expenditures and interest are being incurred. Interest costs are capitalized until the assets are substantially ready for their intended use. If the carrying amount of the asset exceeds its recoverable amount, an impairment loss is recognized. For income tax reporting purposes, such interest is treated as deductible expense in the year the interest is incurred.

Cylinder Deposits

The LPG cylinders remain the property of the Company and are loaned in the concept of commodatum to dealers upon payment by the latter of an equivalent 100% of acquisition cost of cylinders.

The Company maintains the balance of cylinder deposits at an amount equivalent to three days worth of inventory of its biggest dealers, but in no case lower than ₱200 at any given time, to take care of possible returns by dealers.

Cylinder deposits, shown under “Other noncurrent liabilities” account in the consolidated balance sheet, are reduced for estimated non-returns. The reduction is credited directly to income.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a credit adjusted pre-tax rate that reflects current market assessment of the time value of money and, where appropriate, 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.

The Company recognizes provisions arising from legal and/or constructive obligations associated with the cost of dismantling and removing an item of property, plant and equipment and restoring the site where it is located, the obligation for which the Company incurs either when the asset is acquired or as a consequence of having used the asset during a particular year for purposes other than to produce inventories during that year.

Revenue

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and revenue can be reliably measured. The following specific criteria must also be met before revenue is recognized:

Sale of goods. Revenue is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer.

Interest income. Revenue is recognized on a time proportion basis that reflects the effective yield on the assets.

Rental income. Rental income arising on investment properties is accounted for on a straight-line basis over the lease terms.

Dividend income. Dividend income is recognized when the shareholders' right to receive the payment is established.

Operating Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date 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 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 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 specified 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 circumstance gave rise to the reassessment for scenarios a, c or d and at the date of renewal or extension period for scenario b.

For arrangements entered into prior to January 1, 2005, the date of inception is deemed to be January 1, 2005 in accordance with the transitional requirement of Philippine Interpretation IFRIC 4.

Company as a Lessee. Leases where the lessor retains substantially all the risks and benefits of ownership of the assets are classified as operating leases. Operating lease payments are recognized as expense in the consolidated statement of income on a straight-line basis over the lease term.

Company as a Lessor. Leases where the Company retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease terms on the same bases as rental income. Operating lease payments are recognized as income in the consolidated statement of income on a straight-line basis over the lease term.

Foreign Currency-Denominated Transactions and Translations

Transactions in foreign currencies are recorded using the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are restated using the spot exchange rate as of balance sheet date. Exchange gains or losses arising from foreign currency-denominated transactions are credited or charged to current operations.

The functional currency of Ovincor, a foreign subsidiary, is the Philippine peso.

Income Taxes

Current Tax. Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the balance sheet date.

Deferred Tax. Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. 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.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable 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 balance sheet 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.

Income tax relating to items recognized directly in equity is recognized in equity and not in the consolidated statement of income.

Deferred income tax is determined using tax rates (and tax laws) that have been enacted or substantially enacted at the balance sheet date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

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

Sales Tax. Revenues, expenses and assets are recognized net of the amount of sales tax except:

- where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales 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 sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of "Receivables" or "Accounts payable and accrued expenses" account in the consolidated balance sheet.

Earnings Per Share Attributable to the Equity Holders of the Parent

Basic earnings per share is computed by dividing net income by the weighted average number of outstanding shares after giving retroactive effect to any stock split and stock dividends declared during the year. The Company has no dilutive potential common shares outstanding that would require disclosure of diluted earnings per share in the consolidated statement of income.

Segments
The Company's operating businesses are recognized and managed separately according to the nature of the products and invoices provided, with each segment representing a strategic business unit that offers different products and serves different markets. Financial information on business and geographical segments are presented in Note 32.

Contingencies
Contingent liabilities are not recognized in the consolidated financial statements. They are disclosed 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 consolidated financial statements when an inflow of economic benefits is probable.

Subsequent Events
Any post-year-end events that provide additional information about the Company's financial position at the balance sheet date (adjusting event) is reflected in the consolidated financial statements. Post-year-end events that are not adjusting events, if any, are disclosed when material in the notes to consolidated financial statements.

Future Changes in Accounting Policies
The Company has not applied the following PFRS and Philippine Interpretations which are not yet effective for the year ended December 31, 2006:

PFRS 7, "Financial Instruments: Disclosures" and the complementary amendment to PAS 1, "Presentation of Financial Statements," will be effective for annual periods beginning on or after January 1, 2007. PFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, as well as sensitivity analysis to market risk. It replaces PAS 30, "Disclosures in the Financial Statements of Banks and Similar Financial Institutions," and the disclosure requirements in PAS 32, "Financial Instruments: Disclosure and Presentation." It is applicable to all entities that report under PFRS.

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

PFRS 8, "Operating Segments," will be effective for annual periods beginning on or after January 1, 2009. This PFRS adopts a management approach to reporting segment information. PFRS 8 will replace PAS 14, "Segment Reporting," and is required to be adopted only by entities whose debt or equity instruments are publicly traded, or are in the process of filing with the SEC for purposes of issuing any class of instruments in a public market. The information reported would be that which management uses internally for evaluating the performance of operating segments and allocating resources to those segments. Such information may be different from that reported in the consolidated balance sheet and consolidated statement of income and companies will need to provide explanations and reconciliations of the differences. The Company will assess the impact of the standard on its current manner of reporting segment information. The Company will apply PFRS 8 in 2009.

Philippine Interpretation IFRIC 7, "Applying the Restatement Approach under PAS 29, Financial Reporting in Hyperinflationary Economies," will be effective for annual periods beginning on or after March 1, 2006. This interpretation provides guidance on how to apply PAS 29 when an economy first becomes hyperinflationary, in particular, the accounting for deferred income tax. This interpretation has no impact on the consolidated financial statements of the Company. The Company will apply IFRIC 7 in 2007.

Philippine Interpretation IFRIC 11, "PFRS 2 - Group and Treasury Share Transactions," will be effective for annual periods beginning on or after March 1, 2007. This interpretation requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme by the entity even if (a) the entity chooses or is required to buy those equity instruments (e.g., treasury shares) from another party or (b) the shareholder(s) of the entity provide the equity instruments needed. It also provides guidance on how subsidiaries, in their separate financial statements, account for such schemes when their employees receive rights to the equity instruments of the parent company. The Company currently does not have any stock option plan and therefore, does not expect this interpretation to have significant impact on the consolidated financial statements. The Company will apply IFRIC 11 in 2008.

Philippine Interpretation IFRIC 12, "Service Concession Arrangements," will become effective January 1, 2008. This interpretation which covers contractual arrangements arising from entities providing public services, is not relevant to the Company's current operations.

3. Significant Accounting Judgments, Estimates and Assumptions

The preparation of the consolidated financial statements in accordance with PFRS requires the Company to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent assets and contingent liabilities. Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effects of any change in estimates are reflected in the consolidated financial statements as they become reasonably determinable.

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.

Judgments
In the process of applying the Company'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:

Operating Lease Commitments - Company as Lessor/Lessee. The Company has entered into commercial property leases on its investment property portfolio. The Company has determined that it retains all the significant risks and rewards of ownership of the properties leased out on operating leases while the significant risks and rewards for properties leased from third parties are retained by the lessors. Total rent income amounted to ₱345, ₱280 and ₱274 in 2006, 2005 and 2004, respectively (see Note 21), while rent expense amounted to ₱381, ₱306 and ₱271 in 2006, 2005 and 2004, respectively (see Note 18).

Fair Value of Financial Instruments. Where the fair values of financial assets and liabilities recorded in the consolidated balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of liquidity and model inputs such as correlation and volatility for longer dated financial instruments.

The aggregate fair value of the financial assets at FVPL and AFS investments amounted to ₱812 and ₱702 as of December 31, 2006 and 2005, respectively (see Notes 5 and 6).

Estimations and Assumptions
The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing material adjustments to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Allowance for Doubtful Accounts. Allowance for doubtful accounts is maintained at a level considered adequate to provide for potentially uncollectible receivables. The level of allowance is based on past collection experience and other factors that may affect collectibility. An evaluation of the receivables, designed to identify potential charges to the allowance, is performed regularly throughout the year. Specifically, in coordination with Marketing Group, Credit Management evaluates customers who are unable to meet their financial obligations. In these cases, management uses sound judgment based on the best available facts and circumstances, including but not limited to, the length of relationship with the customers and their payment track record. The amounts of provisions differ for each year based on available objective evidence for which the Company may consider that it will probably not be able to collect some of its accounts. Bad debts are written off when identified to be worthless after exhausting all efforts to collect.

An increase in allowance for doubtful accounts would increase the Company's recorded selling and administrative expenses and decrease current assets. Provisions for doubtful accounts/accounts receivable written off amounted to ₱3, ₱106 and ₱162 in 2006, 2005 and 2004, respectively (see Note 18). Reversal of allowance for doubtful accounts amounted to ₱166 in 2006 (see Note 21). Receivables, net of allowance for doubtful accounts, amounted to ₱15,629 and ₱11,863 as of December 31, 2006 and 2005, respectively (see Note 7).

Allowance for Inventory Obsolescence. The allowance for inventory obsolescence consists of collective and specific provisions. A collective provision is established as a certain percentage based on the age and movement of stocks. In case there is write-off or disposal of slow-moving items during the year, a reduction in the allowance for inventory obsolescence is made.

Review of allowance is done every quarter, while a revised set-up or booking is posted at the end of the year based on evaluations or recommendations of the proponents. The amount and timing of recorded expenses for any year would therefore differ based on the judgments or estimates made.

Reversal of allowance for inventory obsolescence amounted to ₱93 in 2006 (see Note 8). Inventories, net of allowance for obsolescence, amounted to ₱26,289 and ₱27,018 as of December 31, 2006 and 2005, respectively (see Note 8).

Useful Lives. The useful life of each of the Company's item of property, plant and equipment and investment properties is estimated based on the period over which the asset is expected to be available for use. Such estimation is based on a collective assessment of practices of similar businesses, internal technical evaluation and experience with similar assets. The estimated useful life of each asset is reviewed periodically and 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 asset. It is possible, however, that future results of operations could be materially affected by changes in the amounts and timing of recorded expenses brought about by changes in the factors mentioned above. A reduction in the estimated useful life of any item of property, plant and equipment and investment properties would increase the recorded cost of goods sold, selling and administrative expenses and decrease noncurrent assets.

There is no change in estimated useful lives of property, plant and equipment and investment properties during the year. Property, plant and equipment and investment properties, net of accumulated depreciation and amortization as of December 31, 2006 and 2005, amounted to ₱25,375 and ₱22,805, respectively (see Notes 9 and 10).

Impairment of Property, Plant and Equipment and Investment Properties. The Company assesses impairment on assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The factors that the Company considers important which could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of use of the acquired assets or the strategy for overall business; and
- significant negative industry or economic trends.

The Company recognizes an impairment loss whenever the carrying amount of an asset exceeds its recoverable value. The recoverable amount is computed using the value in use approach. Recoverable amounts are estimated for individual assets or, if it is not possible, for the cash-generating unit to which the asset belongs. Determining the recoverable value of 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 values and any resulting impairment loss could have a material adverse impact on the results of operations.

No impairment loss was recognized in 2006, 2005 and 2004. The aggregate carrying amount of property, plant and equipment and investment properties, net of accumulated depreciation and amortization amounted to ₱25,375 and ₱22,805 as of December 31, 2006 and 2005, respectively (see Notes 9 and 10).

