

PHILIPPINE LONG DISTANCE TELEPHONE CO

Form 6-K

November 06, 2007

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 6 -K**

**Report of Foreign Private Issuer**

**Pursuant to Rule 13a-16 or 15d-16  
of the Securities Exchange Act of 1934**

**For the month of November 2007**

**Commission File Number 1-03006**

**Philippine Long Distance Telephone Company**

(Exact Name of Registrant as specified in its Charter)

**Ramon Cojuangco Building**

**Makati Avenue**

**Makati City**

**Philippines**

(Address of principal executive offices)

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(Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.)

Form 20-F:  Form 40-F:

(Indicate by check mark whether by furnishing the information contained in this form, the registrant is also thereby furnishing the information to the commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act 1934.)

Yes:  No:

(If  Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b):  
82-\_\_\_\_\_)

EXHIBITS

Exhibit Number		Page
1.1	Announcement date November 6, 2007	
	Management's Discussion and Analysis of Financial Condition and Results of Operations	45
	Consolidated Financial Statements as at September 30, 2007 (unaudited) and December 31, 2006 (audited) and for the nine months ended September 30, 2007 and 2006 (unaudited)	94

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIPPINE LONG DISTANCE TELEPHONE COMPANY

By: /s/Ma. Lourdes C. Rausa-Chan  
Ma. Lourdes C. Rausa-chan  
Senior Vice President, Corporate Affairs and Legal Services Head and Corporate Secretary

**Date:** November 6, 2007

SEC Number **PW-55**  
File Number

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**PHILIPPINE LONG DISTANCE  
TELEPHONE COMPANY**

---

(Company's Full Name)

**Ramon Cojuangco Building  
Makati Avenue, Makati City**

---

(Company's Address)

**(632) 816-8556**

---

(Telephone Number)

**Not Applicable**

---

(Fiscal Year Ending)

(month & day)

**SEC Form 17-Q**

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Form Type

**Not Applicable**

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Amendment Designation (if applicable)

**September 30, 2007**

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Period Ended Date

**Not Applicable**

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(Secondary License Type and File Number)

November 6, 2007

Securities & Exchange Commission  
Money Market Operations Department  
SEC Building, EDSA  
Mandaluyong City

Attention: Director Justina Callangan

Corporations Finance Department

Gentlemen:

In accordance with Section 17.1(b) of the Securities Regulation Code and SRC Rule 17.1, we submit herewith five (5) copies of SEC Form 17-Q with Management's Discussion and Analysis and accompanying unaudited financial statements of the Company for the nine (9) months ended September 30, 2007.

Very truly yours,

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY**

/s/Ma. Lourdes C. Rausa-Chan

**MA. LOURDES C. RAUSA-CHAN**

Corporate Secretary





COVER SHEET

P	W	-	5	5
S.E.C. Registration No.				

PHILIPPINE LONG DISTANCE

TELEPHONE COMPANY

(Company's Full Name)

RAMON C OJUANGCO BLDG.

MAKATI AVE. MAKATI CITY

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

ATTY. MA. LOURDES C. RAUSA-CHAN	816-8405
<b>Contact Person</b>	<b>Company Telephone Number</b>

1	2	3	1	SEC FORM 17-Q	0	6	Every 2nd Tuesday
Month		Day		FORM TYPE	Month		Day
				Annual Meeting			



SECURITIES AND EXCHANGE COMMISSION

**SEC FORM 17-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 17  
OF THE SECURITIES REGULATION CODE ( SRC ) AND**

**SRC 17 (2) (b) THEREUNDER**

1. For the quarterly period ended September 30, 2007

-

2. SEC Identification Number PW-55 3. BIR Tax Identification No. 000-488-793

4. Philippine Long Distance Telephone Company

Exact name of registrant as specified in its charter

5. Republic of the Philippines

Province, country or other jurisdiction of incorporation or organization

6. Industry Classification Code: (SEC Use Only)

7. Ramon Cojuangco Building, Makati Avenue, Makati City 0721

Address of registrant's principal office Postal Code

8. (632) 816-8556

Registrant's telephone number, including area code

9. Not Applicable

Former name, former address, and former fiscal year, if changed since last report

10. Securities registered pursuant to Sections 8 of the SRC

Title of Each Class Number of Shares of Common Stock Outstanding

-

Common Capital Stock, Php5 par value 188,708,152 shares as of September 30, 2007

-

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

Yes  No

12. Check whether the registrant

(a) has filed all reports required to be filed by Section 17 of the SRC during the preceding ten months (or for such shorter period that the registrant was required to file such reports):

Yes  No

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

Yes  No

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

*Our financial statements as at September 30, 2007 (unaudited) and December 31, 2006 (audited) and for the nine months ended September 30, 2007 and 2006 (unaudited) and related notes (pages F-1 to F-95) are filed as part of this report on Form 17-Q.*

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*In the following discussion and analysis of our financial condition and results of operations, unless the context indicates or otherwise requires, references to we, us, our or PLDT Group mean the Philippine Long Distance Telephone Company and its consolidated subsidiaries, and references to PLDT mean the Philippine Long Distance Telephone Company, not including its consolidated subsidiaries (see Note 2 Summary of Significant Accounting Policies and Practices to the accompanying unaudited consolidated financial statements for a list of these subsidiaries, including a description of their respective principal business activities).*

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying unaudited consolidated financial statements and the related notes. Our unaudited consolidated financial statements, and the financial information discussed below, have been prepared in accordance with Philippine Financial Reporting Standards, which differ in certain significant respects from generally accepted accounting principles in the United States.*

*The financial information appearing in this report and in the accompanying unaudited consolidated financial statements is stated in Philippine pesos. All references to pesos, Philippine pesos or Php are to the lawful currency of the Philippines; all references to U.S. dollars, US\$ or dollars are to the lawful currency of the United States; all references to Japanese yen, JP¥ or ¥ are to the lawful currency of Japan and all references to Euro or € are to the lawful currency of the European Union. Translations of Philippine peso amounts into U.S. dollars in this report and in the accompanying unaudited consolidated financial statements were made based on the exchange rate of Php44.974 to US\$1.00, the volume weighted average exchange rate at September 30, 2007 quoted through the Philippine Dealing System.*

*Some information in this report may contain forward-looking statements within the meaning of Section 27A of the U.S. Securities Act of 1933 and Section 21E of the U.S. Securities Exchange Act of 1934. We have based these*

*forward-looking statements on our current beliefs, expectations and intentions as to facts, actions and events that will or may occur in the future. Such statements generally are identified by forward-looking words such as believe, plan, anticipate, continue, estimate, expect, may, will or other similar words.*

*A forward-looking statement may include a statement of the assumptions or bases underlying the forward-looking statement. We have chosen these assumptions or bases in good faith, and we believe that they are reasonable in all material respects. However, we caution you that forward-looking statements and assumed facts or bases almost always vary from actual results, and the differences between the results implied by the forward-looking statements and assumed facts or bases and actual results can be material, depending on the circumstances. When considering forward-looking statements, you should keep in mind the description of risks and cautionary statements in this report. You should also keep in mind that any forward-looking statement made by us in this report or elsewhere speaks only as at the date on which we made it. New risks and uncertainties come up from time to time, and it is impossible for us to predict these events or how they may affect us. We have no duty to, and do not intend to, update or revise the forward-looking statements in this report after the date hereof. In light of these risks and uncertainties, any forward-looking statement made in this report or elsewhere might not occur.*



**Financial Highlights and Key Performance Indicators**

	<b>September 30, 2007</b>	<b>December 31, 2006</b>	<b>Decrease</b>	
			<b>Amount</b>	<b>%</b>

(in millions, except for operational data, exchange rates and earnings per common share) (Unaudited) (Audited)

**Consolidated Balance Sheets**

Total assets	Php227,971	Php241,892	(Php13,921)	(6)
Property, plant and equipment net	159,288	164,190	(4,902)	(3)
Cash and cash equivalents and short-term investments	19,993	25,197	(5,204)	(21)
Total equity	103,692	104,523	(831)	(1)
Notes payable and long-term debt	64,725	80,154	(15,429)	(19)
Net debt(1) to equity ratio	0.43x	0.53x		

	<b>Nine Months Ended</b>		<b>Increase (Decrease)</b>	
	<b>September 30, 2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>

(Unaudited)

**Consolidated Statements of Income**

Revenues and other income	Php103,468	Php95,400	Php8,068	8
Expenses	63,488	65,902	(2,414)	(4)
Income before income tax	39,980	29,498	10,482	36
Net income	26,952	26,367	585	2
Net income attributable to equity holders of PLDT	26,506	25,744	762	3
Net income margin	26%	27%		
Earnings per common share basic	138.71	138.71		

**Consolidated Statements of Cash Flows**

Net cash provided by operating activities	55,499	56,146	(647)	(1)
Net cash used in investing activities	19,557	25,261	(5,704)	(23)
Capital expenditures	14,529	16,872	(2,343)	(14)
Net cash used in financing activities	43,980	41,763	2,217	5

**Operational Data**

Number of cellular subscribers	28,260,095	22,929,431	5,330,664	23
Number of fixed line subscribers	1,751,468	1,747,357	4,111	
Number of broadband subscribers	501,250	219,601	281,649	128
<i>Fixed Line</i>	229,534	118,679	110,855	93
<i>Wireless</i>	271,716	100,922	170,794	169
Number of employees	26,135	26,610	(475)	(2)
<i>Fixed Line</i>	8,057	9,110	(1,053)	(12)
<i>Wireless</i>	5,345	5,328	17	
<i>Information and Communications Technology</i>	12,733	12,172	561	5

Exchange Rates    Php per US\$

September 30, 2007	Php44.974
December 31, 2006	49.045
September 30, 2006	50.249
December 31, 2005	53.062

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(1) *Net debt is derived by deducting cash and cash equivalents and short-term investments from total debt (notes payable and long-term debt).*

## Overview

We are the largest and most diversified telecommunications company in the Philippines. We have organized our business into three main segments:

- *Wireless* wireless telecommunications services provided by Smart Communications, Inc., or Smart, and Pilipino Telephone Corporation, or Piltel, our cellular service providers; Smart Broadband, Inc., or Smart Broadband, our wireless broadband provider; Wolfpac Mobile, Inc., or Wolfpac, our wireless content operator; Mabuhay Satellite Corporation, or Mabuhay Satellite, ACeS Philippines Cellular Satellite Corporation, or ACeS Philippines, and Telesat, Inc., or Telesat, our satellite and very small aperture terminal, or VSAT, operators;
- *Fixed Line* fixed line telecommunications services are primarily provided through PLDT. We also provide fixed line services through PLDT's subsidiaries PLDT Clark Telecom, Inc., Subic Telecommunications Company, Inc., PLDT-Maratel, Inc., Piltel, PLDT Global Corporation, or PLDT Global, Smart-NTT Multimedia, Inc. and Bonifacio Communications Corporation, which together account for approximately 3% of our consolidated fixed line subscribers; and
- *Information and Communications Technology, or ICT* information and communications infrastructure and services for internet applications, internet protocol, or IP-based solutions and multimedia content delivery provided by PLDT's subsidiary ePLDT, Inc., or ePLDT; business process outsourcing, or BPO, provided by SPi Technologies, Inc. and its subsidiaries, or SPi Group (consolidated on July 11, 2006); call center services provided under the umbrella brand name *ePLDT Ventus*, include ePLDT Ventus, Inc., or Ventus, Parlance Systems, Inc., or Parlance, and Vocativ Systems, Inc., or Vocativ; internet access and online gaming services provided by ePLDT's subsidiaries, Infocom Technologies, Inc., or Infocom, Digital Paradise, Inc., or Digital Paradise, Digital Paradise Thailand, Ltd., or Digital Paradise Thailand, netGames, Inc., or netGames, Airborne Access Corporation, or Airborne Access and Level Up!, Inc., or Level Up!; and e-commerce, and IT-related services provided by other investees of ePLDT, as discussed in *Note 9 Investments in Associates* to the accompanying unaudited consolidated financial statements.

We registered total revenues and other income of Php103,468 million in the first nine months of 2007, an increase of Php8,068 million, or 8%, as compared to Php95,400 million in the same period in 2006 primarily due to an increase in our service revenues by Php8,467 million largely from our wireless business.

Expenses decreased by Php2,414 million, or 4%, to Php63,488 million in the first nine months of 2007 from Php65,902 million in the same period in 2006, largely resulting from decreases in depreciation and amortization, and financing costs partly offset by higher compensation and benefits, professional and other contracted services, and taxes and licenses.

Net income attributable to equity holders of PLDT increased by Php762 million, or 3%, to Php26,506 million in the first nine months of 2007 from Php25,744 million in the same period in 2006. However, despite the increase in our net income in 2007, our basic earnings per common share in the first nine months of 2007 and 2006 resulted in the same amount of Php138.71 due to the corresponding increase in the weighted average number of common shares outstanding from 183.1 million in the first nine months of 2006 to 188.6 million in the same period in 2007.

## Results of Operations

The table below shows the contribution by each of our business segments to our revenues and other income, expenses and net income for the nine months ended September 30, 2007 and 2006. Most of our revenues are derived from our operations within the Philippines.

	Wireless	Fixed Line	ICT	Inter-segment Transactions	Total
<b>(in millions)</b>					
<b>For the nine months ended September 30, 2007</b>					
(Unaudited)					
Revenues and other income	Php66,407	Php36,242	Php7,643	(Php6,824)	Php103,468
Service	64,059	35,664	7,416	(6,669)	100,470
Non-service	1,630	119	200	(89)	1,860
Other income	718	459	27	(66)	1,138
Expenses	32,339	30,264	7,709	(6,824)	63,488
Income (loss) before income tax	34,068	5,978	(66)		39,980
Net income for the period	22,947	3,998	7		26,952
Net income attributable to equity holders of PLDT	22,465	3,995	46		26,506

**For the nine months ended  
September 30, 2006**

(Unaudited)

Revenues and other income	60,488	36,629	4,146	(5,863)	95,400
Service	58,016	35,901	3,788	(5,702)	92,003
Non-service	1,842	71	339	(92)	2,160
Equity share in net income of associates			1		1
Other income	630	657	18	(69)	1,236
Expenses	31,655	35,982	4,128	(5,863)	65,902
Income before income tax	28,833	647	18		29,498
Net income for the period	25,757	587	23		26,367
Net income attributable to equity holders of PLDT	25,098	586	60		25,744

<b>Increase (Decrease)</b>	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>Amount</b>	<b>%</b>
Revenues and other income	Php5,919	10	(Php387)	(1)	Php3,497	84	(Php961)	Php8,068	8
Service	6,043	10	(237)	(1)	3,628	96	(967)	8,467	9
Non-service	(212)	(12)	48	68	(139)	(41)	3	(300)	(14)
Equity share in net income of associates					(1)	(100)		(1)	(100)
Other income	88	14	(198)	(30)	9	50	3	(98)	(8)
Expenses	684	2	(5,718)	(16)	3,581	87	(961)	(2,414)	(4)
Income before income tax	5,235	18	5,331	824	(84)	(467)		10,482	36
Net income for the period	(2,810)	(11)	3,411	581	(16)	(70)		585	2
Net income attributable to equity holders of PLDT	(2,633)	(10)	3,409	582	(14)	(23)		762	3

**Wireless**

*Revenues and Other Income*

Our wireless business segment offers cellular services as well as wireless broadband, satellite, VSAT and other services.