Pension Costs. The determination of the obligation and cost for pension and other retirement benefits is dependent on the selection of certain assumptions used by actuary in calculating such amounts. Those assumptions are described in Note 25 and include, among others, discount rate and rate of compensation increase. In accordance with PAS 19, "Employee Benefits," as amended, the Company recognizes all actuarial gains and losses in the consolidated statement of recognized income and expense, and therefore generally affects the recorded obligation. While it is believed that the Company's assumptions are reasonable and appropriate, significant differences in actual experience or significant changes in assumptions may materially affect the Company's pension obligations.

Net pension plan assets amounted to ₱434 and ₱1,137 as of December 31, 2006 and 2005, respectively (see Notes 11 and 25). Included under "Other reserves" account in the consolidated balance sheet are cumulative actuarial losses amounting to ₱510 as of December 31, 2006 and cumulative actuarial gains amounting to ₱123 as of December 31, 2005.

Deferred Tax Assets. Significant judgment is required in determining provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Company recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current income tax and deferred tax provisions in the year in which such determination is made.

Deferred income tax assets as of December 31, 2006 and 2005 amounted to ₱825 and ₱1,080, respectively (see Note 22).

Asset Retirement Obligation. Determining asset retirement obligation requires estimation of the costs of dismantling, installations and restoring leased properties to their original condition. The Company determined the amount of asset retirement obligation by obtaining estimates of dismantling costs from proponent who is responsible for the operation of the asset discounted at the Company's current borrowing rates ranging from 7.25% to 9.38% depending on the life of the capitalized costs. While it is believed that the assumptions used in the estimation of such costs are reasonable, significant changes in these assumptions may materially affect the recorded expense or obligation in future periods.

The Company has asset retirement obligation arising from its refinery. Such obligation is not expected to be settled for the foreseeable future and therefore a reasonable estimate of fair value cannot be determined.

Asset retirement obligation as of December 31, 2006 and 2005 amounted to ₱660 and ₱298, respectively (see Note 15).

Contingencies. The Company currently has various tax assessments and legal claims. The Company develops estimate of the probable costs for the assessments and resolution of these claims in consultation with in-house as well as outside legal counsel handling the prosecution and defense of these cases and is based upon an analysis of potential results. The Company currently does not believe these tax assessments and legal claims will have a material adverse effect on its consolidated financial position and results of operations. It is possible, however, that future results of operations could be materially affected by changes in the estimates or in the effectiveness of strategies relating to these proceedings (see Note 33). No provision for probable losses arising from contingencies was recognized in 2006, 2005 and 2004.

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

4. **Cash and Cash Equivalents**

	2006	2005
Cash on hand and in banks	**₱3,767**	₱3,445
Money market placements	**7,968**	495
	₱11,735	₱3,940

Cash in banks earn interest at the respective bank deposit rates. Money market placements are made for varying periods of up to three months depending on the immediate cash requirements of the Company, and earn interest at the respective money market placement rates.

5. **Financial Assets at FVPL**

	2006	2005
Marketable equity securities	**₱131**	₱82
Proprietary membership shares	**49**	34
	₱180	₱116

Changes in fair value recognized in 2006 and 2005 amounted to ₱63 and ₱14, respectively (see Note 21).

6. **AFS Investments**

This account consists of investments in government securities of Petrogen which are deposited with the Insurance Commission in accordance with the provisions of the Insurance Code, for the benefit and security of policyholders and creditors of Petrogen. These investments bear fixed interest rates ranging from 8.5% to 14.6% in 2006 and 4.5% to 11.8% in 2005.

Following is the breakdown of investments in government securities by contractual maturity dates as of December 31, 2006 and 2005:

	2006	2005
Due in one year or less	**₱103**	₱259
Due after one year through five years	**529**	327
	₱632	₱586

7. **Receivables**

	2006	2005
Trade	**₱11,489**	₱11,890
Others	**4,824**	820
	16,313	12,710
Less allowance for doubtful accounts	**684**	847
	₱15,629	₱11,863

Trade receivables are noninterest-bearing and generally on a 45-day term.

8. **Inventories**

	2006	2005
At cost:		
Petroleum	**₱13,867**	₱14,683
Crude oil and others	**11,905**	11,947
At net realizable value -		
TBA products, materials and supplies	**517**	388
	₱26,289	₱27,018

Using the moving-average method, the cost of petroleum, crude oil and other products would have increased by ₱355 as of December 31, 2006 and ₱619 as of December 31, 2005.

Cost of TBA products, material and supplies amounted to ₱858 as of December 31, 2006 and ₱822 as of December 31, 2005. Reversal of allowance for inventory obsolescence charged to cost of goods sold amounted to ₱93 in 2006 (see Note 17).

Inventories charged to cost of goods sold amounted to ₱194,281, ₱173,789 and ₱132,811 in 2006, 2005 and 2004, respectively (see Note 17).

9. **Property, Plant and Equipment**

	2006						
	Buildings and Related Facilities	**Refinery and Plant Equipment**	**Service Stations and Other Equipment**	**Computers, Office and Motor Equipment**	**Land and Leasehold Improvements**	**Construction in-Progress**	**Total**
Net carrying amount, at January 1, 2006	**₱5,585**	**₱11,569**	**₱707**	**₱445**	**₱2,722**	**₱1,542**	**₱22,570**
Additions	**47**	**-**	**18**	**10**	**15**	**4,962**	**5,052**
Reclassifications	**1,339**	**(1,339)**	**-**	**-**	**-**	**-**	**-**
Depreciation and amortization for the year (see Note 20)	**(599)**	**(1,369)**	**(214)**	**(178)**	**(109)**	**-**	**(2,469)**
Transfers	**840**	**348**	**327**	**226**	**193**	**(1,934)**	**-**
Net carrying amount, at December 31, 2006	**₱7,212**	**₱9,209**	**₱838**	**₱503**	**₱2,821**	**₱4,570**	**₱25,153**

	2006						
	Buildings and Related Facilities	**Refinery and Plant Equipment**	**Service Stations and Other Equipment**	**Computers, Office and Motor Equipment**	**Land and Leasehold Improvements**	**Construction in-Progress**	**Total**
At December 31, 2006							
Cost	**₱13,041**	**₱18,361**	**₱3,390**	**₱2,010**	**₱3,874**	**₱4,570**	**₱45,246**
Accumulated depreciation and amortization	**(5,829)**	**(9,152)**	**(2,552)**	**(1,507)**	**(1,053)**	**-**	**(20,093)**
Net carrying amount	**₱7,212**	**₱9,209**	**₱838**	**₱503**	**₱2,821**	**₱4,570**	**₱25,153**

	2005						
	Buildings and Related Facilities	Refinery and Plant Equipment	Service Stations and Other Equipment	Computers, Office and Motor Equipment	Land and Leasehold Improvements	Construction in-Progress	Total
Net carrying amount, at January 1, 2005	₱5,510	₱9,358	₱540	₱433	₱917	₱5,688	₱22,446
Additions	195	–	16	8	1,861	368	2,448
Depreciation and amortization for the year (see Note 20)	(408)	(1,476)	(177)	(146)	(117)	–	(2,324)
Transfers	288	3,687	328	150	61	(4,514)	–
Net carrying amount, at December 31, 2005	₱5,585	₱11,569	₱707	₱445	₱2,722	₱1,542	₱22,570
At December 31, 2005							
Cost	₱8,081	₱22,105	₱3,037	₱1,796	₱3,667	₱1,542	₱40,228
Accumulated depreciation and amortization	(2,496)	(10,536)	(2,330)	(1,351)	(945)	–	(17,658)
Net carrying amount	₱5,585	₱11,569	₱707	₱445	₱2,722	₱1,542	₱22,570

Interest capitalized in 2006 amounted to ₱52 using capitalization rates of 6.843% and 8.705% for general and specific borrowing peso loans, respectively. Interest capitalized in 2005 amounted to ₱46 using a capitalization rate of 6.94% for general borrowing peso loans.

10. **Investment Properties**

		2006	
	Land	**Office Units**	**Total**
Net carrying amount, at January 1, 2006	**₱48**	**₱187**	**₱235**
Depreciation for the year (see Note 20)	**-**	**(13)**	**(13)**
Net carrying amount, at December 31, 2006	**₱48**	**₱174**	**₱222**
At December 31, 2006			
Cost	**₱48**	**₱263**	**₱311**
Accumulated depreciation	**-**	**(89)**	**(89)**
Net carrying amount	**₱48**	**₱174**	**₱222**

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

	2005		
	Land	Office Units	Total
Net carrying amount, at January 1, 2005	₱32	₱198	₱230
Additions	16	–	16
Depreciation for the year (see Note 20)	–	(11)	(11)
Net carrying amount, at December 31, 2005	₱48	₱187	₱235
At December 31, 2005			
Cost	₱48	₱263	₱311
Accumulated depreciation	–	(76)	(76)
Net carrying amount	₱48	₱187	₱235

The Company's investment properties consist of office units located in Petron MegaPlaza and parcels of land in various locations intended for service stations. Estimated fair values for office units located in Petron MegaPlaza based on zonal valuation determined by the Bureau of Internal Revenue (BIR), amounted to ₱183 in 2006.

Rental income earned from the investment properties amounted to ₱16, ₱20 and ₱15 in 2006, 2005 and 2004, respectively.

There are no other direct selling and administration expenses (i.e., repairs and maintenance) arising from investment properties that generated rent income in 2006, 2005 and 2004.

11. Other Noncurrent Assets

	2006	2005
Net pension plan assets (see Note 25)	**₱434**	₱1,137
Others	**188**	124
	₱622	₱1,261

12. Short-term Loans

This account pertains to unsecured peso loans obtained from local banks with interest ranging from 5.0% to 7.5%, intended to fund the importation of crude oil and petroleum products, capital expenditures and working capital requirements.

13. Accounts Payable and Accrued Expenses

	2006	2005
Accounts payable	**₱1,298**	₱472
Accrued expenses	**1,390**	1,406
Specific and other taxes payable	**425**	336
Derivative liabilities (see Note 30)	**64**	5
Others	**554**	407
	₱3,731	₱2,626

Terms and conditions are as follows:

- Accounts payable are noninterest-bearing and are normally settled on a 30-day term.
- Accrual of unpaid interest and selling and administrative expenses are normally settled within a year.