The following table summarizes our service and non-service revenues and other income from our wireless business for the nine months ended September 30, 2007 and 2006 by service segment:

**Nine Months Ended September 30,**

<b>(in millions)</b>	<b>2007</b>	<b>%</b>	<b>2006</b>	<b>%</b>	<b>Increase (Decrease) Amount</b>	<b>%</b>
Wireless services:						
Service Revenues						
Cellular	Php61,121	92	Php56,086	93	Php5,035	9
Wireless broadband, satellite, VSAT and others	2,938	5	1,930	3	1,008	52
	64,059	97	58,016	96	6,043	10
Non-service Revenues						
Sale of cellular handsets and SIM-packs	1,630	2	1,842	3	(212)	(12)
Other Income	718	1	630	1	88	14
Total Wireless Revenues and Other Income	Php66,407	100	Php60,488	100	Php5,919	10

### *Service Revenues*

Our wireless service revenues increased by Php6,043 million, or 10%, to Php64,059 million in the first nine months of 2007 as compared with Php58,016 million in the same period in 2006, mainly as a result of the growth in the cellular and wireless broadband subscriber base, an increase in inbound international traffic and inbound roaming revenues, partially offset by an increase in interconnection costs and the unfavorable effect of the appreciation of the Philippine peso on dollar-linked revenues. As a percentage of our total wireless revenues and other income, service revenues contributed 97% in the first nine months of 2007 as compared to 96% in the same period in 2006.

### *Cellular Service*

Our cellular service revenues consist of:

- revenues derived from actual usage of the network by prepaid subscribers and any unused peso value of expired prepaid cards or electronic air time loads, net of content costs and discounts given to dealers;
- monthly service fees from postpaid subscribers, including: (1) charges for calls in excess of allocated free local calls; (2) toll charges for national and international long distance calls; (3) charges for text messages of our service customers in excess of allotted free text messages; and (4) charges for value-added services, net of related content provider costs;

- revenues generated from incoming calls and messages to our subscribers, net of interconnection expenses; fees from reciprocal traffic from international correspondents; and revenues from inbound international roaming calls for the service; and
- other charges, including those for reconnection and migration.

Our cellular service revenues in the first nine months of 2007 amounted to Php61,121 million, an increase of Php5,035 million, or 9%, from Php56,086 million in the same period in 2006. Cellular service revenues accounted for 95% of our wireless service revenues in the first nine months of 2007 as compared to 97% in the same period in 2006.

Smart markets nationwide cellular communications services under the brand names *Smart Buddy*, *Smart Gold*, *addict mobile*, and *Smart Infinity*. *Smart Buddy* is a prepaid service while *Smart Gold*, *Smart Infinity* and *addict mobile* are postpaid services, which are all provided through Smart's digital network. Piltel markets its cellular prepaid service under the brand name *Talk N Text* which is provided through Smart's network.

Since 2006, Smart has focused on segmenting its market by offering sector-specific, value-driven packages such as *All Text*, a new variety of top-up service providing a fixed number of messages with prescribed validity periods. Offerings include *All Text 10 Bonus*, with a suggested retail price of Php12, which includes 10 messages to all networks plus five bonus on-network messages with a one-day validity period and, effective March 24, 2007, *All Text Plus*, which offers 90 on-network messages plus 10 messages to all networks for Php20, with one day validity period. *All Text Plus* is in effect until January 26, 2008. *All Text* also has a voice counterpart in *All Talk Call*, a call package which allows three calls of up to three minutes each for local on-network calls for Php20, valid for one day. Other voice offerings include: (a) the *Flat Rate Plus Call*, which allows a subscriber to make: (1) an on-network call of up to three minutes for Php10 or extend the call to five minutes for Php15; or (2) an off-network call of up to two minutes for Php10 or extend the call up to three minutes for Php15, effective March 29, 2007; and (b) *Tipid Talk*, a call package which allows a subscriber to make four calls of up to 30 seconds each for local on-network calls, valid for one day for Php10 and another variant allowing four calls of up to 15 seconds each for local on-network calls, valid for one day for Php5.50. *All Text 10 Bonus*, *All Talk Call*, *Tipid Talk* and *Flat Rate Plus Call* are now permanent offerings. Smart also continues to offer *Smart 258*, a registration-based service which offers unlimited on-network text messaging in load denominations of Php15, Php30 and Php60 with corresponding expiration periods of 1, 2 and 4 days, respectively.

On January 18, 2007, Smart introduced *LAHATxt*, a top-up service for Smart prepaid subscribers which offers a bundle of text messages available to all networks. *LAHATxt 35* provides for 100 text messages to all networks for Php35 with a one day validity period. Likewise, *Talk N Text* subscribers have *LAHATxt 20* which allows a subscriber to make 50 text messages to all networks for Php20, also valid for one day. A variant of the *All Text* promotion, *Gaantxt Plus* is specifically targeted at *Talk N Text* subscribers. For a load of Php10, the promotion gives 40 *Talk N Text* to *Talk N Text* messages plus five messages to all networks valid for one day. The *Gaantxt Plus* promotion is valid until February 1, 2008.

In May 2007, Smart introduced the *Ask-for-Load* service which offers a maximum of three Php5 air time load requests per day to all Smart and *Talk N Text* subscribers.

On October 3, 2007, we offered the *Talk N Text GaanSIM* for Php30 with pre-stored air time of Php1 plus 25 free SMS. The promotion period will run until November 18, 2007.

Smart likewise has in place various promotions to stimulate international usage. These include *International Budget Text* packages, which have a limited duration and a varying number of allowable messages, allow subscribers to send international text to pre-registered recipients of the subscriber's choice, on supported overseas carriers.

Smart also has a roster of 3G services which it commercially launched in May 2006. These services include video calling, video streaming, high-speed internet browsing and downloading of special 3G content, offered at rates similar to those of 2G services.

The following table summarizes key measures of our cellular business as at and for the nine months ended September 30, 2007 and 2006:

(in millions)	Nine Months Ended September 30,			Increase Amount%
	2007	2006	(Unaudited)	
Cellular service revenues	Php61,121	Php56,086	Php5,035	9
<i>By component</i>				
Voice	59,517	54,608	4,909	9
Data	26,858	26,168	690	3
	32,659	28,440	4,219	15
<i>By service type</i>				
Prepaid	59,517	54,608	4,909	9
Postpaid	55,101	50,921	4,180	8
	4,416	3,687	729	20
<i>Others</i> (1)	1,604	1,478	126	9

(1) Refers to other non-subscriber-related revenues consisting primarily of inbound international roaming fees, revenues from Smart's public calling offices and a small number of leased line contracts, revenues from Wolfpac and other Smart subsidiaries and revenue share in PLDT's WeRoam and PLDT Landline Plus services.

	<b>September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase</b>	
			<b>Amount</b>	<b>%</b>
	(Unaudited)			
Cellular subscriber base	28,260,095	22,929,431	5,330,664	23
Prepaid	27,921,504	22,618,675	5,302,829	23
<i>Smart</i>	19,576,658	16,238,917	3,337,741	21
<i>Piltel</i>	8,344,846	6,379,758	1,965,088	31
Postpaid	338,591	310,756	27,835	9
<b>Nine Months Ended September 30,</b>				
	<b>Increase</b>			
	<b>(Decrease)</b>			
	<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>
	(Unaudited)			
Systemwide traffic volumes (in millions)				
Calls (in minutes)	4,690	4,208	482	11
Domestic outbound	2,806	2,578	228	9
International	1,884	1,630	254	16
<i>Inbound</i>	1,737	1,509	228	15
<i>Outbound</i>	147	121	26	21
SMS count	160,168	178,420	(18,252)	(10)
Text messages	158,655	176,640	(17,985)	(10)
<i>Standard</i>	19,278	23,823	(4,545)	(19)
<i>Bucket-Priced</i>	139,183	152,654	(13,471)	(9)
<i>International</i>	194	163	31	19
Value-Added Services	1,480	1,756	(276)	(16)
Financial Services	33	24	9	38

As at September 30, 2007, Smart and Piltel cellular subscribers totaled 28,260,095, an increase of 5,330,664, or 23%, over their combined cellular subscriber base of 22,929,431 as at September 30, 2006. Prepaid subscribers accounted for 99% of our total subscriber base as at September 30, 2007 and 2006. Prepaid and postpaid subscribers totaled 27,921,504 and 338,591 as at September 30, 2007, reflecting net subscriber activations of 4,064,683 and 20,028, respectively, in the first nine months of 2007.

Revenues attributable to our cellular prepaid service amounted to Php55,101 million in the first nine months of 2007, an 8% increase over the Php50,921 million earned in the same period in 2006. Prepaid service revenues in the first nine months of 2007 and 2006 accounted for 93% of voice and data revenues. Revenues attributable to Smart's postpaid service amounted to Php4,416 million in the first nine months of 2007, a 20% increase over the Php3,687 million earned in the same period in 2006, and accounted for 7% of voice and data revenues in 2007 and 2006.



*Voice Services*

Cellular revenues from voice services, which include all voice traffic and voice value-added services such as voice mail and international roaming, increased by Php690 million, or 3%, to Php26,858 million in the first nine months of 2007 from Php26,168 million in the same period in 2006 primarily due to an increase in domestic voice, international long distance and voice roaming revenues, and domestic and international inbound revenues. The increase in domestic and international outbound and inbound revenues may be attributed to increased traffic mainly on account of subscriber growth.

Air time rates for postpaid subscribers vary depending on the type of postpaid plan selected by subscribers.

*Data Services*

Cellular revenues from data services, which include all text messaging-related services as well as value-added services, increased by Php4,219 million, or 15%, to Php32,659 million in the first nine months of 2007 from Php28,440 million in the same period in 2006. Cellular data services accounted for 53% of cellular service revenues in the first nine months of 2007 as compared to 51% in the same period in 2006.

The following table shows the breakdown of cellular data revenues for the nine months ended September 30, 2007 and 2006:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase (Decrease) Amount</b>	<b>%</b>
<b>(in millions)</b>	(Unaudited)			
Text messaging				
Domestic	Php29,059	Php24,156	Php4,903	20
<i>Standard</i>	15,021	16,640	(1,619)	(10)
<i>Bucket-Priced</i>	14,038	7,516	6,522	87
International	1,383	1,425	(42)	(3)
	30,442	25,581	4,861	19
Value-added services				
Standard(1)	1,428	1,967	(539)	(27)
Rich Media(2)	254	200	54	27
<i>Pasa Load</i>	472	642	(170)	(26)
	2,154	2,809	(655)	(23)
Financial services				
<i>Smart Money</i>	60	47	13	28

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Mobile Banking	3	3		
	63	50	13	26
Total	Php32,659	Php28,440	Php4,219	15

(1) Includes standard services such as info-on-demand, ringtone and logo downloads, etc.

(2) Includes MMS, WAP, GPRS, etc.

Text messaging-related services contributed revenues of Php30,442 million in the first nine months of 2007, an increase of Php4,861 million, or 19%, compared to Php25,581 million in the same period in 2006, and accounted for 93% and 90% of the total cellular data revenues in the first nine months of 2007 and 2006, respectively. The increase in revenues from text messaging-related services resulted mainly from Smart's various bucket-priced text promotional offerings. Text messaging revenues from the various bucket plans totaled Php14,038 million in the first nine months of 2007, an increase of Php6,522 million, or 87%, compared to Php7,516 million in the same period in 2006.

Standard text messages totaled 19,278 million in the first nine months of 2007, a decrease of 4,545 million, or 19%, from 23,823 million in the same period in 2006 mainly due to a shift to bucket-priced text services. Bucket-priced text messages in the first nine months of 2007 totaled 139,183 million, a decrease of 13,471 million, or 9%, as compared to 152,654 million in the same period in 2006 mainly on account of the introduction in late 2006 of low-denomination text packages with a fixed number of SMS including off-network messages. While these promotional text offerings resulted in reduced traffic for *Smart 258 Unlimited Text* service, the yield per SMS improved significantly resulting in increased text revenues.

Value-added services, which contributed revenues of Php2,154 million in the first nine months of 2007, decreased by Php655 million, or 23%, from Php2,809 million in the same period of 2006 primarily due to lower usage of standard services and *Pasa Load*, partially offset by higher usage of rich media services in the first nine months of 2007 as compared to the same period in 2006.

*Subscriber Base, ARPU and Churn Rates*

Prepaid subscribers accounted for approximately 99% of our 28,260,095 subscribers as at September 30, 2007, while postpaid subscribers accounted for the remaining 1%. The cellular prepaid subscriber base grew by 23% to 27,921,504 as at September 30, 2007 from 22,618,675 as at September 30, 2006, whereas the postpaid subscriber base increased by 9% to 338,591 as at September 30, 2007 from 310,756 as at September 30, 2006.

Our net subscriber activations for the nine months ended September 30, 2007 and 2006 were as follows:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase (Decrease) Amount %</b>	
			<b>(Unaudited)</b>	
Prepaid	4,064,683	2,490,132	1,574,551	63
Smart	2,694,216	1,094,799	1,599,417	146
Piltel	1,370,467	1,395,333	(24,866)	(2)
Postpaid	20,028	30,678	(10,650)	(35)
<b>Total</b>	<b>4,084,711</b>	<b>2,520,810</b>	<b>1,563,901</b>	<b>62</b>

The following table summarizes our cellular ARPUs for the nine months ended September 30, 2007 and 2006:

	<b>Nine Months Ended September 30,</b>							
	<b>Gross</b>		<b>Increase (Decrease)</b>		<b>Net</b>		<b>Increase (Decrease)</b>	
	<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>	<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>
			<b>(Unaudited)</b>					
Prepaid								
Smart	Php314	Php341	(Php27)	(8)	Php257	Php290	(Php33)	(11)
Piltel	222	231	(9)	(4)	186	197	(11)	(6)
Prepaid Blended	287	312	(25)	(8)	236	265	(29)	(11)
Postpaid Smart	2,086	1,893	193	10	1,491	1,401	90	6
Prepaid and Postpaid Blended	309	333	(24)	(7)	252	280	(28)	(10)

ARPU is computed for each month by dividing the revenues for the relevant services for the month by the average of the number of subscribers at the beginning and at the end of the month. Gross monthly ARPU is computed by dividing the revenues for the relevant services, gross of discounts and allocated content-provider costs, including interconnection income but excluding inbound roaming revenues, by the average number of subscribers. Net monthly ARPU, on the other hand, is calculated based on revenues net of discounts and allocated content-provider costs and interconnection income net of interconnection expense. ARPU for any period of more than one month is calculated as the simple average of the monthly ARPUs in that period.

Prepaid service revenues consist mainly of charges for subscribers' actual usage of their loads. Prepaid blended ARPU in the first nine months of 2007 was Php287, a decrease of 8%, compared to Php312 in the same period in 2006. The average outbound domestic and international voice as well as the average value-added services and inbound revenue per subscriber declined in the first nine months of 2007 compared to the same period in 2006, but were partly offset by an increase in the average text messaging revenue per subscriber. On a net basis, prepaid blended ARPU in the first nine months of 2007 was Php236, a decrease of 11%, compared to Php265 in the same period in 2006.

Monthly ARPU for Smart's postpaid services is calculated in a manner similar to that of prepaid service, except that the revenues consist mainly of monthly service fees and charges on usage in excess of the monthly service fees.

Gross monthly ARPU for postpaid subscribers increased by 10% to Php2,086 while net monthly ARPU increased by 6% to Php1,491 in the first nine months of 2007 as compared to Php1,893 and Php1,401 in the same period in 2006, respectively. Prepaid and postpaid monthly gross blended ARPU was Php309 in the first nine months of 2007, a decrease of 7%, compared to Php333 in the same period in 2006. Monthly net blended ARPU decreased by 10% to Php252 in the first nine months of 2007 as compared to Php280 in the same period in 2006.

Our quarterly prepaid and postpaid ARPUs for the nine months ended September 30, 2007 and 2006 were as follows:

	Prepaid				Postpaid	
	Smart		Piltel		Smart	
	Gross	Net	Gross	Net	Gross	Net
(Unaudited)						
<b>2007</b>						
First Quarter	Php323	Php267	Php228	Php187	Php2,045	Php1,483
Second Quarter	324	265	233	198	2,141	1,526
Third Quarter	293	239	206	173	2,073	1,464
<b>2006</b>						
First Quarter	Php356	Php294	Php245	Php207	Php1,867	Php1,386
Second Quarter	344	294	234	202	1,920	1,414
Third Quarter	323	280	213	184	1,891	1,403
Fourth Quarter	332	286	213	184	1,939	1,425

Churn, or the rate at which existing subscribers have their service cancelled in a given period, is computed based on total disconnections in the period, net of reconnections in the case of postpaid subscribers, divided by the average of the number of subscribers at the beginning and at the end of a month, all divided by the number of months in the same period.

We recognize a prepaid cellular subscriber as an active subscriber when that subscriber activates and uses the SIM card in the subscriber's handset, which contains pre-stored air time. The pre-stored air time, equivalent to Php1 plus 50 free SMS, can only be used upon purchase or reload of air time of any value. Subscribers can reload their air time by purchasing prepaid call and text cards; by purchasing additional air time over the air via *Smart Load*, *All Text* or *Smart Connect*; and by receiving loads of Php2, Php5, Php10 and Php15 via *Pasa Load*, or through their handsets using *Smart Money*. Reloads have validity periods ranging from one day to two months, depending on the amount reloaded. A prepaid cellular subscriber is disconnected if the subscriber does not reload within four months after the full usage or expiry of the last reload. Our current policy is to recognize a prepaid subscriber as active only when the subscriber

activates and uses the SIM card and reloads at least once during the month of initial activation or in the immediate succeeding month.

For Smart prepaid, the average monthly churn rate for the first nine months of 2007 and 2006 were 3.1% and 3.2%, respectively, while the average monthly churn rate for *Talk N Text* subscribers was 3.5% in the first nine months of 2007 and 2006.

The average monthly churn rate for Smart's postpaid subscribers for the first nine months of 2007 was 1.3% compared to 1.2% in the same period in 2006. Smart's policy is to redirect outgoing calls to an interactive voice response system if the postpaid subscriber's account is either 45 days overdue or the subscriber has exceeded the prescribed credit limit. If the subscriber does not make a payment within 44 days of redirection, the account is disconnected. Within this 44-day period, a series of collection activities are implemented, involving the sending of a collection letter, call-out reminders and collection messages via text messaging.

#### *Wireless Broadband, Satellite, VSAT and Other Services*

Our revenues from wireless broadband, satellite, VSAT and other services consist of wireless broadband service revenues for Smart Broadband, rentals received for the lease of Mabuhay Satellite's transponders and Telesat's VSAT facilities to other companies, charges for ACeS Philippines' satellite information and messaging services and service revenues generated from PLDT Global's subsidiaries. Gross revenues from these services for the first nine months of 2007 amounted to Php2,938 million, an increase of Php1,008 million, or 52%, from Php1,930 million in the same period in 2006 principally due to the growth in our wireless broadband business partially offset by lower satellite transponder rental revenues.

Smart Broadband offers a number of wireless broadband services and had 259,477 subscribers as at September 30, 2007 as compared to 92,922 in the same period in 2006. *SmartBro*, the fixed wireless broadband service of Smart linked to Smart's wireless broadband-enabled base stations, allows people to connect to the internet using an outdoor aerial antenna installed in a subscriber's home. Wireless broadband revenues contributed Php1,597 million in the first nine months of 2007, increasing by Php1,088 million, or 214%, from Php509 million in the same period in 2006.

We also offer *PLDT WeRoam*, a wireless broadband service, running on Smart's nationwide wireless network (using GPRS, EDGE and WiFi technologies) and PLDT's extensive IP infrastructure. Some of the recent enhancements to this service are the inclusion of international roaming in key roaming countries all over the world and national WiFi roaming access. Principally targeted at the corporate market, this service had 12,239 subscribers as at September 30, 2007 compared to 8,000 subscribers as at September 30, 2006 and contributed Php92 million to our data revenues, increasing by 64% from Php56 million in the same period in 2006.

*Non-service Revenues*

Our wireless non-service revenues consist of:

- proceeds from sales of cellular handsets; and
- proceeds from sales of cellular SIM-packs.

Our wireless non-service revenues decreased by Php212 million, or 12%, to Php1,630 million in the first nine months of 2007 as compared to Php1,842 million in the same period in 2006 primarily due to a lower volume of postpaid handsets sold and a lower average revenue per handset and SIM-pack, partly offset by a higher volume of prepaid handsets and SIM-packs sold in the first nine months of 2007.

*Other Income*

All other income/gains such as rental income, gain on disposal of property and which do not fall under service and non-service revenues are included under this classification. Our wireless business segment generated other income of Php718 million in the first nine months of 2007, an increase of Php88 million, or 14%, as compared to Php630 million in the same period in 2006.

*Expenses*

Expenses associated with our wireless business in the first nine months of 2007 amounted to Php32,339 million, an increase of Php684 million, or 2%, from Php31,655 million in the same period in 2006. A significant portion of this increase was attributable to higher depreciation and amortization, rent and selling and promotions expenses partially offset by net financing gains. As a percentage of our total wireless revenues and other income, expenses associated with our wireless business accounted for 49% and 52% in the first nine months of 2007 and 2006, respectively.

Cellular business expenses accounted for 92% of our wireless business expenses, while wireless broadband, satellite, VSAT and other business expenses accounted for the remaining 8% of our wireless business expenses in the first nine months of 2007 and 2006.

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The following table summarizes the breakdown of our wireless-related expenses for the nine months ended September 30, 2007 and 2006 and the percentage of each expense item to the total:

	Nine Months Ended September 30,					
	2007		2006		Increase (Decrease) Amount %	
(in millions)		%		%		
Wireless services						
Depreciation and amortization	Php8,907	28	Php7,948	25	Php959	12
Rent	6,274	19	5,157	16	1,117	22
Compensation and benefits(1)	3,730	12	3,928	12	(198)	(5)
Cost of sales	3,443	11	3,600	11	(157)	(4)
Selling and promotions	2,836	9	2,032	7	804	40
Maintenance	2,635	8	2,688	9	(53)	(2)
Professional and other contracted services	1,632	5	1,332	4	300	23
Taxes and licenses	922	3	754	2	168	22
Communication, training and travel	773	2	632	2	141	22
Insurance and security services	564	2	620	2	(56)	(9)
Provisions	272	1	397	1	(125)	(31)
Amortization of intangible assets	124		236	1	(112)	(47)
Financing costs (gains)	(527)	(2)	1,845	6	(2,372)	(129)
Other expenses	754	2	486	2	268	55
Total	Php32,339	100	Php31,655	100	Php684	2

(1) Includes salaries and benefits, incentive plan, pension and manpower rightsizing program, or MRP, costs.

Depreciation and amortization charges increased by Php959 million, or 12%, to Php8,907 million in the first nine months of 2007, principally due to an increase in our depreciable asset base mainly transmission facilities, 3G and broadband networks, and broadband customer-deployed equipment.

Rent expenses increased by Php1,117 million, or 22%, to Php6,274 million on account of an increase in domestic fiber optic network, or DFON, facilities and transmission circuits leased by Smart from PLDT, as well as higher site rental expenses. As at September 30, 2007, we had 4,817 GSM cell sites and 7,401 base stations, compared with 4,365 GSM cell sites and 6,079 base stations as at September 30, 2006.

Compensation and benefits expenses decreased by Php198 million, or 5%, to Php3,730 million primarily due to lower accrued long-term incentive plan, or LTIP, benefit and MRP costs, partly offset by employees' basic pay increase, higher accrued bonuses and other employee benefits of Smart. Smart and subsidiaries' employee headcount increased by 20 to 5,294 in the first nine months of 2007 as compared to 5,274 in the same period in 2006. For further

discussion on our LTIP, please see *Note 21 Employee Benefits* to the accompanying unaudited consolidated financial statements.

Cost of sales decreased by Php157 million, or 4%, to Php3,443 million due to lower average cost of handsets and SIMs. The breakdown of cost of sales for our wireless business for the nine months ended September 30, 2007 and 2006 is as follows:

	<b>Nine Months Ended September</b>			
	<b>30,</b>		<b>Decrease</b>	
<b>(in millions)</b>	<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>
		(Unaudited)		
Cost of cellular handsets and SIM-packs sold	Php3,321	Php3,454	(Php133)	(4)
Cost of satellite air time and terminal units	122	146	(24)	(16)
	Php3,443	Php3,600	(Php157)	(4)

Selling and promotion expenses increased by Php804 million, or 40%, to Php2,836 million due to higher advertising, promotion and commission expenses, partly offset by a decrease in printing cost of prepaid cards with the prevalence of e-loading.

Maintenance expenses decreased by Php53 million, or 2%, to Php2,635 million mainly due to lower repairs and maintenance costs for network facilities and IT software, and a decrease in fuel costs for power generation, partly offset by higher expenses for electricity consumption for cell sites.

Professional and other contracted services increased by Php300 million, or 23%, to Php1,632 million primarily due to higher expenses for contracted services, consultancy and technical services, market research and advisory fees.

Taxes and licenses increased by Php168 million, or 22%, to Php922 million primarily due to higher non-creditable input tax and the Philippine National Telecommunications Commission, or NTC, licenses and fees, partly offset by lower business-related taxes and licenses.

Communication, training and travel expenses increased by Php141 million, or 22%, to Php773 million mainly due to higher mailing and courier charges, and local travel expenses.



Insurance and security services decreased by Php56 million, or 9%, to Php564 million primarily due to the decrease in site security expenses and lower charges on insurance contracts.

Provisions decreased by Php125 million, or 31%, to Php272 million primarily due to a lower level of write-down of slow-moving handsets to net realizable values.

Amortization of intangible assets decreased by Php112 million, or 47%, to Php124 million mainly due to intangible assets relating to technology application arising from the acquisition of Wolfpac which was fully amortized by the end of 2006.

We recognized net financing gains of Php527 million in the first nine months of 2007 as compared to a net financing costs of Php1,845 million in the same period in 2006 due to lower accretion on financial liabilities due to the settlement of Piltel's debt complemented by the appreciation of the Philippine peso to the U.S. dollar in 2007, partly offset by lower interest income and capitalized interest. The breakdown of our financing costs (gains) for our wireless business for the nine months ended September 30, 2007 and 2006 is as follows:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Change</b>	<b>%</b>
<b>(in millions)</b>	(Unaudited)			
Interest on loans and related items	Php1,205	Php1,274	(Php69)	(5)
Accretion on financial liabilities net	665	2,887	(2,222)	(77)
Financing charges	37	33	4	12
Dividends on preferred stock subject to mandatory redemption	14	113	(99)	(88)
Gain on derivative transactions net	(48)	(24)	(24)	100
Capitalized interest	(124)	(205)	81	(40)
Interest income	(860)	(911)	51	(6)
Foreign exchange gains net	(1,416)	(1,322)	(94)	7
	(Php527)	Php1,845	(Php2,372)	(129)

Other expenses increased by Php268 million, or 55%, to Php754 million primarily due to various business and operational-related expenses.

*Provision for Income Tax*

Provision for income tax increased by Php8,045 million, or 262%, to Php11,121 million in the first nine months of 2007 from Php3,076 million in the same period in 2006. In the first nine months of 2007, the effective tax rate for our wireless business was 33% as compared to 11% in the same period in 2006 mainly due to the recognition of deferred tax assets of Piltel in 2006.