14. Long-term Debt

	2006	2005
Unsecured peso loans (net of debt issue cost amounting to ₱70 in 2006)	**₱8,538**	₱1,673
Syndicated dollar bank loans (net of debt issue costs amounting to ₱58 in 2006 and ₱80 in 2005)	**4,374**	5,258
	12,912	6,931
Less current portion (net of debt issue costs amounting to ₱41 in 2006 and ₱21 in 2005)	**1,633**	1,906
	₱11,279	₱5,025

Movements of debt issue costs are as follows:

	2006	2005
Beginning balance	**₱80**	₱100
Additions	**74**	–
Accretion for the year (see Note 21)	**(26)**	(20)
Ending balance	**₱128**	₱80

The salient terms of the foregoing loans are summarized as follows:

Original Amount	Land Bank - ₱2 billion	BPI - ING ₱6.3 billion	NORD - LB US$100 million	Citibank - ₱2 billion
Payment Terms	12 equal quarterly installments starting March 2009 up to November 2011	One time payment in August 2011	Six semi-annual installments starting on the 30th month from June 2004 up to June 2009	13 equal quarterly installments starting April 2004 up to April 2007
Interest (2006)	6.1%	8.875%	5.7% to 6.8%	6.7% to 8.2%
Security	None	None	None	None
Major Covenants	None	Maintenance of certain financial ratios	Maintenance of certain financial ratios	Maintenance of certain financial ratios

As of December 31, 2006, the Company is in compliance with its loan covenants. Loan maturities (gross of ₱128 debt issue costs) for the next five years are as follows:

Year	Amount
2007	₱1,674
2008	1,962
2009	1,770
2010	667
2011	6,967
	₱13,040

15. Other Noncurrent Liabilities

	2006	2005
Asset retirement obligation (ARO)	**₱660**	₱298
Cylinder deposits	**206**	244
Cash bonds	**141**	119
Others	**42**	36
	₱1,049	₱697

Movements of ARO are as follows:

	2006	2005
Beginning balance	**₱298**	₱256
Additions	**10**	9
Effect of change in discount rate	**324**	–
Accretion for the year (see Note 21)	**37**	33
Settlement	**(9)**	–
Ending balance	**₱660**	₱298

The Company has ARO arising from its refinery. Such obligation is not expected to be settled for the foreseeable future and therefore a reasonable estimate of fair value cannot be determined.

16. Changes in Equity

	Equity Attributable to Holders of the Parent			
		Retained Earnings		Minority
	Capital Stock	Appropriated	Unappropriated	Interest
Balance at January 1, 2006	**₱9,375**	**₱11,652**	**₱6,352**	**₱108**
Net income for the year	**-**	**-**	**6,011**	**7**
Actuarial gains due to limit on recognized plan asset - net of tax effect	**-**	**-**	**176**	**-**
Appropriation for capital projects	**-**	**5,369**	**(5,369)**	**-**
Cash dividends - ₱ 0.10 per share	**-**	**-**	**(938)**	**-**
Balance at December 31, 2006	**₱9,375**	**₱17,021**	**₱6,232**	**₱115**
Balance at December 31, 2004, as restated	₱9,375	₱6,906	₱5,623	₱110
Effect of changes in accounting for financial instruments (see Note 2)	–	–	(39)	(9)
Balance at January 1, 2005, as adjusted	9,375	6,906	5,584	101
Net income for the year	–	–	6,044	7
Actuarial gains due to limit on recognized plan asset - net of tax effect	–	–	408	–
Appropriation for capital projects	–	4,746	(4,746)	–
Cash dividends - ₱0.10 per share	–	–	(938)	–
Balance at December 31, 2005	₱9,375	₱11,652	₱6,352	₱108
Balance at January 1, 2004	₱9,375	₱5,551	₱4,874	₱103
Net income for the year	–	–	4,094	7
Actuarial losses due to limit on recognized plan asset - net of tax effect	–	–	(115)	–
Appropriation for capital projects	–	1,355	(1,355)	–
Cash dividends - ₱0.20 per share	–	–	(1,875)	–
Balance at December 31, 2004	₱9,375	₱6,906	₱5,623	₱110

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

a. Capital Stock

	Number of Shares	Amount
Authorized - ₱1.00 par value	10,000,000,000	₱10,000
Issued and outstanding	9,375,104,497	₱9,375

Petron was registered with the SEC on December 15, 1966.

The issued and outstanding common shares have been adjusted for the fractional shares issued in prior years.

b. Retained Earnings

i. Declaration of Cash Dividends

In 2006 and 2005, the Company declared a cash dividend of ₱0.10 per share amounting to ₱938 to all stockholders of record as of June 2, 2006 and May 12, 2005, respectively. In 2004, a cash dividend of ₱0.20 per share amounting to ₱1,875 was declared to all stockholders of record as of May 19, 2004.

ii. Appropriation for Capital Projects

Petron appropriated ₱5,369 in 2006 and ₱4,746 in 2005 for future capital projects.

17. Cost of Goods Sold

	2006	2005	2004
Inventories (see Notes 8, 23 and 26)	**₱194,281**	₱173,789	₱132,811
Depreciation and amortization (see Note 20)	**1,536**	1,459	1,009
Employee costs (see Notes 19 and 25)	**406**	411	378
Others - net (see Note 8)	**1,291**	1,551	1,200
	₱197,514	₱177,210	₱135,398

18. Selling and Administrative Expenses

	2006	2005	2004
Employee costs (see Notes 19 and 25)	**₱1,199**	₱1,023	₱1,225
Depreciation and amortization (see Note 20)	**946**	876	847
Purchased services and utilities	**817**	748	734
Maintenance and repairs	**473**	567	629
Rent (see Note 23)	**381**	306	271
Advertising	**222**	398	403
Materials and office supplies	**164**	281	260
Expenses related to oil spill incident in Guimaras (see Note 33f)	**122**	–	–
Taxes and licenses	**104**	102	177
Provision for doubtful accounts/accounts receivable written-off	**3**	106	162
Others	**54**	120	169
	₱4,485	₱4,527	₱4,877

19. Employee Costs

Employee costs consist of:

	2006	2005	2004
Salaries, wages and other employee costs	**₱1,601**	₱1,432	₱1,596
Pension costs (see Note 25)	**4**	2	7
	₱1,605	₱1,434	₱1,603

The above amounts are distributed as follows:

	2006	2005	2004
Cost of goods sold (see Note 17)	**₱406**	₱411	₱378
Selling and administrative expenses (see Note 18)	**1,199**	1,023	1,225
	₱1,605	₱1,434	₱1,603

20. Depreciation and Amortization

Depreciation and amortization are distributed as follows:

	2006	2005	2004
Cost of goods sold -			
Property, plant and equipment (see Notes 9 and 17)	**₱1,536**	₱1,459	₱1,009
Selling and administrative expenses (see Note 18):			
Property, plant and equipment (see Note 9)	**933**	865	835
Investment properties (see Note 10)	**13**	11	12
	946	876	847
	₱2,482	₱2,335	₱1,856

21. Interest Expense, Interest Income and Others

	2006	2005	2004
Interest expense:			
Short-term loans (see Note 12)	**(₱1,608)**	(₱810)	(₱985)
Long-term debt (see Note 14)	**(594)**	(805)	(341)
Accretion on ARO (see Note 15)	**(37)**	(33)	(28)
Product borrowings	**(31)**	(57)	(87)
Accretion on debt issue costs (see Note 14)	**(26)**	(20)	(10)
Others	**(388)**	(366)	(224)
	(₱2,684)	(₱2,091)	(₱1,675)

	2006	2005	2004
Interest income:			
Money market placements	**₱250**	₱249	₱180
Trade receivables	**83**	42	124
Cash in banks	**12**	9	8
Product loaning	**9**	13	28
Investment bonds	**–**	–	2
Others	**8**	4	2
	₱362	₱317	₱344

Other income (charges):			
Rent	**₱345**	₱280	₱274
Foreign exchange gain (loss) - net	**388**	306	(298)
Derivatives net of fair value loss (see Note 30)	**(279)**	(260)	–
Reversal of allowance for doubtful accounts	**166**	–	–
Changes in fair value of financial assets at FVPL (see Note 5)	**63**	14	(91)
Insurance claims (see Note 23)	**29**	–	–
Gain on settlement of ARO (see Note 15)	**13**	–	–
Miscellaneous	**(226)**	(176)	(280)
	₱499	₱164	(₱395)

22. Income Taxes

The major components of provision for (benefit from) income tax are as follows:

	2006	2005	2004
Current income tax -			
Current income tax charge	**₱1,723**	₱2,057	₱1,339
Deferred income tax:			
Relating to origination and reversal of temporary differences	**₱108**	₱102	(₱16)
Change in tax rate	**55**	(68)	–
	₱163	₱34	(₱16)

The significant components of deferred tax assets and liabilities are as follows:

	2006	2005
Deferred tax assets:		
Rental	**₱163**	₱205
Inventory differential	**124**	217
ARO	**81**	90
Various allowances, accruals and others	**456**	565
	824	1,077
Deferred tax liabilities:		
Excess of double-declining over straight-line method of depreciation and amortization	**1,270**	1,267
Capitalized taxes and duties on inventories deducted in advance	**388**	411
Unrealized foreign exchange gain - net	**112**	97
Capitalized interest, duties and taxes on property, plant and equipment deducted in advance and others	**358**	445
	2,128	2,220
	(₱1,304)	(₱1,143)

Net deferred tax assets of the subsidiaries without right of offset amounted to ₱1 and ₱3 as of December 31, 2006 and 2005, respectively.

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

The components deferred tax liabilities charged to equity are as follows:

	2006	2005
Net pension plan asset	**₱130**	₱372
Unrealized fair value gains on AFS investments	**9**	1
	₱139	₱373

The reconciliation between the provision for income tax computed at the applicable statutory income tax rates and, using tax rates of 35% in 2006 and 32% for the period starting January 1 to October 31 and 35% for the period starting from November 1 to December 31 in 2005 and 32% in 2004, provision for income tax as shown in the consolidated statements of income is summarized as follows:

	2006	2005	2004
Income tax computed at statutory income tax rates	**₱2,766**	₱2,646	₱1,736
Additions (reductions) resulting from:			
Income subject to income tax holiday (see Note 31)	**(736)**	(440)	(410)
Changes in fair value of financial assets at FVPL (see Note 21)	**(22)**	(5)	29
Interest income subjected to lower final tax and others	**(122)**	(110)	(32)
	₱1,886	₱2,091	₱1,323

Provision for income tax includes final withholding tax on interest income.

On May 24, 2005, the President of the Republic of the Philippines signed into law Republic Act (RA) No. 9337, which took effect on November 1, 2005, introducing the following changes:

a. Regular corporate income tax (RCIT) rate for domestic corporations and resident and non-resident foreign corporations is increased to 35% (from 32%) beginning November 1, 2005 and the rate will be reduced to 30% beginning January 1, 2009. RCIT rate shall be applied on the amount computed by multiplying the number of months covered by the new rate within the fiscal year by the taxable income of the corporation for the period, divided by 12 months.

b. Power of the President upon the recommendation of the Secretary of Finance to increase the rate of value added tax (VAT) to 12% (from 10%), after any of the following conditions has been satisfied:

   i. VAT collection as a percentage of gross domestic product (GDP) of the previous year exceeds two and four-fifth percent (2 4/5%); or

   ii. National Government deficit as a percentage of GDP of the previous year exceeds one and one-half percent (1 1/2%).

   On January 31, 2006, a Revenue Memorandum Circular No. 7-2006 was issued approving the recommendation of the Secretary of Finance to increase VAT to 12% (from 10%) effective February 1, 2006.

c. Input VAT on completed/finished capital goods should be spread evenly over the useful life or 60 months, whichever is shorter, if the acquisition costs, excluding the VAT component thereof exceed ₱1. On the other hand, input VAT on assembled or constructed capital goods shall be recognized at the time of payment to the independent constructors as it involved a sale of service.

d. Input VAT credit in every quarter shall not exceed 70% of the output VAT if the amount of input VAT exceeds the total output VAT. The excess input VAT shall be carried over to the succeeding period/s and is not allowed to be written-off for income tax purposes.

   However, last November 21, 2006, RA No. 9361 was approved removing the 70% cap on input VAT. This means that VAT-registered taxpayers are allowed to have excess input taxes, and not VAT payable, at the end of any taxable quarter. The excess input VAT shall be carried over to the succeeding quarter or quarters. This new ruling is effective December 13, 2006.