*Net Income*

Our wireless business segment recorded a net income of Php22,947 million in the first nine months of 2007, a decrease of Php2,810 million, or 11%, over Php25,757 million registered in the same period in 2006 on account of higher provision for income tax largely due to Piltel's recognition of deferred tax assets in 2006.

Fixed Line

*Revenues and Other Income*

Our fixed line business provides local exchange service, international and national long distance services, data and other network services, and miscellaneous services. Total fixed line revenues generated from our fixed line business in the first nine months of 2007 totaled Php36,242 million, a decrease of Php387 million, or 1%, from Php36,629 million in the same period in 2006.

The following table summarizes revenues from our fixed line business for the nine months ended September 30, 2007 and 2006 by service segment:

	<b>Nine Months Ended September 30,</b>				<b>Increase (Decrease)</b>	
	<b>2007</b>	<b>%</b>	<b>2006</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
			(Unaudited)			
<b>(in millions)</b>						
Fixed line services:						
Service Revenues						
Local exchange	Php11,889	33	Php12,862	35	(Php973)	(8)
International long distance	6,685	19	7,434	20	(749)	(10)
National long distance	4,864	13	5,117	14	(253)	(5)
Data and other network	11,180	31	9,420	26	1,760	19
Miscellaneous	1,046	3	1,068	3	(22)	(2)
	35,664	99	35,901	98	(237)	(1)

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Non-Service Revenues	119		71		48	68
Other Income	459	1	657	2	(198)	(30)
Total Fixed Line Revenues and Other Income	Php36,242	100	Php36,629	100	(Php387)	(1)

Service Revenues

*Local Exchange Service*

Our local exchange service revenues consist of:

- flat monthly fees for our postpaid and fixed charges for our bundled and data services;
- installation charges and other one-time fees associated with the establishment of customer service;
- revenues from usage of prepaid cards for calls within the local area and any unused peso value of expired prepaid cards; and
- charges for special features, including bundled value-added services such as call waiting, call forwarding, multi-party conference calling, speed calling and caller ID.

The following table summarizes key measures of our local exchange service business as at and for the nine months ended September 30, 2007 and 2006:

		<b>Nine Months Ended</b>	
		<b>September 30,</b>	
		<b>Increase</b>	
		<b>(Decrease)</b>	
<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>

Total local exchange service revenues (in millions of pesos) **11,889** **12,862** **(973)** **(8)**  
(Unaudited)

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Number of fixed line subscribers	1,751,468	1,747,357	4,111	
Postpaid	1,454,678	1,443,893	10,785	1
Prepaid	296,790	303,464	(6,674)	(2)
Number of fixed line employees	8,057	9,110	(1,053)	(12)
Number of fixed line subscribers per employee	217	192	25	13

Revenues from our local exchange service decreased by Php973 million, or 8%, to Php11,889 million in the first nine months of 2007 from Php12,862 million in the same period in 2006. The decrease was primarily due to the appreciation of the peso which required us to make downward adjustments in our monthly local service rates and the change in subscriber base mix in favor of prepaid subscribers with lower average revenue per user. The percentage contribution of local exchange revenues to our total fixed line service revenues decreased to 33% in the first nine months of 2007 as compared to 36% in the same period in 2006.

Initially intended as an affordable alternative telephone service for consumers under difficult economic conditions, our prepaid fixed line services now form an important part of our overall churn and credit risk exposure management and subscriber retention strategy. PLDT currently has three prepaid fixed line services: *Teletipid* and *Telesulit*, both funded by consumable prepaid cards, and the *Telepwede*, which is funded by e-loads (available at Smart or PLDT e-load retailers). *Telepwede* subscribers are charged Php115 to receive incoming calls and can reload for as low as Php30 to make outgoing calls. Local call rates are made more affordable at Php2 per call, unlimited. Upon the launch of *Telepwede*, PLDT stopped offering *Teletipid* and *Telesulit* to new subscribers. PLDT is constrained to discontinue *Teletipid* and *Telesulit* as they run on an old technology platform which has now become obsolete and such platform will be fully retired by May 1, 2008. Last day of reloading was set last November 1, 2007 allowing subscribers ample time to consume their account balances and complete the maximum account life up to May 1, 2008. Subscribers of *Teletipid* and *Telesulit* were advised via print ads, direct mailers and call outs of their option to upgrade to *Telepwede* or to regular PLDT postpaid.

In March 2007, PLDT launched the PLDT Landline Plus, a fixed wireless service where subscribers to the service benefit from a text-capable home phone. This service is initially offered outside Metro Manila with the phone unit at Php2,400 and a monthly service fee of Php600 and Php1,000 for residential and business subscribers, respectively. As at September 30, 2007, there were a total of 13,250 PLDT Landline Plus subscribers.

Pursuant to a currency exchange rate adjustment, or CERA, mechanism authorized by the NTC, we adjust our postpaid monthly local service rates upward or downward by 1% for every Php0.10 change in the peso-to-dollar exchange rate relative to a base rate of Php11.00 to US\$1.00. In the first nine months of 2007, we implemented five downward adjustments and one upward adjustment in our monthly local service rates, while there were six downward adjustments and three upward adjustments in the same period in 2006. The average Philippine peso to U.S. dollar rate factored in our monthly local service rates in the first nine months of 2007 was Php48.30 to US\$1.00, compared to an average of Php52.03 to US\$1.00 in the same period in 2006. This change in the average peso-to-dollar rate translated to a peso appreciation of 7%, which resulted in a net decrease of approximately 7% in our average monthly local service rates in the first nine months of 2007. In its letter dated July 16, 2007, the NTC has approved our request to use annual average exchange rates as our basis in CERA computation instead of the currently used monthly averages. Accordingly, effective August 18, 2007, our CERA computation is based on the average Philippine peso to U.S. dollar exchange rate of Php49.76 covering the period July 2006 to June 2007.

*International Long Distance Service*

Our international long distance service revenues, which we generate through our international gateway facilities, consist of:

- inbound call revenues representing settlements from foreign telecommunications carriers for inbound international calls, virtual transit and hubbing service and reverse charged calls such as received collect and home country direct service;
- access charges paid to us by other Philippine telecommunications carriers for terminating inbound international calls to our local exchange network; and
- outbound call revenues representing amounts billed to our customers (other than our cellular customers) for outbound international calls, net of amounts payable to foreign telecommunications carriers for terminating calls in their territories.

The following table shows information about our international fixed line long distance business for the nine months ended September 30, 2007 and 2006:

	<b>Nine Months Ended September 30,</b>			
			<b>Increase (Decrease)</b>	
	<b>2007</b>	<b>2006</b>	<b>Amount</b>	<b>%</b>
	(Unaudited)			
Total international long distance service revenues (in millions)	Php6,685	Php7,434	(Php749)	(10)
Inbound	5,506	6,220	(714)	(11)
Outbound	1,179	1,214	(35)	(3)
International call volumes (in million minutes, except call ratio)	1,702	1,582	120	8
Inbound	1,493	1,442	51	4
Outbound	209	140	69	49
Inbound-outbound call ratio	7.1:1	10.3:1		

Our total international long distance service revenues decreased by Php749 million, or 10%, to Php6,685 million in the first nine months of 2007 from Php7,434 million in the same period in 2006 primarily due to the peso appreciation and a decrease in average termination rates for inbound calls mitigated by an increase in call volumes. The percentage contribution of international long distance service revenues to our total fixed line service revenues decreased to 19% in the first nine months of 2007 from 21% in the same period in 2006.

Our revenues from inbound international long distance service decreased by Php714 million, or 11%, to Php5,506 million due to the appreciation of the Philippine peso to the U.S. dollar coupled with a decrease in average rate per minute due to the change in call mix with more traffic terminating to cellular operators where the net revenue kept by us is lower. These decreasing effects were partially offset by an increase in inbound traffic volume by 51 million minutes to 1,493 million minutes in the first nine months of 2007. The appreciation of the Philippine peso to the U.S. dollar with average exchange rates of Php47.53 in the first nine months of 2007 and Php52.19 in the same period in 2006 contributed to the decrease in our inbound international long distance revenues in peso terms, since settlement charges for inbound calls are billed in U.S. dollars or in special drawing rights, an established method of settlement among international telecommunications carriers using values based on a basket of foreign currencies that are translated into pesos at the time of billing.

Our revenues from outbound international long distance service decreased by Php35 million, or 3%, to Php1,179 million in the first nine months of 2007 primarily due to a decline in average revenue per minute as a result of a lower average collection rate with the introduction of low-rate services such as *PLDT ID-DSL* and *Budget Card*, and the peso appreciation in 2007, which more than offset the increase in outbound international call volumes in 2006.

#### *National Long Distance Service*

Our national long distance service revenues consist of:

- per minute charges for calls made by our fixed line customers outside of the local service areas but within the Philippines, net of interconnection charges payable for calls carried through the backbone network of, and/or terminating to the customer of, another telecommunications carrier;
- access charges received from other telecommunications carriers for calls carried through our backbone network and/or terminating to our customers; and
- fixed charges paid by other telephone companies, charges retained by PLDT for calls terminating to cellular subscribers within the local area, and local access charges paid by cellular operators for calls by cellular subscribers that terminate to our local exchange network.

The following table shows our national long distance service revenues and call volumes for the nine months ended September 30, 2007 and 2006:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase (Decrease) Amount %</b>	
	(Unaudited)			
Total national long distance service revenues (in millions)	Php4,864	Php5,117	(Php253)	(5)
National long distance call volumes (in million minutes)	1,652	1,688	(36)	(2)

Our national long distance service revenues decreased by Php253 million, or 5%, to Php4,864 million in the first nine months of 2007 from Php5,117 million in the same period in 2006 primarily due to a decrease in call volumes coupled with a lower average revenue per minute in the first nine months of 2007. The percentage contribution of national long distance revenues to our fixed line service revenues accounted for 14% in the first nine months of 2007 and 2006.

#### *Data and Other Network Services*

Our data and other network service revenues include charges for leased lines, IP-based, packet-based and switched-based services. These services are used for domestic and international communications such as private networking, broadband and narrowband internet-based data communications, and packet-based communication.

The following table shows information about our data and other network service revenues for the nine months ended September 30, 2007 and 2006:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase (Decrease) Amount %</b>	
	(Unaudited)			
Data and other network service revenues (in millions)	Php11,180	Php9,420	Php1,760	19
Number of DSL broadband subscribers	229,534	118,679	110,855	93
Number of <i>PLDT Vibe</i> narrowband subscribers	268,984	294,778	(25,794)	(9)

In the first nine months of 2007, our data and other network services posted revenues of Php11,180 million, an increase of Php1,760 million, or 19%, from Php9,420 million in the same period in 2006 primarily due to increases in leased lines, IP-based and switched-based data services, particularly Diginet and DFON rental, and *PLDT DSL* mitigated by lower *PLDT Vibe* services. The percentage contribution of this service segment to our fixed line service revenues increased to 31% in the first nine months of 2007 from 26% in the same period in 2006.

IP-based products include *PLDT DSL (myDSL and BizDSL)*, *PLDT Vibe* and I-Gate. *PLDT DSL* broadband internet service is targeted for heavy individual internet users as well as for small and medium enterprises, while *PLDT Vibe*, *PLDT*'s dial-up/narrowband internet service, is targeted for light to medium residential or individual internet users. I-Gate, our dedicated leased line internet access service, on the other hand, is targeted at enterprises and value-added service providers.

*DSL* contributed revenues of Php2,764 million in the first nine months of 2007, an increase of Php432 million, or 19%, from Php2,332 million in the same period in 2006 primarily due to an increase in the number of subscribers. *DSL* reached 229,534 subscribers as at September 30, 2007 compared with 118,679 subscribers in the same period in 2006. *DSL* offers a number of packages with maximum speeds ranging from 88 kbps to 5 Mbps depending on the plan.

*PLDT Vibe* revenues decreased by Php82 million, or 28%, to Php206 million in the first nine months of 2007 from Php288 million in the same period in 2006 primarily due to lower number of plan subscribers as well as the declining usage of Vibe prepaid. The declining number of Vibe plans and regular monthly users for Vibe prepaid may be attributed to the migration from Vibe dial-up to *DSL* which is now priced more competitively. As at September 30, 2007, *PLDT Vibe* registered users totaled 268,984, of which 76,122 were exclusive postpaid users, 187,263 were exclusive prepaid users, and 5,599 were both postpaid and prepaid users. As at September 30, 2006, *PLDT Vibe* registered users totaled 294,778, of which 111,137 were exclusive postpaid users, 168,815 were exclusive prepaid users, and 14,826 were both postpaid and prepaid users.

In support of the growing data requirements of the small and medium enterprise market, the network footprints of BRAINS, IP-VPN and *Shops.work*, *PLDT*'s private local networking services, have been expanded with the roll-out of Next Generation Network, or NGN, facilities in key business areas across the country.

The continued growth in data services revenues can be attributed to several product offerings. The steady demand for dedicated connectivity or private networking from the corporate market using *PLDT*'s traditional international and domestic data offerings – Fibernet, Arcstar, Acacia, I-Gate, Diginet, BRAINS, IP-VPN and *Shops.work*, among others continues to provide us with a stable revenue source.



On October 17, 2007, PLDT, with its robust and reliable nationwide telecommunications network, teamed up with Intel to offer the Simplified Networks on Auto Pilot, or SNAP, a turn-key and cost-effective IT networking solution that can help increase profitability and competitiveness. For a flat monthly fee arrangement, SNAP handles a company's IT requirements which includes the latest Intel processors and hardware components, server solutions, technical support and broadband connectivity.

Dignet, our domestic private leased line service, has been providing Smart's increasing fiber optic and leased line data requirements. Dignet revenues increased by Php841 million, or 20%, to Php5,118 million in the first nine months of 2007 as compared to Php4,277 million in the same period in 2006 mainly due to Smart's DFON rental of Php3,833 million and Php3,011 million in the first nine months of 2007 and 2006, respectively.

#### *Miscellaneous*

Miscellaneous service revenues are derived mostly from directory advertising and facilities management and rental fees. In the first nine months of 2007, these revenues decreased by Php22 million, or 2%, to Php1,046 million from Php1,068 million in the same period in 2006 mainly due to a decline in facilities management fees, mitigated by an increase in rental income owing to higher co-location charges. The percentage contribution of miscellaneous service revenues to our total fixed line service revenues was 3% in the first nine months of 2007 and 2006.