23. **Related Party Transactions**

The significant transactions with related parties are as follows:

			2006	
Name of Company	Relationship	Nature of Transaction	**Transaction Amount**	**Balance at End of Year**
Saudi Arabian Oil Company (Saudi Aramco)	Ultimate parent of Aramco Overseas Company B.V. (Stockholder)	Crude purchases	**₱145,099**	**(₱36)**
Philippine National Oil Company (PNOC)	Stockholder	Leases	**147**	**(33)**

			2005	
Name of Company	Relationship	Nature of Transaction	Transaction Amount	Balance at End of Year
Saudi Aramco	Ultimate parent of Aramco Overseas Company B.V. (Stockholder)	Crude purchases	₱122,826	(₱5,728)
PNOC	Stockholder	Leases	145	–

- Petron and Saudi Aramco have a term contract to purchase and supply, respectively, 90% of Petron's monthly crude oil requirements over a 20-year period at Saudi Aramco's standard Far East selling prices. Outstanding liabilities of Petron for such purchases are shown as part of "Liabilities for crude oil and petroleum product importation" account in the consolidated balance sheets.

- Petron has long-term lease agreements with PNOC until August 2018 covering certain lots where its refinery and other facilities are located. Lease charges on refinery facilities escalate at 2% a year, subject to increase upon reappraisal (see Note 24).

Total compensation and benefits of key management personnel of the Company, amounting to ₱319, ₱290 and ₱278 in 2006, 2005 and 2004, respectively, consist of:

	2006	2005	2004
Salaries and other short-term employee benefits	**₱277**	₱248	₱232
Post-employment benefits (see Note 25)	**42**	42	46
	₱319	₱290	₱278

24. **Operating Lease Commitments**

Company as Lessee
The Company entered into commercial leases on certain parcels of land. These leases have an average life of between one to 16 years with renewal options included in the contracts. There are no restrictions placed upon the Company by entering into these leases. The lease agreements include upward escalation adjustment of the annual rental rates.

Future minimum rental payable under the non-cancellable operating lease agreements as of December 31 follows:

	2006	2005
Within one year	**₱384**	₱377
After one year but not more than five years	**1,728**	1,518
After five years	**1,558**	2,620
	₱3,670	₱4,515

Company as Lessor
The Company has entered into lease agreements on its investment property portfolio, consisting of surplus office spaces and parcels of land. The non-cancellable leases have remaining terms of between three to five years. All leases include a clause to enable upward escalation adjustment of the annual rental rates.

Future minimum rental receivable under the non-cancelable operating lease agreements as of December 31 follows:

	2006	2005
Within one year	**₱177**	₱168
After one year but not more than five years	**202**	175
After five years	**123**	141
	₱502	₱484

25. **Pension Plan**

The following tables summarize the components of net pension costs recognized in the consolidated statements of income and the funded status and amounts recognized in the consolidated balance sheets for the pension plan.

Net Pension Costs (Recognized in Selling and Administrative Expenses)

	2006	2005	2004
Current service cost	**₱122**	₱101	₱106
Interest cost on benefit obligation	**256**	239	206
Expected return on plan assets	**(374)**	(338)	(305)
Net pension costs	**₱4**	₱2	₱7
Actual return on plan assets	**₱687**	₱437	₱395

Actuarial Gain (Loss) Recognized Directly in Equity

	2006	2005	2004
Actuarial gain (loss) for the year due to present value of obligation	**(₱1,282)**	(₱363)	₱364
Actuarial gain for the year	**313**	99	90
Actuarial gain (loss) due to limit on recognized plan assets	**270**	620	(168)
Net actuarial gain (loss) recognized	**(₱699)**	(₱356)	₱286

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

Net Pension Asset

	2006	2005
Defined benefit obligation	₱3,783	₱2,330
Fair value of plan assets	4,217	3,737
Pension asset	434	1,407
Less unrecognized assets due to limit	-	270
Net pension asset recognized (see Note 11)	₱434	₱1,137

Changes in the present value of the defined benefit obligation are as follows:

	2006	2005
Opening defined benefit obligation	₱2,330	₱1,709
Interest cost	256	239
Current service cost	122	101
Benefits paid	(207)	(82)
Actuarial loss on obligation	1,282	363
Closing defined benefit obligation	₱3,783	₱2,330

Changes in the fair value of plan assets are as follows:

	2006	2005
Opening fair value of plan assets	₱3,737	₱3,382
Expected return	374	338
Benefits paid	(207)	(82)
Actuarial gains on plan assets	313	99
Closing fair value of plan assets	₱4,217	₱3,737

The Company does not expect to contribute to its defined benefit pension plan until 2010.

The major categories of plan assets as a percentage of the fair value of total plan assets are as follows:

	2006	2005
Cash	1%	5%
Government securities	57%	71%
Stocks	31%	15%
Real estate	7%	8%
Others	4%	1%
	100%	100%

The overall expected rate of return on assets is determined based on the market prices prevailing on that date, applicable to the period over which the obligation is to be settled. There has been a significant change in the expected rate of return on assets due to the improved stock market scenario.

As of January 1, 2006 and 2005, the principal assumptions used in determining obligations for the Company's pension plan are shown below:

	2006	2005
Discount rate	11%	14%
Expected rate of return on plan assets	10%	10%
Future salary increases	8.5%	9%

The prevailing discount rate as of December 31, 2006 is 7.25%.

Amounts for the current and previous four periods are as follows:

	2006	2005	2004	2003	2002
Defined benefit obligation	₱3,783	₱2,330	₱1,709	₱1,821	₱2,073
Fair value of plan assets	4,217	3,737	3,382	3,047	2,841
Surplus	₱434	₱1,407	₱1,673	₱1,226	₱768

Experience adjustments on present value of obligation amounted to ₱151 in 2006.

26. **Supplementary Information**

a. Processing License Agreement

Petron has an agreement with Pennzoil-Quaker State International Corporation (Pennzoil) for the exclusive right to manufacture, sell and distribute in the Philippines certain Pennzoil products until December 31, 2008. The agreement also includes the license to use certain Pennzoil trademarks in exchange for the payment of royalty fee based on net sales value. Royalty expense amounting to ₱0.9, ₱1.07 and ₱1.20 in 2006, 2005 and 2004, respectively, are included as part of "Cost of goods sold" account in the consolidated statements of income.

b. Fuel Supply Contract with National Power Corporation (NPC)

The Company entered into various fuel supply contracts with NPC. Under the agreement, the Company supplies the bunker fuel and diesel fuel oil requirements to selected NPC plants and NPC-supplied Independent Power Plants.

In the bidding held last November 9, 2006, for NPC fuel requirements from January to December 2007, Petron won a total of 13,604 kiloliters (KL) of diesel fuel and 308,584 KL of bunker fuel worth ₱2,390 and ₱6,967, respectively.

Sales from the above transactions amounted to ₱10,727, ₱10,211 and ₱11,453 in 2006, 2005 and 2004, respectively.

27. **Basic Earnings Per Share Attributable to Equity Holders of the Parent**

	2006	2005	2004
Net income attributable to equity holders of the parent	**₱6,011**	₱6,044	₱4,094
Weighted average number of shares	**9,375,104,497**	9,375,104,497	9,375,104,497
Basic earnings per share	**₱0.64**	₱0.64	₱0.44

28. **Supplemental Disclosure of Cash Flow Information**
Changes in operating assets and liabilities:

	2006	2005	2004
Decrease (increase) in assets:			
Trade receivables	**₱337**	(₱2,084)	(₱2,503)
Inventories	822	(4,769)	(4,316)
Other current assets	**(5,842)**	(1,796)	(69)
Increase (decrease) in liabilities:			
Liabilities for crude oil and petroleum product importation	**(289)**	1,814	(445)
Accounts payable and accrued expenses	**859**	158	706
	(4,113)	(6,677)	(6,627)
Provisions (reversal of allowance) for doubtful accounts, inventory obsolescence and others	**(169)**	351	534
	(₱4,282)	(₱6,326)	(₱6,093)

29. **Financial Risk Management Objectives and Policies**

The Company's principal financial instruments include bank loans, cash and cash equivalents and derivative instruments. The main purpose of bank loans is to finance working capital relating to the importation of crude and petroleum products, as well as to partly fund capital expenditures. The Company has other financial assets and liabilities such as trade receivables and trade payables and investments in debt and equity securities, which are generated directly from its operations.

It is the Company's policy not to enter into derivative transactions for speculative purposes. The Company uses commodity price swaps to protect its margin on industrial fuel from potential price volatility of crude oil and industrial fuel oil. It also enters into short-term forward currency contracts to hedge its currency exposure on crude oil importations.

The main risks arising from the Company's financial instruments are foreign exchange risk, interest rate risk, credit risk, liquidity risk and commodity price risk. The BOD regularly reviews and approves the policies for managing these financial risks, as summarized below:

Foreign Exchange Risk
Foreign exchange risk occurs due to currency differences in the Company's assets and liabilities The Company's foreign currency-denominated assets and liabilities were predominantly in U.S. dollars in 2006 and 2005.

This is a major structural risk for the Company since crude and product imports, which comprise the bulk of its inputs to operations, are U.S. dollar-denominated. On the other hand, the Company receives peso-denominated revenue for the majority of its product sales.

The Company pursues a policy of hedging foreign exchange risk by purchasing currency forwards or by substituting U.S. dollar-denominated liabilities with peso-based debt. The natural hedge provided by dollar-denominated assets is also factored in hedging decisions. As a matter of policy, currency hedging is limited to the extent of 100% of the underlying exposure.

The Company is allowed to engage in active risk management strategies for a portion of its foreign exchange risk exposure. Loss limits are in place, monitored daily and regularly reviewed by management.

Interest Rate Risk
The Company's exposure to interest rate risk is mainly related to its long-term debt instruments. Currently, the Company has achieved a balanced mix of fixed and floating rates on its various long-term debts.

Future hedging decisions for floating interest rates will continue to be guided by an assessment of the overall interest rate risk profile of the Company's consolidated balance sheet and the net effect on this of possible interest rate movements.

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

Credit Risk
In effectively managing credit risk, Petron regulates and extends credit only to qualified and credit-worthy customers in consonance with established Company credit policies and guidelines and credit verification procedures. Requests for credit lines from trade customers undergo stages of review between the Marketing and Finance Groups while approvals, which are based on amounts of credit lines requested, are vested among line managers and top management that include the President and the Chairman. To the extent practicable, Petron also requires collateral as security for a credit facility to mitigate risk of customer's default.

In monitoring trade receivables and credit lines, Petron maintains up-to-date records where daily sales and collection transactions of all customers are recorded in real-time and month-end statements of accounts are forwarded to customers as collection medium. In close coordination with Petron's Marketing Group which is primarily tasked with collecting customers' accounts through the account executives scattered nationwide, Credit Department regularly reports to management trade receivable balances (monthly) and credit utilization (semi-annual) efficiency. The Company has made provisions, where necessary, for potential losses on credits extended.

The Company's exposure to credit risk arises from default of the counterparty with a maximum exposure equal to the carrying amount of these instruments, net of the value of collaterals, if any.

Counterparties to financial instruments consist of a large number of prime financial institutions. The Company does not expect any counterparty to default in its obligations, given the high credit ratings. The Company has no significant concentration of credit risk with any counterparty.

Liquidity Risk
The Company is exposed to the possibility that adverse changes in the business environment and/or its operations would result to substantially higher working capital requirements and the subsequent difficulty in financing additional working capital.

The Company manages liquidity risk by maintaining a pool of credit lines from financial institutions that exceeds expected financing requirements for working capital. The Company likewise regularly evaluates other financing instruments and arrangements to broaden the Company's range of financing sources.

Commodity Price Risk
To minimize the Company's risk of potential losses due to volatility of Dubai and Singapore's Mean of Platts (MOPS) prices, the Company implemented commodity hedging for hedgeable petroleum products. Hedging policy (including the use of commodity price swaps) developed by the Risk Management Committee is already in place. Decisions are guided by the conditions set and approved by the Company's management.

30. **Financial Instruments**

Derivative Instruments
The Parent Company's derivative transactions are intended as economic hedge of well-defined foreign currency and commodity price risks. The Parent Company opted to adopt non-hedge accounting treatment for all its derivative transactions (including embedded derivatives).

Freestanding Derivatives. The Parent Company uses IFO-Dubai crack spread swaps to protect its margin on export and domestic sales of industrial fuel oil products. The cost base of the Parent Company's industrial fuel is that of the crude oil, most of which is supplied by Saudi Aramco and is priced based on Dubai/Oman crude price. On the other hand, the selling price of the industrial fuel is based on MOPS. Under the crack spread swap, the Parent Company and its counterparties agree to a monthly exchange of cash settlements based on a specified reference price, depending on the commodity being hedged. For the IFO portion of the crack spread swap that hedges the price risks on industrial fuel oil products, the Company acts as the floating rate payer and the reference price index is the monthly MOPS for HSFO 180 CST. For the Dubai portion that hedges the price risks on crude oil, the Parent Company acts as the fixed rate payer and the reference price index is the monthly average for Platt's Dubai Crude. The swap agreements effectively hedge the Parent Company's margin on industrial fuel oil. As of December 31, 2006 and 2005, there are no outstanding commodity swaps.

On January 22, 2007, Petron concluded with Mitsui & Co. Energy Risk Management a Fuel Oil / Dubai crack swap for February 2007 for a volume of 10,000 barrels. Approved monthly allowable volume to be hedged ranges from 250,000-500,000 barrels, depending on export volumes contracted for a given month.

The Parent Company also enters into deliverable and non-deliverable short-term currency forward contracts to hedge its foreign currency exposure on crude oil importations. As of December 31, 2006 and 2005, the Parent Company has outstanding currency forward contracts with an aggregate notional amount of US$109 and US$45, respectively, and weighted average contracted forward rate of ₱49.704 to US$1.00 and ₱53.206 to US$1.00, respectively. The net fair value loss on these currency forward contracts as of December 31, 2006 and 2005 amounted to ₱64 and ₱5, respectively.

Embedded Derivatives. Embedded foreign currency derivatives exist in certain of the Parent Company's U.S. dollar-denominated sales and purchase contracts for various fuel products. Under the sales contracts, the Parent Company agrees to fix the peso equivalent of the invoice amount based on the average Philippine Dealing System (PDS) rate of the month of delivery. In the purchase contracts, the peso equivalent is determined using the average PDS rate of the month preceding the month of delivery. The net fair value gain on these transactions as of December 31, 2006 and 2005 amounted to ₱58 and ₱60, respectively.

Fair Value Changes on Derivatives
The net movements in fair value changes of all derivative transactions in 2006 and 2005 are as follows:

	MTM Loss
Fair values at January 1, 2006	**(₱55)**
Net changes in fair value during the year (see Note 21)	**279**
Less fair value of settled instruments	**218**
Balance at December 31, 2006	**₱6**
Fair values at January 1, 2005	₱31
Net changes in fair value during the year (see Note 21)	260
Less fair value of settled instruments	346
Balance at December 31, 2005	(₱55)

Included in the consolidated balance sheets as follows:

	2006	2005
Derivative assets (included under "Other current assets" account)	**₱58**	₱60
Derivative liabilities (see Note 13)	**(64)**	(5)
Net	**(₱6)**	₱55

Interest Rate Risk

The following table sets out the carrying amount, by maturity, of the Company's financial instruments that are exposed to interest rate risk:

	Interest Rates	Within 1 Year	1-2 years	2-3 Years	3-4 years	4-5 Years	Total
2006 Fixed Rate:							
Short-term debt (PHP)	**5.3%**	**₱28,115**	**-**	**-**	**-**	**-**	**₱28,115**
Long-term debt - (FXCN in PHP)	**8.875%**	**-**	**-**	**-**	**-**	**₱6,300**	**₱6,300**
2006 Floating Rate:							
Long-term loan (Landbank)	**6.1%**	**-**	**-**	**₱667**	**₱667**	**₱666**	**₱2,000**
Long-term loan (Citibank)	**7.4%**	**₱308**	**-**	**-**	**-**	**-**	**₱308**
Long-term loan (NORD in USD)	**6.2%**	**$28**	**$40**	**$22**	**-**	**-**	**$90**
2005 Fixed Rate -							
Short-term debt (PHP)	7.0%	₱21,432	–	–	–	–	₱21,432
2005 Floating Rate:							
Long-term loan (Landbank)	7.2%	750	–	–	–	–	750
Long-term loan (Citibank)	8.0%	₱615	₱308	–	–	–	₱923
Long-term loan (NORD in USD)	5.8%	$10	$28	–	$62	–	$100

Interest on financial instruments classified as floating rate was repriced quarterly for the peso loans and quarterly or semi-annually for the U.S. dollar-denominated loans. Interest on financial instruments classified as fixed rate was fixed until the maturity of the instrument. Other financial liabilities of the Company that were not included in the above tables were noninterest-bearing and were, therefore, not subject to interest rate risk.

The Company has interest-bearing assets of ₱12,367 as of December 31, 2006 and ₱4,526 as of December 31, 2005, of which ₱11,598 and ₱4,330, respectively, have maturities within 1 year (see Notes 4 and 6). Financial assets at FVPL are noninterest-bearing investments and are therefore not subject to interest rate volatility (see Note 5).

The following table sets forth the carrying values and estimated fair values of the Company's financial assets and liabilities:

	2006		2005	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Current financial assets:				
Cash and cash equivalents	**₱11,735**	**₱11,735**	₱3,940	₱3,940
Financial assets at FVPL	**180**	**180**	116	116
AFS investments	**103**	**103**	259	259
Receivables	**15,629**	**15,629**	11,863	11,863
Derivative assets (included under "Other current assets" account)	**58**	**58**	60	60
Total current financial assets	**27,705**	**27,705**	16,238	16,238
Noncurrent financial assets - AFS investments	**529**	**529**	327	327
Total financial assets	**₱28,234**	**₱28,234**	₱16,565	₱16,565
Current financial liabilities:				
Short-term loans	**₱28,135**	**₱28,135**	₱21,407	₱21,407
Liabilities for crude oil and petroleum product importation	**7,541**	**7,541**	7,911	7,911
Accounts payable and accrued expenses	**2,752**	**2,752**	1,883	1,883
Total current financial liabilities	**38,428**	**38,428**	31,201	31,201
Noncurrent financial liabilities:				
Cash bonds (included under "Other noncurrent liabilities" account)	**141**	**135**	119	98
Long-term debt (including current portion)	**12,912**	**12,973**	6,931	7,032
Total financial liabilities	**₱51,481**	**₱51,536**	₱38,251	₱28,331

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for financial assets and which it is practicable to estimate such value:

Financial Assets at FVPL and AFS Investments. Market values have been used to determine the fair values of traded government securities and equity shares.

Derivative Assets and Liabilities. The fair values of freestanding and bifurcated forward currency transactions are calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

Cash Bonds. Fair value is estimated as the present value of all future cash flows discounted using the applicable rates for similar types of instruments. Discount rates used in 2006 and 2005 are 5.690% and 9.968%, respectively.

Long-term Debt - Floating Rate. For variable rate loans that reprice every three months, the carrying value approximates the fair value because of recent and regular repricing based on current market rates. For variable rate loans that reprice every six months, the fair value is determined by discounting the principal amount plus the next interest payment using the prevailing market rate for the period up to the next repricing date. Average discount rates used in 2006 and 2005 are 5.142% and 4.411%, respectively.

Other Financial Assets and Liabilities. Due to the short-term nature of the transactions, the fair values of cash and cash equivalents, receivables, short-term loans, liabilities for crude oil and petroleum product importation and accounts payable and accrued expenses approximate the carrying amounts as of balance sheet dates.

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31. **Registration with the BOI**

Petron is registered with the BOI under the New Omnibus Investments Code of 1987 (Executive Order 226) as a pioneer, new producer status of Mixed Xylene. Under the terms of its registration, Petron is subject to certain requirements principally that of producing required metric tons of Mixed Xylene every year.

As a registered enterprise, Petron is entitled to the following benefits on its Mixed Xylene operations:

a. Income Tax Holiday (ITH) for six years from actual start of Mixed Xylene commercial operations (December 1999) until 2005. On May 10, 2005, the BOI approved Petron’s application under Certificate of Registration No. DP98-148, for the one year extension of its ITH incentive. The approved bonus year is for the period December 5, 2005 to December 4, 2006;

b. Tax credits for taxes on duties on raw materials and supplies used for its export products and forming parts thereof; and

c. Simplified custom procedures and others.

In October 2003, the BOI approved Petron’s application under RA No. 8479, otherwise known as the Downstream Oil Industry Deregulation Act (RA No. 8479), for new investments at its Bataan Refinery for an Isomerization Unit and a Gas Oil Hydrotreater (Project). The BOI is extending the following major incentives:

a. ITH for five years without extension or bonus year from January 2005 or actual start of commercial operations, whichever is earlier;

b. Duty of three percent and VAT on imported capital equipment and accompanying spare parts;

c. Exemption from real property tax on production equipment or machinery; and

d. Exemption from contractor’s tax.

Petron has availed of ITH credits amounting to ₱736 in 2006, ₱440 in 2005 and ₱410 in 2004.

On October 20, 2005, Petron registered with the BOI under the Omnibus Investments Code of 1987 (Executive Order 226) as (1) a non-pioneer, new export producer status of Mixed Xylene; (2) a pioneer, new export producer status of Benzene and Toluene; and (3) a pioneer, new domestic producer status of Propylene. Under the terms of its registration, Petron is subject to certain requirements principally that of exporting at least seventy percent (70%) of the production of the mentioned petrochemical products every year except for the produced propylene.

As a registered enterprise, Petron is entitled to the following benefits on its Petrochemical Products (Mixed Xylene, Benzene and Toluene, and Propylene) operations:

a. ITH (1) for four years from May 2008 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Mixed Xylene; (2) for six years from May 2008 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Benzene and Toluene; and (3) for six years from December 2007 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Propylene;

b. Tax credit equivalent to the national internal revenue taxes and duties paid on raw materials and supplies and semi-manufactured products used in producing its export product and forming parts thereof for ten years from start of commercial operations; and

c. Simplification of custom procedures and others.

On October 21, 2005, the BOI approved Petron’s application under RA No. 8479 for new investment at its Bataan Refinery for a Petro Fluid Catalytic Cracking Unit. Subject to Petron’s compliance with the terms and conditions of registration, the BOI is extending the following major incentives:

a. ITH for five years without extension or bonus year from December 2007 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration subject to a 22% ITH rate of exemption;

b. Minimum duty of three percent and VAT on imported capital equipment and accompanying spare parts;

c. Exemption from real property tax on production equipment or machinery; and

d. Exemption from contractor's tax.