#### *Non-service Revenues*

Non-service revenues increased by Php48 million, or 68%, to Php119 million in the first nine months of 2007 from Php71 million in the same period in 2006 primarily due to higher computer sales in relation to our DSL promotion.

#### *Other Income*

All other income/gains such as rental income and gain on disposal of property, which do not fall under service and non-service revenues, are included under this classification. In the first nine months of 2007, our fixed line business segment registered a decrease in other income of Php198 million, or 30%, to Php459 million from Php657 million in the same period in 2006 mainly due to lower income from disposal of assets and various materials.

#### *Expenses*

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Expenses related to our fixed line business totaled Php30,264 million in the first nine months of 2007, a decrease of Php5,718 million, or 16%, as compared to Php35,982 million in the same period in 2006. The decrease was primarily due to lower depreciation and amortization, selling and promotion expenses, and financing costs partially offset by higher professional and other contracted services, taxes and licenses, and compensation and benefits.

The following table shows the breakdown of our total fixed line-related expenses for the nine months ended September 30, 2007 and 2006 and the percentage of each expense item to the total:

	Nine Months Ended September 30,				Increase (Decrease)	
	2007	%	2006	%	Amount	%
			(Unaudited)			
<b>(in millions)</b>						
Fixed line services:						
Depreciation and amortization	Php9,330	31	Php15,248	42	(Php5,918)	(39)
Compensation and benefits(1)	7,879	26	7,519	21	360	5
Financing costs	4,386	15	5,331	15	(945)	(18)
Maintenance	2,730	9	2,442	7	288	12
Professional and other contracted services	1,243	4	682	2	561	82
Rent	1,205	4	1,202	3	3	
Provisions	857	3	478	1	379	79
Selling and promotions	831	3	1,345	4	(514)	(38)
Taxes and licenses	728	2	491	2	237	48
Insurance and security services	330	1	388	1	(58)	(15)
Communication, training and travel	319	1	369	1	(50)	(14)
Cost of sales	118		113		5	4
Other expenses	308	1	374	1	(66)	(18)
<b>Total</b>	<b>Php30,264</b>	<b>100</b>	<b>Php35,982</b>	<b>100</b>	<b>(Php5,718)</b>	<b>(16)</b>

(1) Includes salaries and benefits, incentive plan, pension and MRP costs.

Depreciation and amortization charges decreased by Php5,918 million, or 39%, to Php9,330 million due to higher additional depreciation charges recognized by PLDT in 2006 on certain properties and equipment affected by our NGN roll-out. In the first nine months of 2007, we recognized additional depreciation of Php1,100 million relating to Piltel's equipment that are also affected by the NGN roll-out.

Compensation and benefits expenses increased by Php360 million, or 5%, to Php7,879 million primarily due to the effect of collective bargaining agreement-related increases in salaries and benefits, and an increase in pension benefits and MRP costs, partially offset by the lower costs of LTIP. For further discussion on our LTIP, please see *Note 21 Employee Benefits* to the accompanying unaudited consolidated financial statements.

Financing costs decreased by Php945 million, or 18%, to Php4,386 million largely due to lower interest on loans and related items and lower hedge costs. These were partially offset by higher loss on derivative transactions and lower interest income. The breakdown of financing costs for our fixed line business for the nine months ended September 30, 2007 and 2006 is as follows:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Change</b>	<b>%</b>
<b>(in millions)</b>	<b>(Unaudited)</b>			
Interest on loans and related items	Php3,800	Php4,826	(Php1,026)	(21)
Hedge costs	908	1,090	(182)	(17)
Loss on derivative transactions	353	175	178	102
Accretion on financial liabilities net	130	156	(26)	(17)
Financing charges	1	11	(10)	(91)
Interest income	(238)	(373)	135	(36)
Capitalized interest	(275)	(223)	(52)	23
Foreign exchange gains net	(293)	(331)	38	(11)
	<b>Php4,386</b>	<b>Php5,331</b>	<b>(Php945)</b>	<b>(18)</b>

Maintenance expenses increased by Php288 million, or 12%, to Php2,730 million primarily due to higher maintenance costs for domestic cable and wire facilities as more operating and maintenance-related restorations were incurred in the first nine months of 2007 as compared to the same period in 2006.

Professional and other contracted services increased by Php561 million, or 82%, to Php1,243 million primarily due to PLDT's higher consultancy service fees coupled with higher contracted services.

Rent expenses increased by Php3 million to Php1,205 million due to an increase in pole rental charges and higher office and building rentals, partially offset by the decrease in transponder lease and domestic leased circuit charges.

Provisions increased by Php379 million, or 79%, to Php857 million primarily due to higher provision of doubtful accounts as a result of higher than anticipated uncollectible receivables complemented by higher provision for assessments in the first nine months of 2007 compared to the same period in 2006.

Selling and promotion expenses decreased by Php514 million, or 38%, to Php831 million primarily as a result of a collective effort in efficient media spending in relation to various products and services, partially offset by higher public relations expense.

Taxes and licenses increased by Php237 million, or 48%, to Php728 million, mainly on account of higher business-related taxes.

Insurance and security services decreased by Php58 million, or 15%, to Php330 million primarily due to lower premiums on property all-risk, industrial all-risk and industrial fire insurance.

Communication, training and travel expenses decreased by Php50 million, or 14%, to Php319 million due to the decrease in mailing and courier charges, and local and foreign travel.

Cost of sales increased by Php5 million, or 4%, to Php118 million due to the higher computer-bundled sales in relation to our DSL promotion and *WeRoam* subscriptions.

Other expenses decreased by Php66 million, or 18%, to Php308 million due to lower various business and operational-related expenses.

#### *Provision for Income Tax*

Provision for income tax amounted to Php1,980 million in the first nine months of 2007 as compared to Php60 million in the same period in 2006 primarily due to higher taxable income as a result of lower depreciation in 2007.

#### *Net Income*

In the first nine months of 2007, our fixed line business segment contributed a net income of Php3,998 million, an increase of Php3,411 million, or 581%, as compared to Php587 million in the same period in 2006 mainly as a result of a 16% decrease in fixed line-related expenses, particularly depreciation and amortization partially offset by a slight decrease in our service revenues.

#### Information and Communications Technology

*Revenues and Other Income*

Our ICT business provides BPO, call center, internet and online gaming, data center and other services.

On April 16, 2007, SPi acquired, through a wholly-owned US subsidiary, 100% of Springfield Service Corporation, or Springfield, for an aggregate purchase price of US\$35 million, or Php1,664 million, plus possible future earn-out payments with an aggregate fair value at acquisition date of Php962 million. Springfield is one of the largest players in the medical billing and revenue cycle management market. As at September 30, 2007, SPi's total investment in Springfield amounted to Php2,685 million, including fair value of possible future earn-out payments of Php960 million and incidental costs of Php59 million, see *Note 11 Goodwill and Intangible Assets* to the accompanying unaudited financial statements for related discussion.

For further discussion, see *Note 2 Summary of Accounting Policies and Practices Basis of Preparation* to the accompanying unaudited consolidated financial statements.

In the first nine months of 2007, our ICT business generated revenues of Php7,643 million, an increase of Php3,497 million, or 84%, from Php4,146 million in the same period in 2006. This increase was largely due to the consolidation of the SPi Group and Level Up! and the continued increase of our call center revenues.

The following table summarizes revenues from our ICT business for the nine months ended September 30, 2007 and 2006 by service segment:

	2007		2006		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
	(Unaudited)					
<b>(in millions)</b>						
Service Revenues						
BPO	Php3,989	52	Php930	23	Php3,059	329
Call center	2,357	31	1,920	46	437	23
Internet and online gaming	686	9	561	14	125	22
Vitroã data center	311	4	287	7	24	8
Others	73	1	90	2	(17)	(19)
	7,416	97	3,788	92	3,628	96
Non-service Revenues						
Point Product Sales	200	3	339	8	(139)	(41)
Other Income	27		18		9	50

Equity share in net income of associates	1	(1)	(100)
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Total ICT Revenues and Other Income	Php7,643	100	Php4,146	100	Php3,497	84
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*Service Revenues*

Service revenues generated by our ICT segment amounted to Php7,416 million in the first nine months of 2007, an increase of Php3,628 million, or 96%, as compared to Php3,788 million in the same period in 2006 primarily as a result of the consolidation of the SPi Group and Level Up! and the continued growth of our call center business.

*Business process outsourcing*

BPO revenues consist of:

- editorial and content production services to the scholarly scientific, technical and medical (SSTM) journal publishing industry;
- digital content conversion services to information organizations such as online and traditional publishers, libraries, educational institutions, Global 1,000 corporations and government agencies worldwide;
- pre-press project management services to book publishers;
- litigation support services which involve conventional coding and electronic discovery support services for corporations, international law firms, corporate counsels and government agencies;
- conversion services of medical record/data from handwritten or speech format to electronic format and patient scheduling, coding and compliance assistance, consulting and specialized reporting services; and
- revenue cycle management services for U.S. medical facilities.

We provide our BPO services primarily through the SPi Group, which ePLDT acquired on July 11, 2006. BPO contributed revenues of Php3,989 million in the first nine months of 2007, an increase of Php3,059 million, or 329%, from Php930 million in the same period in 2006 primarily from SPi Group services, and accounted for 54% and 25% of total service revenues of our ICT business in the first nine months of 2007 and 2006, respectively.

### *Call Center*

We are focused on developing our call center business which capitalizes on the availability of English-speaking college graduates in the Philippines with a strong customer service orientation. ePLDT has established one umbrella brand name, *ePLDT Ventus*, for all of its call center businesses, including Ventus, Vocativ and Parlance. Ventus provides offshore contact center outsourcing solutions specializing in inbound customer care. Vocativ provides customer and technical support to its clients in the Philippines, United States and the United Kingdom, while Parlance provides exclusive customer support and billing requirements to one of the largest direct-to-home satellite television providers in the United States. In addition, Infocom, through its Customer Service Outsourcing Group, handles PLDT group's nationwide technical helpdesk operations.

Call center revenues consist of:

- inbound calls for customer care, product inquiries, sales and technical support based on active minutes, billable hours and full-time equivalents;
- outbound calls for sales and collections based on active minutes, billable hours and full-time equivalents; and
- service income for e-mail handling, web chat, web co-browsing, data entry and BPO based on transaction volume.

Revenues relating to our call center business increased by Php437 million, or 23%, to Php2,357 million in the first nine months of 2007 from Php1,920 million in the same period in 2006 primarily due to the expansion of our facilities. In total, we own and operate approximately 5,800 seats with 5,010 customer service representatives, or CSRs, as at September 30, 2007 compared to approximately 5,130 seats with 4,010 CSRs as at September 30, 2006. In 2006, *ePLDT Ventus* launched two new sites bringing our total call center site count to seven as at September 30, 2007.

Call center revenues accounted for 32% and 51% of total service revenues of our ICT business in the first nine months of 2007 and 2006, respectively.

*Internet and online gaming*

Internet service revenues consist of:

- revenues derived from actual usage of the internet access network by prepaid subscribers and any unused peso value of expired prepaid cards or electronic internet time loads, and community access of computers and desktop publishing based on actual usage, net of discounts given to dealers;
  
- monthly service fees from postpaid corporate and consumer subscribers including:  
(1) charges for internet usage in excess of allocated free plan internet hours; (2) one-time installation and activation fees; and (3) fees for value-added services including e-mail and web hosting services;
  
- one-time fees generated from the reselling of internet-related solutions such as security solutions and domain registration;
  
- franchise and royalty fees for *Netopia* internet cafés, including a one-time subscription fee and monthly recurring franchise fees based on certain conditions in the franchise agreement;
  
- online gaming revenues from unique subscribers, including one-time sale of gaming cards and electronic pins, and top-up fees upon actual consumption of gaming credits or after expiration of any unused peso value thereof.

Revenues from our internet and online gaming businesses increased by Php125 million, or 22%, to Php686 million in the first nine months of 2007 from Php561 million in the same period in 2006 primarily due to the consolidation of Level Up! in May 2006 which resulted in an increase in revenues by Php27 million, and an increase in Infocom's revenues by Php60 million. Our internet and online gaming business revenues accounted for 9% and 15% of total service revenues of our ICT business in the first nine months of 2007 and 2006, respectively.

*Vitroä data center*



ePLDT operates an internet data center under the brand name *Vitroä* which provides co-location services, server hosting, hardware and software maintenance services, website development and maintenance services, webcasting and webhosting, shared applications, data disaster recovery and business continuity services, intrusion detection, and security services such as firewalls and managed firewalls.

*Vitroä* revenues consist of:

- monthly service fees derived from co-location services, server hosting, hardware and software maintenance services, website development and maintenance services, web hosting, data recovery security services and other value-added services; and
- installation charges or one-time fees associated with the set-up of services and professional services of *Vitroä*'s certified professionals.

In the first nine months of 2007, *Vitroä* contributed revenues of Php311 million, an increase of Php24 million, or 8%, from Php287 million in the same period in 2006 primarily due to an increase in co-location revenues and server hosting. *Vitroä* revenues accounted for 4% and 8% of service revenues of our ICT business in the first nine months of 2007 and 2006, respectively.

#### *Others*

Other revenues consist of fees generated from the issuance of digital certificates and licenses and revenues derived from IT helpdesk/contact center solutions and terminals for credit, debit and credit card transactions.

Revenues from other businesses related to our ICT segment decreased by Php17 million, or 19%, to Php73 million in the first nine months of 2007 from Php90 million in the same period in 2006.

Please refer to *Note 9 Investments in Associates* to the accompanying unaudited consolidated financial statements for further discussion on ePLDT's investments.

#### *Non-service Revenues*



**(in millions)**

## ICT services:

Compensation and benefits(1)	Php3,984	52	Php1,738	42	Php2,246	129
Professional and other contracted services	938	12	416	10	522	125
Depreciation and amortization	715	9	463	11	252	54
Rent	495	6	356	9	139	39
Maintenance	380	5	258	6	122	47
Communication, training and travel	365	5	170	4	195	115
Selling and promotions	194	3	205	5	(11)	(5)
Cost of sales	184	2	293	7	(109)	(37)
Amortization of intangible assets	162	2	19	1	143	753
Taxes and licenses	66	1	43	1	23	53
Insurance and security services	34	1	21	1	13	62
Provisions	15		(3)		18	600
Financing costs (gains)	(2)		54	1	(56)	(104)
Other expenses	179	2	95	2	84	88
Total	Php7,709	100	Php4,128	100	Php3,581	87

(1) Includes salaries and benefits, incentive plan, pension and MRP costs.