In December 2005, the BOI approved Petron's application under RA No. 8479 as an Existing Industry Participant with New Investment in Modernization of the firm's Grease Manufacturing Plant in Pandacan, Manila. The BOI is extending the following major incentives:

a. ITH for a period of five years without extension or bonus year from March 2006 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration subject to base figure of 845 metric tons of grease product representing Petron's highest attained sales volume prior to rehabilitation;

b. Minimum duty of three percent and VAT on imported capital equipment, machinery and accompanying spare parts;

c. Tax credit on domestic capital equipment on locally fabricated capital equipment which is equivalent to the difference between the tariff rate and the three percent duty imposed on the imported counterpart;

d. Exemption from taxes and duties on imported spare parts for consigned equipment with bonded manufacturing warehouse;

e. Exemption from real property tax on production equipment or machinery; and

f. Exemption from contractor's tax.

32. **Segment Information**

The Company's operating businesses are organized and managed according to the nature of the products marketed, with each segment representing a strategic business unit that offers different products and serves different markets.

The Company's major sources of revenues are as follows:

a. Sales from petroleum and other related products which include gasoline, diesel and kerosene offered to motorists and public transport operators through its service station network around the country;

b. Insurance premiums from the business and operation of all kinds of insurance and reinsurance, on sea as well as on land, of properties, goods and merchandise, of transportation or conveyance, against fire, earthquake, marine perils, accidents and all other forms and lines of insurance authorized by law, except life insurance;

c. Lease of acquired real estate properties for petroleum, refining, storage and distribution facilities, gasoline service stations and other related structures;

d. Sales on wholesale or retail and operation of service stations, retail outlets, restaurants, convenience stores and the like; and

e. Export sales of various petroleum products to other Asian countries such as Cambodia, Korea, China and Australia.

The following tables present revenue and income information and certain asset and liability information regarding the business segments for the years ended December 31, 2006, 2005 and 2004. Segment assets and liabilities exclude deferred tax assets and liabilities.

	Petroleum	Insurance	Leasing	Marketing	Elimination	Total
Year Ended December 31, 2006						
Revenue:						
External sales	**₱209,395**	**₱ -**	**₱ -**	**₱2,331**	**₱ -**	**₱211,726**
Inter-segment sales	**1,777**	**542**	**288**	**-**	**(₱2,607)**	**-**
Segment results	**9,101**	**516**	**268**	**78**	**(236)**	**9,727**
Net income	**5,944**	**143**	**37**	**75**	**(181)**	**6,018**
Assets and liabilities:						
Segment assets	**85,421**	**1,541**	**2,507**	**850**	**(2,804)**	**87,515**
Segment liabilities	**53,268**	**353**	**1,924**	**394**	**(2,119)**	**53,820**
Other segment information:						
Property, plant and equipment	**22,193**	**1**	**1**	**467**	**2,491**	**25,153**
Depreciation and amortization	**2,436**	**-**	**-**	**41**	**5**	**2,482**
Year Ended December 31, 2005						
Revenue:						
External sales	190,346	–	–	1,143	–	191,489
Inter-segment sales	882	539	316	–	(1,737)	–
Segment results	9,186	512	303	21	(270)	9,752
Net income	5,765	166	34	29	57	6,051
Assets and liabilities:						
Segment assets	67,185	1,366	2,347	587	(2,602)	68,883
Segment liabilities	39,519	150	1,800	205	(1,919)	39,755
Other segment information:						
Property, plant and equipment	19,797	1	1	429	2,342	22,570
Depreciation and amortization	2,315	–	–	20	–	2,335

(Amounts in Millions, Except Par Value, Share and Per Share Amounts, Exchange Rates and Commodity Volumes)

	Petroleum	Insurance	Leasing	Marketing	Elimination	Total
Year Ended December 31, 2004						
Revenue:						
External sales	147,059	–	–	366	–	147,425
Inter-segment sales	297	531	249	–	(1,077)	–
Segment results	6,627	505	229	–	(211)	7,150
Net income	3,887	158	35	13	8	4,101
Assets and liabilities:						
Segment assets	61,561	1,222	2,231	419	(2,304)	63,129
Segment liabilities	39,285	137	1,674	81	(1,720)	39,457
Other segment information:						
Property, plant and equipment	20,029	2	–	163	2,252	22,446
Depreciation and amortization	1,848	–	–	8	–	1,856

The following tables present additional information on the petroleum business segment of the Company for the years ended December 31, 2006, 2005 and 2004:

	Retail	Lube	Gasul	Industrial	Marketing	Total
Year Ended December 31, 2006						
Revenue	**₱86,155**	**₱1,497**	**₱8,955**	**₱73,553**	**₱41,012**	**₱211,172**
Property, plant and equipment	**4,236**	**573**	**263**	**55**	**17,066**	**22,193**
Capital expenditures	**250**	**-**	**79**	**7**	**4,233**	**4,569**
Year Ended December 31, 2005						
Revenue	82,621	1,537	8,351	68,776	29,943	191,228
Property, plant and equipment	4,450	603	195	52	14,497	19,797
Capital expenditures	327	–	30	–	1,058	1,415
Year Ended December 31, 2004						
Revenue	65,075	1,107	7,650	54,594	18,930	147,356
Property, plant and equipment	4,608	12	206	65	15,255	20,146
Capital expenditures	577	2	37	21	4,996	5,633

Geographical Segments

The following tables present revenue and expenditure and certain asset information regarding the geographical segments of the Company for the years ended December 31, 2006, 2005 and 2004:

	Petroleum	Insurance	Leasing	Marketing	Elimination/ Others	Total
Year Ended December 31, 2006						
Revenue:						
Local	**₱176,891**	**₱495**	**₱288**	**₱2,331**	**(₱2,607)**	**₱177,398**
Export/International	**34,281**	**47**	**-**	**-**	**-**	**34,328**
Year Ended December 31, 2005						
Revenue:						
Local	167,703	465	316	1,143	(1,737)	167,890
Export/International	23,525	74	–	–	–	23,599
Year Ended December 31, 2004						
Revenue:						
Local	134,275	463	249	366	(1,077)	134,276
Export/International	13,081	68	–	–	–	13,149

33. **Other Matters**

a. In 1998, the Company contested before the Court of Tax Appeals (CTA) the collection by the BIR of deficiency excise taxes amounting to ₱1,108 representing back taxes, surcharge and interest arising from the Company's acceptance and use of Tax Credit Certificates (TCCs) worth ₱659 from 1993 to 1997. In July 1999, the CTA ruled that, as a fuel supplier of BOI-registered companies, the Company was a qualified transferee for the TCCs. The CTA ruled that the collection by the BIR of the alleged deficiency excise taxes was contrary to law. The BIR appealed the ruling to the CTA where the case is still pending.

In November 1999, the Department of Finance (DOF) Center ExCom cancelled Tax Debit Memos (TDMs) worth ₱475, the related TCCs and their assignments. The BIR implemented this with a letter of assessment worth ₱651 deficiency taxes (inclusive of interest and charges) for the years 1995 to 1997, as a result of the cancellation. The Company contested on the grounds that the assessment has no factual and legal basis and that the cancellation of the TDMs was void. The Company elevated this protest to the CTA on July 10, 2000. On August 23, 2006, the Second Division of the CTA rendered its decision denying Petron's petition and ordered it to pay the BIR ₱580 representing deficiency excise taxes for 1995 to 1997 plus 20% interest per annum from December 4, 1999. Petron's motion for reconsideration was denied on November 23, 2006. Petron has filed the necessary appeal with the CTA en banc and is awaiting resolution thereon.

In January 2002, the BIR issued another assessment worth ₱739 deficiency taxes (inclusive of interest and charges) for the years 1995 to 1998, as a result of the cancellation of TCCs and TDMs by the DOF Center ExCom. The Company protested this assessment on the same legal grounds used against the tax assessment issued by the BIR in 1999. The Company elevated the protest to the CTA where the case is pending.

In the TCC-related criminal cases, two of which have been filed by the Office of the Ombudsman with the Sandiganbayan and four are currently with the Ombudsman on preliminary investigation, Petron officials are uniformly charged or accused of having conspired with former officials of DOF, One-Stop-Shop Center, BIR and the Bureau of Customs (BOC) and with private individuals to defraud the government by accepting fraudulently issued TCCs and thereafter, by using these TCCs in payment of taxes. Petron officers had acted on or signed the Deeds of Assignment in official capacities. The Company continues to express its full confidence in the integrity of its former and current officers and employees. The Company, therefore, expects that the charges against these Petron officers and employees will be dismissed.

The Company maintains that it has not been involved in the issuance of these TCCs and that it had relied on the approval by the DOF and the BIR with respect to the issuance, the assignment and the use of these TCCs. The Company and its officers maintain that they have not gained any undue advantage in any of the TCC transaction and for each TCC that was duly assigned and accepted the Company issued an equivalent credit note that was used to pay for fuel products of the Company.

Petron officers who were already arraigned in the first Sandiganbayan case went up to the Supreme Court (SC) after the Sandiganbayan reversed an earlier ruling dismissing the case for failure on the part of the Ombudsman to prosecute. The second Sandiganbayan case remains pending.

b. Petron has unused letters of credit totaling approximately ₱257 as of December 31, 2006 and ₱30 as of December 31, 2005.

c. Implementation of RA No. 8749, "Philippine Clean Air Act of 1999"

Petron has been fully complying with the Clean Air Act (CAA) since the law was implemented. It introduced its low-sulfur "Diesel Max" to the market three months ahead of the CAA-mandated schedule. Under the CAA law, oil firms are mandated to lower the sulfur content of ADO to 0.05% by January 1, 2004 nationwide.

Beyond CAA compliance, Petron is the only oil company that has invested substantial resources to upgrade its production capabilities to meet CAA specifications. In January 2005, it commissioned its Isomerization Unit that will enable the Company to produce isomerates for blending with gasoline to meet current specifications. The unit is part of the ₱5,000 refinery project that also includes a Gas Oil Hydrotreater that was commissioned in April 2005. With these two units, Petron is the only oil company that can serve the local market's demand for CAA-compliant fuels entirely from local production.

d. Pandacan Terminal Operations

The City Council of Manila (City Council), citing concerns of safety, security and health, passed City Ordinance No. 8027 (Ordinance No. 8027) reclassifying the areas occupied by the oil terminals of Petron, Shell and Chevron (formerly Caltex) from industrial to commercial, making the operation of the terminals therein unlawful.

In an effort to address the concerns of the City Council, the oil companies implemented a Scale Down Program to reduce tankage capacities, create buffer zones and consolidate operation of their facilities. The Petron Linear Park was inaugurated on December 17, 2003. This serves as additional safety and security buffer zone, further enhancing the safety of the facilities.

Of the 28 tanks that were committed to be dismantled under the Memorandum of Understanding signed between the three oil companies, the Department of Energy and the City of Manila, 26 have been decommissioned/dismantled. The dismantling of the remaining two tanks is contingent upon full integration of the Pandacan Terminal Operations.

To date, the first phase of the engineering, procurement and construction is already more than 98% complete. On the other hand, the second phase of the engineering, procurement and construction is 40% complete.