Compensation and benefits increased by Php2,246 million, or 129%, to Php3,984 million largely due to the increased number of employees and corresponding salaries and employee benefits resulting from the expansion of our call center business and the consolidation of the SPi Group and Level Up! in 2006.

Professional and other contracted services increased by Php522 million, or 125%, to Php938 million primarily due to higher consultancy fees and subcontracted services incurred by the SPi Group related to its BPO services.

Depreciation and amortization charges increased by Php252 million, or 54%, to Php715 million primarily due to an increase in the depreciable asset base in relation to the expansion of our call center business and the consolidation of the SPi Group in July 2006.

Rent expenses increased by Php139 million, or 39%, to Php495 million primarily due to higher office space rentals and leased circuits from other carriers incurred by our call center business, the SPi Group and Level Up!.

Maintenance expenses increased by Php122 million, or 47%, to Php380 million primarily due to higher maintenance costs for new call center facilities plus higher electricity charges for *Vitro*™ and the consolidation of the SPi Group and Level Up!.

Communication, training and travel expenses increased by Php195 million, or 115%, to Php365 million primarily due to the increased cost of phone lines, bandwidth and information system charges, coupled with the increase in local travel costs, mailing and courier charges and freight and hauling charges incurred by our call center and BPO businesses.

Selling and promotion expenses decreased by Php11 million, or 5%, to Php194 million mainly due to the SPi Group's lower advertising and marketing spending.

Cost of sales decreased by Php109 million, or 37%, to Php184 million primarily due to lower software and hardware sales.

Amortization of intangible assets increased by Php143 million to Php162 million in relation to the acquisition of the SPi Group and Level Up!. See *Note 11 - Goodwill and Intangible Assets* to the accompanying unaudited consolidated financial statements for further discussion.

Taxes and licenses increased by Php23 million, or 53%, to Php66 million primarily due to the consolidation of the SPi Group and higher business-related taxes.

Insurance and security services increased by Php13 million, or 62%, to Php34 million primarily due to higher premium costs and an increase in the value of assets insured.

Provisions increased by Php18 million, or 600%, to Php15 million mainly due to anticipated uncollectible accounts.

Financing gains amounted to Php2 million in the first nine months of 2007 primarily due to a gain on derivative transactions; no similar transaction was recorded in the same period in 2006. This was partially offset by higher accretion on financial liabilities particularly on interest expense on contingent consideration.

Other expenses increased by Php84 million, or 88%, to Php179 million mainly due to higher business-related costs, such as office supplies.

*Benefit from Income Tax*

Benefit from income tax amounted to Php73 million in the first nine months of 2007 primarily due to the corresponding deferred tax effect of the amortization of intangible assets in relation to the acquisition of the SPi Group and Level Up!, as compared to Php5 million in the same period in 2006.

### *Net Income*

In the first nine months of 2007, our ICT business segment registered a net income of Php7 million as compared to Php23 million in the same period in 2006 mainly as a result of an 87% increase in ICT expenses mainly from the consolidation of the SPi Group, partly offset by the 84% increase in ICT-related revenues mainly from the consolidation of the SPi Group and increased contribution of our call center business.

### **Liquidity and Capital Resources**

The following table shows our consolidated cash flows for the nine months ended September 30, 2007 and 2006 as well as our consolidated capitalization and other selected financial data as at September 30, 2007 and December 31, 2006:

	<b>Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2007</b>	<b>2006</b>
	(Unaudited)	
<b>(in millions)</b>		
<b>Cash Flows</b>		
Net cash provided by operating activities	Php55,499	Php56,146
Net cash used in investing activities	19,557	25,261
<i>Capital expenditures</i>	<i>14,529</i>	<i>16,872</i>
Net cash used in financing activities	43,980	41,763
Net decrease in cash and cash equivalents	8,399	11,399
	<b>September</b>	<b>December</b>
	<b>30,</b>	<b>31,</b>
	<b>2007</b>	<b>2006</b>
	(Unaudited)	(Audited)
<b>(in millions)</b>		
<b>Capitalization</b>		
Long-term portion of interest-bearing financial liabilities net of current portion:		
Long-term debt	Php57,273	Php63,769
Obligations under capital lease	26	106
Preferred stock subject to mandatory redemption		1,369

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	57,299	65,244
Current portion of interest-bearing financial liabilities:		
Notes payable	487	201
Long-term debt maturing within one year	6,965	16,184
Obligations under capital lease maturing within one year	911	924
Preferred stock subject to mandatory redemption	1,114	
	9,477	17,309
Total interest-bearing financial liabilities	66,776	82,553
Total equity	103,692	104,523
	Php170,468	Php187,076
<b>Other Financial Data</b>		
Total assets	Php227,971	Php241,892
Property, plant and equipment - net	159,288	164,190
Cash and cash equivalents	8,471	16,870

As at September 30, 2007, our consolidated cash and cash equivalents totaled Php8,471 million. Principal sources of consolidated cash and cash equivalents in the first nine months of 2007 were cash flows from operating activities amounting to Php55,499 million and drawings from Smart s, PLDT s and ePLDT s debt facilities aggregating Php5,429 million. These funds were used principally for dividend payments of Php28,394 million, capital outlays of Php14,529 million, total debt principal payments of Php16,294 million, interest payments of Php4,423 million and short-term investments of Php3,553 million.

### *Operating Activities*

Our consolidated net cash flows from operating activities decreased by Php647 million, or 1%, to Php55,499 million in the first nine months of 2007 from Php56,146 million in the same period in 2006. A significant portion of our cash flow is generated by our wireless business, which contributed approximately 60% of our total revenues and other income in the first nine months of 2007 and 2006. Revenues from our fixed line and ICT services accounted for 33% and 7%, respectively, of our total revenues and other income in the first nine months of 2007 compared to 36% and 4%, respectively, in the same period in 2006.

Cash flows from operating activities of our wireless business amounted to Php34,502 million in the first nine months of 2007, an increase of Php4,620 million, or 15%, compared to Php29,882 million in the same period in 2006. The increase in our wireless business segment s cash flows from operating activities was primarily due to the decrease in our working capital requirements owing to the settlement of various payables in 2006. Likewise, cash flows from operating activities of our fixed line business increased to Php18,825 million due to lower working capital requirements in the first nine months of 2007, compared to Php15,476 million in the same period in 2006. We believe that our continuing strong cash flows from operating activities on a consolidated basis will allow us to defray our current liabilities despite our current ratio being less than 1:1 as at September 30, 2007.

Until April 2006, Smart was subject to loan covenants that restricted its ability to pay dividends, redeem preferred shares, make distributions to PLDT or otherwise provide funds to PLDT or any associate without the consent of its lenders. Smart was able to obtain waivers from Finnvera and certain of its lenders for all dividend payments made by Smart to PLDT up to March 2006. Dividend payments made by Smart to PLDT after April 2006 did not require prior creditor consent as all loan facilities that contain such restrictions have already been repaid. Cash dividends paid by Smart to PLDT for the nine months ended September 30, 2007 and 2006 amounted to Php26,927 million and Php20,600 million, respectively.

On September 17, 2007, Piltel paid cash dividends to various preferred shareholders in the aggregate amount of Php2,746 million, of which Php2,734 million was paid to PLDT.

### *Investing Activities*

Net cash used in investing activities amounted to Php19,557 million in the first nine months of 2007, a decrease of Php5,704 million, or 23%, compared to Php25,261 million in the same period in 2006. This was primarily a net result of: (1) the increase in short-term investments by Php3,594 million in the first nine months of 2007 mainly due to Smart's increased investment in money market placements with over 90 days maturity; (2) a decrease in capital expenditures by Php2,343 million; and (3) lower investment acquisition by Php8,437 million. However, we expect capital expenditures to be higher in the last quarter of 2007.

Our consolidated capital expenditures in the first nine months of 2007 totaled Php14,529 million, a decrease of Php2,343 million, or 14%, from Php16,872 million in the same period in 2006 primarily due to Smart's and ePLDT's lower capital spending. Smart's capital spending of Php6,981 million in the first nine months of 2007 was used primarily to further upgrade its core, access and transmission network facilities, expand its wireless broadband facilities and develop IT platforms for new businesses. PLDT's capital spending of Php7,118 million was principally used to finance the expansion and upgrade of its submarine cable facilities, fixed line data and IP-based network services. ePLDT and its subsidiaries' capital spending of Php394 million was primarily used to fund its continued call center expansion. The balance represented other subsidiaries' capital spending. Consolidated capital expenditures in the first nine months of 2006 amounted to Php16,872 million, of which Php9,163 million, Php6,881 million and Php737 million were attributable to Smart, PLDT and ePLDT, respectively.

### *Financing Activities*

On a consolidated basis, we used net cash of Php43,980 million for financing activities, net of loan drawings by Smart, in the first nine months of 2007, an increase of Php2,217 million, or 5%, compared to Php41,763 million in the same period in 2006. The net cash used in financing activities was mainly utilized for debt repayments, interest payments, and dividend payments distributed to PLDT common and preferred stockholders.

*Debt Financing*

Additions to our consolidated long-term debt in the first nine months of 2007 totaled Php5,429 million mainly from Smart's drawings related to the financing of its network expansion projects. Payments in respect of principal and interest of our total debt amounted to Php16,294 million and Php4,423 million, respectively, in the first nine months of 2007, of which Php11,343 million and Php3,256 million were attributable to PLDT, respectively.

The following table shows our long-term debt, including current portion, as at September 30, 2007 and December 31, 2006:

	September 30, December 31,		Increase (Decrease)	
	2007 (Unaudited)	2006 (Audited)	Amount	%
<b>(in millions)</b>				
U.S. Dollar Debt:				
Export Credit Agencies-Supported Loans	Php9,321	Php14,981	(Php5,660)	(38)
Fixed Rate Notes	30,410	40,971	(10,561)	(26)
Term Loans	15,399	18,611	(3,212)	(17)
Satellite Acquisition Loans	1,342	2,083	(741)	(36)
	56,472	76,646	(20,174)	(26)
Philippine Peso Debt:				
Peso Fixed Rate Corporate Notes	4,988	808	4,180	517
Term Loans	2,778	2,499	279	11
	7,766	3,307	4,459	135
	Php64,238	Php79,953	(Php15,715)	(20)

For a complete discussion of our long-term debt, see *Note 17 Interest-bearing Financial Liabilities Long-term Debt* to the accompanying unaudited consolidated financial statements.

Our long-term debt decreased by Php15,715 million, or 20%, to Php64,238 million as at September 30, 2007, largely due to debt amortizations and prepayments in line with our efforts to reduce overall debt level, and also due to the appreciation of the peso. The debt levels of Mabuhay, ePLDT, PLDT and Smart decreased by 36%, 35%, 27% and 2% to Php1,342 million, Php37 million, Php38,036 million and Php24,824 million, respectively, as at September 30, 2007.

On May 22, 2007, PLDT signed loan agreements with The Philippine American Life and General Insurance Company for Php400 million and The Philam Bond Fund, Inc. for Php20 million to refinance their respective participations in the Ten-Year Note under the Php1,270 million Peso Fixed Rate Corporate Notes which were repaid on June 12, 2007.



Both loans will mature on June 12, 2014.

On February 15, 2007 Smart issued Php5 billion unsecured fixed rate corporate notes, made up of Series A notes amounting to Php3.8 billion and Series B notes amounting to Php1.2 billion with five and ten year terms, respectively. Series A notes were priced at 5.625%, while Series B notes were priced at 6.500%. Funds raised from the issuance of these notes will be used primarily for Smart's capital expenditures for network improvement and expansion.

On October 16, 2006, Smart signed a U.S. Dollar Term Loan Facility with Metropolitan Bank and Trust Company to finance the related Phase 9 GSM Facility for an amount of US\$50 million. This loan facility was drawn in full on October 10, 2007. Please see *Note 17 Interest-bearing Financial Liabilities - Long-term Debt* to the accompanying unaudited consolidated financial statements for a detailed discussion of our long-term debt.

The scheduled maturities of our outstanding consolidated long-term debt at nominal values as at September 30, 2007 are as follows:

Year (Unaudited)	US\$ Loans (in millions)	Peso Loans	Total	
2007(1)	US\$40	Php1,803	Php139	Php1,942
2008	147	6,608	558	7,166
2009	263	11,830	570	12,400
2010	71	3,183	568	3,751
2011	15	668	568	1,236
2012 and onwards	830	37,335	5,384	42,719
	US\$1,366	Php61,427	Php7,787	Php69,214

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(1) October 1, 2007 through December 31, 2007.

Approximately Php26,495 million principal amount of our consolidated outstanding long-term debt as at September 30, 2007 is scheduled to mature over the period from 2007 to 2011. Of this amount, Php13,317 million was attributable to PLDT, Php11,800 million to Smart and the remainder to Mabuhay Satellite and ePLDT.

#### *Debt Covenants*

Our debt instruments contain restrictive covenants, including covenants that could prohibit us from paying dividends on common stock under certain circumstances, and require us to comply with specified financial ratios and other financial tests, calculated in conformity with Philippine Financial Reporting Standards, at relevant measurement dates, principally at the end of each quarterly period. We have complied with all of our maintenance financial ratios as required under our loan covenants and other debt instruments.

Please see *Note 17 Interest-bearing Financial Liabilities Debt Covenants* to the accompanying unaudited consolidated financial statements for a detailed discussion of our covenants.

### *Financing Requirements*

We believe that our available cash, including cash flow from operations, will provide sufficient liquidity to fund our projected operating, investment, capital expenditures and debt service requirements for the next 12 months.

As a result of our improving cash flows and reduced debt levels, we currently intend to gradually increase our dividend payout ratio as we improve our leverage ratios. For 2006, our dividend payout ratio was 60% of 2006 earnings per share, excluding the special dividend discussed below, which we intend to increase to 70% in 2007.

On August 7, 2007, we declared a special dividend of Php40 per share attributable to our 2006 earnings. This special dividend is an incremental dividend payout representing approximately 25% of our 2006 earnings per share. As a result of such special dividend declaration, our total dividend payments attributable to our 2006 earnings increased to Php140 per share, inclusive of the regular dividends paid out of our 2006 earnings aggregating Php100 per share.