The Joint Venture (PDSI) took over the operations of the "scaled-down" facilities on November 1, 2004 after the City of Manila issued the business permit applied for.

Simultaneous with the Scale Down Program, the case of Social Justice Society vs. Atienza (SJS vs. Atienza case) was filed on December 31, 2002. In April 2003, subsequent to the filing of the SJS vs. Atienza case, Petron, Shell and Chevron filed separate cases before the RTC questioning the constitutionality and validity of Ordinance No. 8027. Shell and Chevron were able to secure TRO and, after further proceedings, writs of preliminary injunction against the City of Manila and/or its officials from implementing Ordinance No. 8027. The separate cases of Shell and Chevron remain pending to date and the writ of injunction continue in effect. On the other hand, Petron was able to secure a status quo Order from the RTC, following an agreement between Petron and the City of Manila to maintain the status quo Order until further orders of the Court or termination of the case. The case was referred to mediation before the Philippine Mediation Center but the parties failed to come to any agreement.

During the pendency of the above-cited cases, on March 16, 2006, the City Council passed City Ordinance No. 8119 (Ordinance No. 8119) adopting the Comprehensive Land Use Plan and Zoning Regulations of 2006 in which, the area of the Pandacan Oil Terminals was reclassified as high density residential/mixed zone use, and at the same time gave non-conforming establishments seven years from effectivity of the Ordinance No. 8119 to relocate. Shell and Chevron filed a Complaint against the City of Manila questioning the validity and constitutionality of Ordinance No. 8119 and is currently being heard for presentation of evidence by Shell and Chevron. Petron has filed its own Complaint questioning Ordinance No. 8119 before the RTC and Petron has been able to secure a TRO preventing the City of Manila from enforcing Ordinance No. 8119.

As a result of the passage of Ordinance No. 8119, on February 20, 2007, Petron, Mayor of Manila and the City Council filed a Joint Motion to Withdraw Complaint and Counterclaims in the case filed by Petron questioning Ordinance No. 8027, citing that Ordinance No. 8119 repealed Ordinance No. 8027, for which reason, the case filed by Petron before the RTC has been rendered questionable.

On March 7, 2007, the SC rendered a decision in the SJS vs. Atienza case, directing the Mayor of Manila to immediately enforce Ordinance No. 8027. It is Petron's position that the SC failed to consider supervening events, notably (i) the passage of Ordinance No. 8119 which supersedes Ordinance No. 8027, as well as (ii) the writs of injunction from the RTC presenting the implementation of Ordinance No. 8027. On March 12, 2007, Petron, together with Shell and Chevron, filed an Urgent Motion for Leave Intervention and Urgent Motion to Admit Motion for Reconsideration of the decision dated March 7, 2007, citing the foregoing grounds that make the SC's decision and the enforcement of Ordinance No. 8027 improper. Further, Petron, Shell and Chevron noted the ill-effects of the sudden closure of the Pandacan Oil Terminals on the entire country.

On March 22, 2007, the Department of Energy, through its counsel, the Office of the Solicitor General, filed a motion for the governments to intervene, in support of the oil companies' position. On March 23, 2007, Petron received an order from the SC ordering the parties to file their comments within five days from receipt of the order and setting the same for oral arguments. This order, in effect, stayed any action by the City of Manila.

The Company is in the process of finalizing the study of various alternatives. As of April 3, 2007, an estimate of the potential impact cannot be made.

e. Navotas Business Tax

In the case of Petron vs. Mayor Tobias Tiangco concerning the imposition of business tax for the sale of diesel at the Navotas Bulk Plant, the TRO issued by the SC is still in effect and will prevent the closure of the Bulk Plant until the case is decided by the SC.

f. Oil Spill Incident in Guimaras

M/T Solar I sank in rough seas in the afternoon of August 11, 2006 en route to Zamboanga, loaded with about 2 million liters of industrial fuel oil. It now lies about 640 meters beneath the sea, at approximately 13 nautical miles southwest of Guimaras.

Petron immediately dispatched its oil spill gear, equipment and oil spill teams upon receiving information of the incident. An aerial and surface assessment was conducted to determine the extent of the oil spill.

Inspection by the Survey Ship Shinsei Maru (Shinsei Maru), using a remote-operated vehicle (ROV), found the vessel upright and in stable condition with minimal traces of leakage. All cargo compartment valves were tightened by the ROV to ensure against further leakage. The Shinsei Maru was contracted by the Protection and Indemnity (P & I) Club and the International Oil Pollution Compensation (IOPC) from Fukada Salvage & Marine Works Co. Ltd.

On separate investigations conducted by the Special Task Force on Guimaras by the Department of Justice (DOJ) and the Special Board of Marine Inquiry (SBMI), both found the owners of M/T Solar I, Sunshine Marine Development Corporation (SMDC), liable. The DOJ found no criminal liability on the part of Petron. However, the SBMI found Petron to have overloaded the vessel. Petron has appealed the findings of the SBMI to the Department of Transportation and Communication and is awaiting its resolution.

On September 18, 2006, the Mayor of Nueva Valencia, Guimaras filed a criminal complaint before the Fiscal's Office in Guimaras against Petron officers and the President of SMDC for violation of environmental laws. A resolution was issued by the public prosecutor dismissing the criminal complaint on all counts. A Motion for Reconsideration was filed by the counsel for Guimaras Municipality last April 4, 2007; on the other hand, the counsel for Petron filed opposition to the Motion for Reconsideration. The Company is awaiting resolution on this incident.

The Company implemented a "Cash for Work" program involving residents of the affected areas in the clean-up operations, providing them with a daily allowance. The Company also mobilized its employees to assist in the operations. By the middle of November 2006, Petron had cleaned up all affected shorelines and was affirmed by the inspections made by Task Force Solar I Oil Spill (SOS), a multi-agency group composed of officials from the Local Government Units, Department of Health, Department of Environment and Natural Resources, Department of Social Welfare and Development (DSWD), and the Philippine Coast Guard.

The Company collected a total of 6,000 metric tons of debris which were brought to the Holcim Cement facility in Lugait, Misamis Occidental for processing/treatment of waste. On November 20, 2006, one of the last barge shipments of oil debris unfortunately sank en route to the same plant.

The Company is working closely with the provincial government, DSWD, Department of Agriculture, Technical Education and Skills Development Authority and the Philippine Business for Social Progress in developing livelihood programs for the locals. Last November 27, 2006, Petron held a scientific conference in cooperation with the University of the Philippines - Visayas, the National Disaster Coordinating Council, the World Wildlife Fund and the Guimaras Provincial Government with the objective of developing an integrated assessment and protocol for the rehabilitation of the province. The Company has also replicated its own educational programs in partnership with the Department of Education. Ground breaking ceremonies for the construction of a four-classroom school in Barangay Tando, Nueva Valencia and a Library Hub in Barangay San Miguel, Jordan, Guimaras was held last March 15, 2007. The two facilities are expected to be open in time for the next school year.

With regard to the retrieval of the remaining oil still trapped in M/T Solar I, the P & I Club contracted a sub-sea systems technology provider (Sonsub) to recover the oil from the sunken vessel. The recovery vessel, Allied Shield, arrived at Bacolod Real Estate Development Corporation Pier in Bacolod City last March 10, 2007. After unloading the ISO-certified tanks and hoses, the vessel proceeded to the site in March 11, 2007. Oil recovery operation was technically completed on April 1, 2007. A total of 9,000 liters of oil was recovered.

Representatives from the IOPC met with the claimants from various affected areas of Guimaras to give an orientation on the requirements of the claim as well as the documents required to be submitted in support of the claim. Petron has filed a total of ₱188 against the IOPC. As of January 2007, a total of ₱105 has been paid to Petron. Payment of claims for Guimaras fishermen were completed in March 2007. Release of checks for Iloilo claimants will start on the second week of April 2007.

Total expenses incurred as of December 31, 2006 amounted to ₱122, net of reimbursements from IOPC amounting to ₱105 (see Note 18).

LIST OF BANKS AND FINANCIAL INSTITUTIONS

ABN AMRO Bank
Allied Banking Corporation
Arab Petroleum Investments
Australia and New Zealand Banking Group, Ltd.
Ayala Life Assurance, Inc.
Banco de Oro
Bank of Butterfield
Bank of China
Bank of the Philippine Islands
Banque Saudi Fransi
BDO Private Bank
BNP Paribas
BPI Capital Corporation
Calyon Corporate and Investment Bank
Cathay United Bank
China Banking Corporation
Chinatrust Commercial Bank Corporation
CIMB Bank Berhad
Citibank, N. A.
Citicorp International Limited
Deutsche Bank
Development Bank of the Philippines
DZ Bank AG
Equitable PCI Bank
ING Bank N. V., Manila Branch
Insular Life Assurance Co.
JP Morgan Chase Bank, N.A.
Land Bank of the Philippines
Mega International Commercial Bank Co., Ltd.
Metropolitan Bank and Trust Company
Mizuho Corporate Bank, Ltd.
Norddeutsche Landesbank Girozentrale, Singapore
PCI Capital Corporation
Philippine National Bank
Pioneer Life, Inc.
Rizal Commercial Banking Corporation
Robinsons Savings Bank
Samba Financial Group
SB Capital Investment Corporation
Schroders (Bermuda), Ltd.
Security Bank Corporation
Societe Generale
Standard Chartered Bank
The Bank of Bermuda, Ltd.
The Bank of Tokyo-Mitsubishi UFJ, Ltd.
The Hongkong and Shanghai Banking Corporation, Ltd.
The Saudi Investment Bank
Union Bank of the Philippines
United Coconut Planters Bank

Board of DIRECTORS

Nicasio I. Alcantara, 64 years old, has been an Executive Director and the Chairman of Petron Corporation since July 30, 2001. At present, he is also the Chief Executive Officer. Prior to joining Petron, he was Chairman/President of various corporations of the Alcantara Group of Companies.

Khalid D. Al-Faddagh, 51 years old, has been a Director since July 2001 and the President of Petron since July 2003. He was the company's Chief Executive Officer from July 2004-2006. He has over 20 years of experience in various professional and management positions in Saudi Aramco.

Abdullah O. Al-Baiz, 49 years old, has been a Director since February 2007. Mr. Al-Baiz has had 15 years of experience in the management and technical field of the oil industry. His most recent position prior to joining Petron was as Saudi Aramco's New Business Evaluation Department Manager.

Basil A. Abul-Hamayel, 43 years old, has been a Director of the company since July 2004 and currently a member of the Board Audit Committee. He has 24 years of service with Saudi Aramco. Currently, he is the manager of Corporate Finance, Insurance and Asset Management Department of Saudi Aramco. Prior to this position, Mr. Abul-Hamayel was Petron's Vice President for Corporate Planning.

Herminio S. Aquino, 57 years old, has been a Director of the company since November 2004 and currently a member of the Board Audit Committee. He is also the Chairman of Trackworks, Inc., Interconsult (Asia Pacific), Inc. and 7-Series, Inc.

NICASIO I. ALCANTARA
Chairman & Chief Executive Officer

KHALID D. AL-FADDAGH
President

ABDULLAH O. AL-BAIZ
Director

BASIL A. ABUL-HAMAYEL
Director

HERMINIO S. AQUINO
Director

ALBERTO A. PEDROSA
Director

KHALID G. AL-BUAINAIN
Director

BERNARDINO R. ABES
Director

DOUHAN H. AL-DOUHAN
Director

EMILIA T. BONCODIN
Director

Alberto A. Pedrosa, 74 years old, was elected Director of the company in March 2005. He is currently the Chairman and Publisher of Republika, a news magazine focused on the 42,000 barangays in the country. Mr. Pedrosa was a former Ambassador Extraordinary and Plenipotentiary to Belgium, Luxembourg and the European Union from 1992 to 1995.

Khalid G. Al-Buainain, 48 years old, has been a non-executive Director of the company since July 2003. Currently the Vice President for Refining of Saudi Aramco since June 2003, the Chairman of Luberef and a member of the Saudi Aramco Executive Advisory Committee.

Bernardino R. Abes, 76 years old, has been a non-executive Director of the company since July 2001. He is currently the Chairman of the Government Service Insurance System, following a three-year term as Chairman of the Social Security Commission.

Douhan H. Al-Douhan, 71 years old, has been an Independent Director since July 2001. He has been the Managing Director of Randa Trading & Construction in Saudi Arabia since 2004.

Emilia T. Boncodin, 52 years old, has been an Independent Director since April 2006. She is currently a Professor at the National College of Public Administration and Governance of the University of Philippines. She was the Secretary of the Department of Budget and Management from January 2001 to July 2005 and in February to June 1998.

Management COMMITTEE

NICASIO I. ALCANTARA
Chairman and Chief Executive Officer

KHALID D. AL-FADDAGH
President

JOSE JESUS G. LAUREL
Vice President for Legal and External Affairs

ANTONIO G. PELAYO
Vice President for Finance and Subsidiaries

ALFRED A. TRIO
Vice President for Refinery

SULAIMAN M. ABABTAIN
Vice President for Corporate Planning

FELIMON E. ANTIPORTA
Vice President for Supply and Operations

JOSE K. CAMPOS, JR.
Vice President for Marketing

MA. CONCEPCION F. DE CLARO
Controller

ROSARIO R. EIJANSANTOS
Treasurer

LUIS A. MAGLAYA
Corporate Secretary

DEPOTS AND TERMINALS

LUZON

APARRI
J.P. de Carreon St. Punta
Aparri, Cagayan
(078) 888-2456/888-2071

BATANGAS
Bo. Mainaga, Mabini, Batangas
(043) 487-0418/487-0377
(043) 487-0419 (Fax)

CALAPAN
Roxas St. Brgy. Ilaya
Calapan City, Oriental Mindoro
(043) 288-1779

LIMAY
Petron Bataan Refinery
Limay, Bataan
(02) 886-3187-96 loc. 390-394

NAVOTAS
PFDA Compound
Navotas, Metro Manila
(02) 281-4826/281-1297

PALAWAN
Parola, Brgy. Maunlad
Puerto Princesa City, Palawan
(048) 433-2682/433-3329

PANDACAN
Jesus St., Pandacan, Manila

Order & Billing
(02) 563-8491 to 95

Dispatching
(02) 563-3047/563-8521 loc. 223

PASACAO
Brgy. Camangi
Pasacao, Camarines Sur
(054) 513-9258/513-9175
(054) 513-9175 (Fax)

PORO
Poro Pt.
San Fernando, La Union
(072) 242-6032 to 34

ROSARIO
Gen. Trias, Rosario, Cavite
(046) 438-2860/438-1996

SAN JOSE
1020 A. Mabini St.
San Jose, Occidental Mindoro
(043) 491-1938

VISAYAS

AMLAN
Tandayag, Amlan, Negros Oriental
(035) 527-0790/417-0793/417-0795

BACOLOD
Bo. San Patricio
Bacolod City, Negros Occidental
(034) 433-9690/433-9687 to 89

ILOILO
Lapuz, Iloilo City
(033) 337-6895/338-1893

ISABEL
Lide, Isabel, Leyte
(053) 556-0177/337-2289

MACTAN
MEPZ, Lapu-lapu City
(032) 340-4620/340-4629

MANDAUE
Looc, Mandaue City, Cebu
(032) 346-5135/344-7341 to 51

ORMOC
Bo. Linao
Ormoc City, Leyte
(053) 255-9070/561-1239

ROXAS
Arnaldo Blvd. Culasi, Roxas City
(036) 621-1992/621-0722

TACLOBAN
Anibong, Tacloban City
(053) 325-6432 to 33
(053) 523-1686

TAGBILARAN
Graham Ave., Tagbilaran, Bohol
(038) 411-3397

MINDANAO

BAWING
Purok Cabu
Bawing, General Santos City
(083) 380-7725 to 26

DAVAO
Km. 9, Bo. Pampanga
Davao City
(082) 234-2185/233-0399

GENERAL SANTOS
P. Acharon Blvd.
Bula, Gen. Santos City
(083) 553-4923

ILIGAN
Bo. Tuminobo
Iligan City, Lanao del Norte
(063) 492-0653/351-6704/221-5264

JIMENEZ
Jimenez, Misamis Occidental
(088) 272-3230/272-3243

NASIPIT
Talisay, Nasipit, Agusan del Norte
(085) 283-3126/343-2218/19

TAGOLOAN
Tagoloan, Misamis Oriental
(08822) 740-072/740-263

ZAMBOANGA
Bgy. Campo Islam
Lower Calarian, Zamboanga City
(062) 991-1245/991-1571/991-4352

AIRPORT INSTALLATIONS

DAVAO
Davao Airport
(082) 234-2185/86/233-0399

ILOILO
Petron ITP Aviation
Brgy. Airport, Mandurriao, Iloilo City
(033)321-3183

LAOAG
Laoag Airport
c/o NAIA 833-7084

NAIA
JOCASP, CPD, NAIA, Pasay City
(02) 833-7084/831-5842

LPG OPERATIONS

GASUL-PASIG
Bo. Ugong, Pasig, Metro Manila
(02) 671-2687 (DL)/671-9817(TL)

GASUL-SAN FERNANDO
San Fernando, Pampanga
(045) 961-3564

LEGASPI
Lakandula Drive
Bgy. Bonot, Legaspi City
(052) 480-8113

CALAMBA WAREHOUSE
Calamba, Laguna
(049) 545-6481

PRODUCTS

FUELS

Automotive Fuels
Blaze
Petron XCS-Complete
Combustion System
Xtra Unleaded
Regular Unleaded
Diesel Max
Xtend Autogas

Industrial Fuels
Petron Fuel Oil
IF-1
LSFO
Intermediate Fuels
Special Fuel Oil
Industrial Diesel Fuel

Aviation Fuels
Aviation Gasoline
Jet A- I

Household Fuels
Gasul
Gaas

AUTOMOTIVE LUBRICATING OILS

Diesel Engine Oils
Rev-X All Terrain
Rev-X Trekker
Rev-X Hauler
Rev-X HD
Petron HDX
Petron XD3
Petron XD 2040
Petron 2040
Petron Railroad Extra

Gasoline Engine Oils
Ultron Race
Ultron Rallye
Ultron Touring
Ultron Extra
Petron MO

Motorcycle Oils
Petron Sprint 4T
2T Premium
2T Enviro
2T Autolube
2T Powerburn

Automotive Gear Oils
Petron GX
Petron GEP
Petron GST

Automotive Transmission Fluids
Petron ATF Premium
Petron TF 38
Petron TDH 50

INDUSTRIAL LUBRICATING OILS

Turbine, Hydraulic and Circulating Oils
Hydrotur AWX
Hydrotur AW
Hydrotur AW (GT)
Hydrotur EP 46
Hydrotur N 100
Hydrotur R
Hydrotur SX 32
Hydrotur SX 68
Hydrotur SX 220
Hydrotur T
Hydrotur TEP

Industrial Gear Oils
Hypex EP (Oil-Based)
Hypex EP (Asphalt-Based)
Milrol 5K
Gearfluid
Gearkote

Cutting Oils
Turnol
Petrokut 10
Petrokut 27

Refrigeration Oils
Zerflo 68
Suniso

Other Industrial Lubricating Oils
Petrocyl S
Petrocyl
Airlube
Spinol 15
Spinol 10E
Petrosine 68
Voltran 60

MARINE LUBRICATING OILS

Marine Cylinder Oils
Petromar DCL 7050
Petromar DCL 4000 Series

Marine Trunk Piston Engine Oils
Petromar XC 5540
Petromar XC 5040
Petromar XC 4040
Petromar XC 3000 Series
Petromar XC 2000 Series
Petromar XC 1500 Series
Petromar XC 1000 Series

Other Marine Lubricants
Petromar 65
Petromar HD Marine Series

GREASES

Regular Performance Greases
Petrogrease MP
Petrogrease XX

Premium Performance Greases
Molygrease EP2
Molygrease Premium
Petrogrease EP
Petrogrease Premium

High Temperature Greases
Molygrease EP 1P and EP 2P
Petrogrease EP 290 and
EP 375
Petrogrease HT

Complex Greases
Petrogrease Aluminum
Complex
Petrogrease Lithium
Complex
Petrogrease Lithium
Complex with Moly

Food Grade Greases
Petrogrease Food Grade

ASPHALTS

Penetration Asphalt
Petropen

Cutback Asphalt
Petropen CB

Emulsified Asphalt
Petromul CSS -1

Blown Asphalts
Asphaltseal
Asphalt Joint Sealer

SPECIAL PRODUCTS

Process Oils
Process Oils
Product 50 R
Printsol 600
Rubbex 130
Stemol
Jute Batching Oil
Aldro Oil

Heat Transfer Oil
Petrotherm 32

Cleaning Agent
Greasolve
Carbon Flush

Flushing Oil
STM

Sealing Lubricant
Dust Stop Oil

Protective Coatings
Petrokote 500
Petrokote 392
Marinekote
Marinekote SS
Autokote
Cablelube
Cablekote

Others
Petron Farm Trac Oil
Petron Marine HD Oil
Bull's Eye

AFTERMARKET SPECIALTIES

PetroMate Specialties
PetroMate Oil Saver
PetroMate Oil Improver
PetroMate Gas Saver
PetroMate Diesel Power
Booster
PetroMate Engine Flush
PetroMate Super Coolant
PetroMate Clean N' Shine
PetroMate Penetrating Oil
PetroMate Greaseaway
PetroMate Brake and Clutch
Fluid

AVIATION LUBRICANTS

Braycote 622
Nyco Grease GN 22
Hydraunycoil FH 51
Royco 481
Aviation Oil EE
Invarol FJ 13
Exxon Turbo Oil 2389
Exxon Turbo Oil 2380
Univis J-13
Turbonycoil 35 M

INFORMATION AND ASSISTANCE

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E-mail: contactus@petron.com

Shareholder Services and Assistance
For questions or comments regarding dividend payments, change of address, account status, lost or damaged stock certificates, please get in touch with:

Stockholder Services Section
Public Affairs Department
39/F Petron MegaPlaza
358 Sen. Gil Puyat Avenue
Makati City 1200 Philippines
Tel. No. (632) 886-3888
Fax No. (632) 886-3064

Or with our stock transfer agent:

Stock Transfer Service, Inc.
8/F Phinma Plaza
39 Plaza Drive, Rockwell Center
Makati City 1200 Philippines
Tel. No. (632) 898-7555
Fax No. (632) 898-7597

Institutional Investor Inquiries
Petron Corporation welcomes inquiries from analysts, the financial community and institutional investors. Please write or call:

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Annual reports, quarterly reports and other information on Petron can be downloaded from our website: **www.petron.com**.

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