The following table sets forth the dividend declaration, on PLDT's common stock pertaining to 2006 and 2007 earnings:

<b>Earnings</b>	<b>Approved</b>	<b>Date Record</b>	<b>Payable</b>	<b>Amount</b>	
				<b>Per share</b>	<b>Total (in millions)</b>
2006	August 8, 2006	August 21, 2006	September 21, 2006	Php50	Php9,379
2006	March 6, 2007	March 20, 2007	April 20, 2007	50	9,429
2006	August 7, 2007	August 24, 2007	September 24, 2007	40	7,548
				Php140	Php26,356
2007	August 7, 2007	August 24, 2007	September 24, 2007	Php60	Php11,322

*Credit Ratings*

None of our existing indebtedness contains provisions under which credit rating downgrades would trigger a default, changes in applicable interest rates or other similar terms and conditions.

PLDT's current credit ratings are as follows:

<b><u>Rating Agency</u></b>	<b><u>Credit Rating</u></b>	<b><u>Outlook</u></b>
Moody's Investor Service, or Moody's	Foreign Currency Senior Unsecured Debt Rating	Ba2 Stable
	Local Currency Corporate Family Rating	Baa2 Stable
Fitch Ratings, or Fitch	Long-term Foreign Currency Rating	BB+ Stable
	Long-term Local Currency Rating	BB+ Stable
	Long-term Foreign Currency Issuer Default Rating, or IDR	BB+ Stable
	Long-term Local Currency Issuer Default Rating	BBB Stable
	National Long-term Rating	AAA(ph1) Stable

On August 14, 2007, Fitch upgraded PLDT's long-term local currency IDR to BBB from BBB- with a stable outlook and at the same time affirmed PLDT's long-term foreign currency IDR of BB+ with a stable outlook, PLDT's global bonds and senior notes at BB+. The rating action recognizes PLDT's sustained strengthening financial profile through 2006 and the first half of 2007, with a strong positive free cash flow generation enabling significant reductions in both gross and net debt levels. The upgrade also reflects our sustained strong operating performance and its pre-eminent position in the Philippine telecommunications sector.

On May 31, 2007, Moody's upgraded our local currency corporate family rating to Baa2 with a stable outlook from Baa3. At the same time, Moody's affirmed our foreign currency senior unsecured debt rating at Ba2 with a stable outlook. This rating action concluded the review for possible upgrade that Moody's commenced on April 11, 2007. The upgrade reflects the continued improvement in our financial profile and the consolidation of our strong operating performance.

*Equity Financing*

PLDT raised Php74 million and Php57 million from the exercise by certain officers and executives of stock options in the first nine months of 2007 and 2006, respectively.



*Long-term Operating Lease Obligations*

**Digital Passage Service Contracts.** PLDT has existing Digital Passage Service Contracts with foreign telecommunication administrations for several dedicated circuits to various destinations for 10 to 25 years expiring at various dates. As at September 30, 2007, PLDT's aggregate remaining obligation under these contracts amounted to approximately Php4 million.

**License Agreement with Mobius Management Systems (Australia) Pty Ltd., or Mobius.** PLDT entered into a license agreement with Mobius pursuant to which Mobius has granted PLDT a non-exclusive, non-assignable and non-transferable license for the use of computer software components. Under this agreement, Mobius is also required to provide maintenance services for a period of one year at no additional maintenance charge. PLDT may purchase maintenance services upon expiration of the first year for a fee of 15% of the current published license fee. As at September 30, 2007, PLDT's aggregate remaining obligation under this agreement was approximately Php20 million.

**Other Long-term Operating Lease Obligations.** The PLDT Group has various long-term lease contracts for periods ranging from two to ten years covering certain offices, warehouses, cell sites telecommunication equipment locations and various office equipment. In particular, Smart has lease obligations amounting to Php3,181 million as at September 30, 2007 in respect of office and cell site rentals with over 3,000 lessors nationwide, PLDT has lease obligations amounting to Php78 million as at September 30, 2007 in respect of office and lot rentals with over 175 lessors nationwide, ePLDT has lease obligations amounting to Php183 million as at September 30, 2007 in respect of certain office space rentals and PLDT Global has lease obligations amounting to Php45 million as at September 30, 2007 in respect of certain office space rentals.

*Long-term Capital Lease Obligations*

For a discussion of our long-term capital lease obligations, see *Note 17 Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements.

*Unconditional Purchase Obligations*

**Air Time Purchase Agreement with AIL.** PLDT was a party to a Founder National Service Provider, or NSP, ATPA, entered into with AIL in March 1997, which was amended in December 1998 (as amended, the Original ATPA), under which PLDT was granted the exclusive right to sell AIL services as NSP in the Philippines. In exchange, the Original ATPA required PLDT to purchase from AIL a minimum of US\$5 million worth of air time (the Minimum Air Time Purchase Obligation) annually over ten years commencing January 1, 2002 (the Minimum Purchase Period),

the purported date of commercial operations of Garuda I Satellite. In the event that AIL's aggregate billed revenue is less than US\$45 million in any given year, the Original ATPA also required PLDT has to make supplemental air time purchase payments not to exceed US\$15 million per year during the Minimum Purchase Period (the Supplemental Air Time Purchase Obligation).

After lengthy negotiations including a collaboration arrangement with Inmarsat, AIL and ACeS signed a term sheet (Banks Term Sheet) in September 2006 (as amended in October 2006, November 2006 and February 2007) with the majority of AIL's bank creditors. The Banks Term Sheet was used as the basis for negotiations amongst the parties to amend the Amended Credit Agreement. Under the Banks Term Sheet, a majority of the banks agreed, subject to the satisfaction of certain conditions, among other things to amend the Original ATPA as set forth in an attachment to the Banks Terms Sheet and to restructure AIL's indebtedness. For further discussion please see *Note 20 Related Party Transactions* to the accompanying unaudited consolidated financial statements.

As at September 30, 2007, PLDT's aggregate remaining minimum obligation under the amended ATPA was approximately Ph796 million.

#### *Other Long-term Obligations*

***Mandatory Conversion and Purchase of Shares.*** As discussed in *Note 17 Interest-bearing Financial Liabilities*, as at September 30, 2007, PLDT had issued a total of 3 million shares of Series V Convertible Preferred Stock, 5 million shares of Series VI Convertible Preferred Stock and 4 million shares of Series VII Convertible Preferred Stock in exchange for a total of 58 million shares of Series K Class I Convertible Preferred Stock of Piltel, pursuant to the debt restructuring plan of Piltel adopted in June 2001. As at September 30, 2007, 2,687,490 shares of Series V Convertible Preferred Stock, 4,588,860 shares of Series VI Convertible Preferred Stock and 3,842,000 shares of Series VII Convertible Preferred Stock had been voluntarily converted to PLDT common shares. As at September 30, 2007, 33,950 shares of Series V and 706,244 shares of Series VI Convertible Preferred Stocks remained outstanding.

Each share of Series V and VI Convertible Preferred Stocks is convertible at any time at the option of the holder into one PLDT common share. On the date immediately following the seventh anniversary of the issue date of the Series V and Series VI Convertible Preferred Stocks, the remaining outstanding shares under these series will be mandatorily converted to PLDT common shares. Under a put option exercisable for 30 days, holders of common shares received on mandatory conversion of the Series V and VI Convertible Preferred Stocks will be able to require PLDT to purchase such PLDT common shares for Ph1,700 per share and US\$36.132 per share, respectively.

The aggregate value of the put option based on outstanding shares as at September 30, 2007 was Ph1,205 million which is puttable on June 4, 2008, if all of the outstanding shares of Series V and VI Convertible Preferred Stocks were mandatorily converted and all the common shares were put to PLDT at that time. The market value of the underlying common shares was Ph2,154 million, based on the market price of PLDT common shares of Ph2,910 per share as at September 30, 2007.

Please refer to *Note 17 Interest-bearing Financial Liabilities Preferred Stock Subject to Mandatory Redemption* to the accompanying unaudited consolidated financial statements for further discussion.

### *Commercial Commitments*

As at September 30, 2007, our outstanding commercial commitments, in the form of letters of credit, amounted to Php1,846 million. These commitments will expire within one year.

### **Quantitative and Qualitative Disclosures about Market Risks**

Our operations are exposed to various risks, including liquidity risk, foreign exchange risk and interest rate risk. The importance of managing these risks has significantly increased in light of considerable change and continuing volatility in both the Philippine and international financial markets. With a view to managing these risks, we have incorporated financial risk management functions in our organization, particularly in our treasury operations and equity issues and sales of certain assets.

#### *Liquidity Risk Management*

We seek to manage our liquidity profile to be able to finance our capital expenditures and service our maturing debts. To cover our financing requirements, we currently intend to use internally generated funds and proceeds from debt and equity issues and sales of certain assets.

As part of our liquidity risk management program, we regularly evaluate our projected and actual cash flow information and continuously assess conditions in the financial markets for opportunities to pursue fund-raising initiatives. These initiatives may include bank loans, export credit agency-guaranteed facilities, and debt capital and equity market issues.

#### *Foreign Exchange Risk Management*

The revaluation of our foreign-currency denominated assets and liabilities as a result of the appreciation or depreciation of the Philippine peso is recognized as foreign exchange gains or losses as at the balance sheet date. The

extent of foreign exchange gains or losses is largely dependent on the amount of foreign currency debt and hedges we carry. While a certain percentage of our revenues are either linked to or denominated in U.S. dollars, most of our indebtedness and related interest expense, a substantial portion of our capital expenditures and a portion of our operating expenses are denominated in foreign currencies, mostly in U.S. dollars. As such, a strengthening or weakening of the Philippine peso against the U.S. dollar will decrease or increase in Philippine peso terms both the principal amount of our unhedged foreign currency-denominated debts and the related interest expense, our foreign currency-denominated capital expenditures and operating expenses as well as our U.S. dollar linked and U.S. dollar denominated revenues. In addition, many of our financial ratios and other financial tests are affected by the movements in the Philippine peso to U.S. dollar exchange rate.

To manage our foreign exchange risks, stabilize cash flows, and improve investment and cash flow planning, we enter into forward foreign exchange contracts, currency swap contracts, currency option contracts and other hedging products aimed at reducing and/or managing the adverse impact of changes in foreign exchange rates on our operating results and cash flows. However, these hedges do not cover all of our exposure to foreign exchange risks. Specifically, we use forward foreign exchange contracts, currency swap contracts, foreign currency option contracts to manage the foreign exchange risks associated with our foreign currency-denominated loans. In order to manage hedge costs of these contracts, we utilize structures that include credit-linkage with PLDT as the reference entity, a combination of foreign currency option contracts, and fixed to floating coupon only swap agreements. We accounted for these instruments as either cash flow hedges, wherein changes in the fair value are recognized as cumulative translation adjustments in equity until when the hedged transaction affects the consolidated statement of income or when the hedging instrument expires, or transactions not designated as hedges, wherein changes in the fair value are recognized directly as income or expense for the period.

As at September 30, 2007, approximately 89% of our total consolidated debts was denominated in U.S. dollars. Consolidated foreign currency-denominated debt was reduced to Php56,472 million from Php81,850 million as at September 30, 2006. PLDT's outstanding long-term principal only currency swap contracts and foreign currency option contracts amounted to US\$550 million and US\$136 million, respectively, as at September 30, 2007. Consequently, the unhedged portion of consolidated debts amounts is approximately 45% or 38%, net of our U.S. dollar cash balances as at September 30, 2007.

For the nine months ended September 30, 2007, approximately 38% of our consolidated revenues are either denominated in U.S. dollars or are linked to the U.S. dollars. In this respect, the recent appreciation of the peso against the U.S. dollar reduced our revenues, and consequently, our cash flow from operations in peso terms.

The Philippine peso had appreciated by 8% against the U.S. dollar to Php44.974 to US\$1.00 as at September 30, 2007, from Php49.045 to US\$1.00 as at December 31, 2006. Likewise, as at September 30, 2006, the peso had appreciated by 5% to Php50.249 to US\$1.00 from Php53.062 to US\$1.00 as at December 31, 2005. As a result of the foreign exchange movements as well as the amount of our outstanding foreign currency debts and hedges, we recognized foreign exchange gains of Php1,662 million and Php1,601 million in the first nine months of 2007 and 2006, respectively.



For further discussions of these contracts, see *Note 24 Financial Assets and Liabilities Derivative Financial Instruments* to the accompanying unaudited consolidated financial statements.

### ***Interest Rate Risk Management***

On a limited basis, we enter into interest rate swap agreements in order to manage our exposure to interest rate fluctuations. As at September 30, 2007, PLDT's outstanding interest rate swap contracts amounted to US\$31 million. For further discussions of these contracts, see *Note 24 Financial Assets and Liabilities Derivative Financial Instruments* to the accompanying unaudited consolidated financial statements.

We make use of hedging instruments and structures solely for reducing or managing financial risks associated with our liabilities and not for trading or speculative purposes.

### **Impact of Inflation and Changing Prices**

Inflation can be a significant factor in the Philippine economy, and we are continually seeking ways to minimize its impact. In recent periods, we do not believe inflation has had a material impact on our operations. The average inflation rate in the Philippines in the first nine months of 2007 was 2.6%, compared to 6.8% in the same period in 2006.

## **PART II OTHER INFORMATION**

### ***Sale and transfer of Piltel's Fixed Line Business to PLDT***

On November 5, 2007, Piltel's Board of Directors approved the sale and transfer of Piltel's fixed line business to PLDT or any of its subsidiaries which provides fixed line service, subject to the execution of a definitive agreement and fulfillment of certain closing conditions including the procurement of the requisite regulatory approvals. The sale and transfer will allow Piltel to concentrate its resources on its wireless business. It will also bring together the PLDT Group's LEC businesses such that these LEC businesses can derive operating efficiencies while extending to Piltel's fixed line subscribers the opportunity to benefit from the upgrades being undertaken at PLDT. PLDT has been managing Piltel's fixed line business since July 2001 under a Facilities Management Agreement, or FMA

***Consent Solicitation for the US\$250 Million 11.375% Notes due 2012, and Consent Solicitation for the US\$175 Million 10.5% Notes due 2009 and US\$300 Million 8.35% Notes due 2017***

On November 6, 2007, PLDT commenced a solicitation of consents from holders of its outstanding 11.375% Notes due 2012, or the 2012 Notes, to effect certain proposed amendments relating to the limitation on restricted payments and limitation on dividends and a solicitation of consents from holders of its outstanding 10.5% Notes due 2009, or the 2009 Notes, and 8.35% Notes due 2017, or the 2017 Notes, to effect certain proposed amendments relating to the limitation on dividends.

Specifically, the proposed amendments, once effective, would give PLDT greater flexibility to make certain restricted payments, amend limitations on PLDT paying dividends or distributions, and reduce PLDT's permitted leverage ratios pursuant to the terms of the notes.

PLDT's key financial indicators including revenues, profitability and operating cash flows have improved over time compared to when the notes were issued. PLDT is focused on maintaining its market leadership, investing in new growth areas to boost its core telecommunications business and diversifying its revenue sources. PLDT is also focused on pursuing an efficient capital structure by adjusting its dividend and distribution policy to maintain an optimal level of cash on its balance sheet. PLDT believes that the existing Limitation on Restricted Payments and the existing Limitation on Dividends, constrain its ability to pursue these objectives. To demonstrate its continued commitment to maintaining a prudent capital structure, PLDT will simultaneously tighten its debt capacity.

***Incorporation of SPi Global Solutions Corporation, or SPi Global***

On October 5, 2007, the Philippine SEC approved the incorporation of SPi Global, a wholly-owned subsidiary of ePLDT. SPi Global will be the holding company of the BPO voice and non-voice businesses of ePLDT.

***Related Party Transactions***

***a. Air Time Purchase Agreement between PLDT and AIL and Related Agreements***

For a more detailed discussion on the ATPA, see *Contractual Obligations and Commercial Commitments Unconditional Purchase Obligations* *Air Time Purchase Agreement with AIL* .

*b. Transactions with Major Stockholders, Directors and Officers*

Transactions to which PLDT or any of its subsidiaries is a party, in which a director, key officer or owner of more than 10% of the outstanding common stock of PLDT, or any member of the immediate family of a director, key officer or owner of more than 10% of the outstanding common stock of PLDT had a direct or indirect material interest, as at September 30, 2007 (unaudited) and December 31, 2006 (audited) and for the nine months ended September 30, 2007 and 2006 (unaudited) are as follows:

*Cooperation Agreement with First Pacific and certain affiliates, or the FP Parties, NTT Communications and DoCoMo* In connection with the transfer by NTT Communications of approximately 12.6 million shares of PLDT's common stock to DoCoMo pursuant to a Stock Sale and Purchase Agreement dated January 31, 2006 between NTT Communications and DoCoMo, the FP Parties, NTT Communications and DoCoMo entered into a Cooperation Agreement, dated January 31, 2006. Under the Cooperation Agreement, the relevant parties extended certain rights of NTT Communications under the Stock Purchase and Strategic Investment Agreement dated September 28, 1999, as amended, and the Shareholders Agreement dated March 24, 2000, to DoCoMo, including:

- certain contractual veto rights over a number of major decisions or transactions; and
- rights relating to the representation on the board of directors of PLDT and Smart, respectively, and any committees thereof.

Key provisions of the Cooperation Agreement pertain to, among other things, restrictions on the ownership of shares of PLDT by NTT Communications and DoCoMo, limitation on competition, business cooperation, additional rights of DoCoMo, change in control and termination. See *Note 20 Related Party Transactions* to the accompanying unaudited consolidated financial statements for further details.

*Integrated i-mode Services Package Agreement between DoCoMo and Smart* An Integrated i-mode Services Package Agreement was entered into by Smart and DoCoMo on February 15, 2006, under which DoCoMo agreed to grant Smart, on an exclusive basis within the territory of the Philippines for a period of five years, an integrated i-mode services package including a non-transferable license to use the licensed materials and the i-mode brand, as well as implementation support and assistance and post-commercial launch support from DoCoMo. Pursuant to this agreement, Smart is required to pay an initial license fee and running royalty fees based on the revenue arising from i-mode subscription fees and data traffic. Outstanding obligation under this agreement amounted to Php53 million as at December 31, 2006. Smart has no outstanding obligation under this agreement as at September 30, 2007.

*Advisory Services Agreement between DoCoMo and PLDT* An Advisory Services Agreement was entered into by DoCoMo and PLDT on June 5, 2006, in accordance with the Cooperation Agreement dated January 31, 2006.

Pursuant to the Advisory Services Agreement, DoCoMo will provide the services of certain key personnel in connection with certain aspects of the business of PLDT and Smart. Also, said agreement governs the terms and conditions of the appointments of such key personnel and the corresponding fees related thereto. Total fees under this agreement amounted to Php56 million and Php25 million for the nine months ended September 30, 2007 and 2006, respectively. Outstanding liability under this agreement amounted to Php18 million and Php32 million as at September 30, 2007 and December 31, 2006, respectively.

*Other Agreements with NTT Communications and/or its Affiliates* Under certain agreements, (1) NTT Communications provides advisory services for various business areas of PLDT; (2) PLDT is licensed to market managed data and other services using NTT Communications Arcstar brand; and (3) PLDT and NTT Communications agreed to cooperative arrangements for conventional international telecommunications services. Total fees under these agreements totaled Php83 million and Php144 million for the nine months ended September 30, 2007 and 2006, respectively. PLDT's outstanding obligations under these agreements amounted to Php18 million as at September 30, 2007 and December 31, 2006.

*Agreement between Smart and Asia Link B.V., or ALBV.* Smart has an existing Technical Assistance Agreement with ALBV, a subsidiary of the First Pacific Group, for the latter's provision of technical support services and assistance in the operations and maintenance of cellular business for a period of five years, subject to renewal upon mutual agreement between the parties. The agreement provides for quarterly payments of technical service fees equivalent to 2% of the net revenues of Smart. In January 2004, the agreement was amended, reducing the technical service fees to be paid by Smart to ALBV to 1% of net revenues effective January 1, 2004. On February 18, 2004, Smart and ALBV entered into a renewal of the Technical Assistance Agreement extending the effectivity of the terms thereof to February 23, 2008. Furthermore, in view of the acquisition by Smart of ownership of 92.1% of the outstanding common stock of Piltel held by PLDT, the parties agreed to make the consolidated net revenues of Smart the basis for the computation of the 1% technical service fees payable by Smart to ALBV, effective January 1, 2005. Total service fees charged to operations under this agreement amounted to Php449 million and Php398 million for the nine months ended September 30, 2007 and 2006, respectively. As at September 30, 2007, Smart had advanced the payment of service fees to ALBV amounting to Php151 million. As at December 31, 2006, Smart had an outstanding liability to ALBV of Php128 million.

Smart also has an existing Services Agreement with ALBV for a period of 25 years starting January 1, 1999, which will automatically expire unless renewed by mutual agreement of both parties. Under the agreement, ALBV provides advice and assistance to Smart in sourcing capital equipment and negotiating with international suppliers, arranging international financing and other services therein consistent with and for the furtherance of the objectives of the services. Service agreement fees were paid for the whole 25-year period. Outstanding prepaid management fees as at September 30, 2007 and December 31, 2006 amounted to Php830 million and Php869 million, respectively. Financing service fee charged to operations amounted to Php38 million each for the nine months ended September 30, 2007 and 2006.

*Agreements relating to insurance companies* Gotuaco del Rosario and Associates, or Gotuaco, acts as the broker for certain insurance companies to cover certain insurable properties of the PLDT Group. Insurance premiums are remitted to Gotuaco and the broker's fees are settled between Gotuaco and the insurance companies. In addition, PLDT has an insurance policy with Malayan Insurance Co., Inc., or Malayan, wherein premiums are directly paid to

Malayan. Total insurance expenses under these agreements amounted to Php168 million and Php189 million for the nine months ended September 30, 2007 and 2006, respectively. Two directors of PLDT have direct/indirect interests in or serve as a director/officer of Gotuaco and Malayan.

For a more detailed discussion of the related party transactions enumerated above, see *Note 20 Related Party Transactions* to the accompanying unaudited consolidated financial statements.





## ANNEX AGING OF ACCOUNTS RECEIVABLE

The following table shows the aging of unaudited consolidated trade receivables as at September 30, 2007:

Type of Accounts Receivable	Total	Current	31-60 Days	61-90 Days	Over 91 Days
(In Millions)					
<b>I. Trade Receivables</b>					
1. Retails subscribers	Php8,535	Php1,776	Php976	Php246	Php5,537
2. Foreign administrations	4,466	1,338	1,128	509	1,491
3. Corporate subscribers	7,443	767	981	490	5,205
4. Domestic carriers	1,858	444	98	98	1,218
5. Dealers and agents	2,348	1,694	94	148	412
Subtotal	Php24,650	Php6,019	Php3,277	Php1,491	Php13,863
<b>II. Non-Trade Receivables</b>					
	1,641				
		Less: Allowance for doubtful accounts		Less: Allowance for doubtful accounts	
Total	26,291				
Less: Allowance for doubtful accounts	16,046				
<b>Total Receivables - net</b>	<b>Php10,245</b>				







**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**

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AS AT SEPTEMBER 30, 2007 (UNAUDITED) AND DECEMBER 31, 2006 (AUDITED)  
AND FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 (UNAUDITED)

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES**

## CONSOLIDATED BALANCE SHEETS

(in million pesos, except par value and per share amounts)

	September 30, 2007 (Unaudited)	December 31, 2006 (Audited)
<b><u>ASSETS</u></b>		
<b>Noncurrent Assets</b>		
Property, plant and equipment - net (Notes 2, 3, 8 and 17)	159,288	164,190
Investments in associates (Notes 2, 9 and 17)	1,343	636
Investments-available-for-sale (Notes 2 and 24)	142	116
Investment in debt securities (Notes 2 and 24)	268	
Investment properties (Notes 2, 3 and 10)	580	587
Goodwill and intangible assets (Notes 2, 3 and 11)	13,701	12,214
Deferred income tax assets (Notes 2, 4 and 6)	13,808	19,658
Derivative financial assets (Notes 2 and 24)	93	434
Prepayments - net of current portion	799	843
Advances and refundable deposits - net of current portion (Notes 2 and 20)	1,413	1,066
<b>Total Noncurrent Assets</b>	<b>191,435</b>	<b>199,744</b>
<b>Current Assets</b>		
Cash and cash equivalents (Notes 2, 13 and 24)	8,471	16,870
Short-term investments (Notes 2 and 24)	11,522	8,327
Trade and other receivables (Notes 2, 3, 14 and 24)	10,245	10,158
Inventories and supplies (Notes 2 and 15)	1,641	1,230
Derivative financial assets (Notes 2 and 24)	80	47
Current portion of prepayments	4,385	5,360
Current portion of advances and refundable deposits (Notes 2 and 20)	192	156
<b>Total Current Assets</b>	<b>36,536</b>	<b>42,148</b>
<b>TOTAL ASSETS</b>	<b>227,971</b>	<b>241,892</b>
<b><u>EQUITY AND LIABILITIES</u></b>		
<b>Equity Attributable to Equity Holders of PLDT (Notes 2, 7 and 16)</b>		
Preferred stock, Php10 par value, authorized - 822,500,000 shares; issued and outstanding - 441,819,482 shares as at September 30, 2007 and 442,375,057 shares as at December 31, 2006	4,418	4,424
Common stock, Php5 par value, authorized - 234,000,000 shares; issued and outstanding - 188,708,152 shares as at September 30, 2007 and 188,434,695 shares as at December 31, 2006	944	942
Stock options issued (Note 21)	10	40
Equity portion of convertible preferred stock (Note 17)	9	9
Capital in excess of par value	66,998	66,574
Retained earnings (Note 7)	30,614	32,784

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Cumulative translation adjustments (Note 24)	<b>(1,223)</b>	(1,796)
Total Equity Attributable to Equity Holders of PLDT	<b>101,770</b>	102,977
<b>Minority interest</b>	<b>1,922</b>	1,546
Total Equity	<b>103,692</b>	104,523

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS *(continued)*

(in million pesos, except par value and per share amounts)

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
<b>Noncurrent Liabilities</b>		
Interest-bearing financial liabilities - net of current portion (Notes 2, 8, 17, 22 and 24)	<b>57,299</b>	65,244
Deferred income tax liabilities (Notes 2, 4 and 6)	<b>523</b>	402
Derivative financial liabilities (Notes 2 and 24)	<b>6,800</b>	6,872
Pension and other employee benefits (Notes 2, 3 and 21)	<b>3,855</b>	2,982
Customers deposits	<b>2,210</b>	2,204
Other noncurrent liabilities (Notes 2, 3, 8, 14 and 18)	<b>8,885</b>	7,581
Total Noncurrent Liabilities	<b>79,572</b>	85,285
<b>Current Liabilities</b>		
Accounts payable (Notes 2 and 24)	<b>12,042</b>	8,634
Accrued expenses and other current liabilities (Notes 2, 3, 17, 19, 20 and 21)	<b>15,933</b>	19,102
Unearned revenues (Note 2)	<b>3,334</b>	3,274
Derivative financial liabilities (Notes 2 and 24)	<b>15</b>	108
Provisions for assessments (Notes 20, 22 and 23)	<b>474</b>	446
Current portion of interest-bearing financial liabilities (Notes 2, 8, 17, 22 and 24)	<b>9,477</b>	17,309
Dividends payable (Notes 2, 7, 17 and 24)	<b>1,068</b>	773
Income tax payable (Notes 2 and 6)	<b>2,364</b>	2,438
Total Current Liabilities	<b>44,707</b>	52,084
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>227,971</b>	241,892

*See accompanying Notes to Unaudited Consolidated Financial Statements.*

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME****(in million pesos, except per share amounts)**

	<b>Nine Months Ended September 30, 2007 2006</b>		<b>Three Months Ended September 30, 2007 2006</b>	
	(Unaudited)			
<b>INCOME</b>				
Service revenues (Note 4)	<b>100,470</b>	92,003	<b>33,449</b>	31,364
Non-service revenues (Notes 4 and 5)	<b>1,860</b>	2,160	<b>543</b>	696
Equity share in net income of associates (Note 4)		1		(2)
Other income (Note 4)	<b>1,138</b>	1,236	<b>685</b>	900
	<b>103,468</b>	95,400	<b>34,677</b>	32,958
<b>EXPENSES</b>				
Depreciation and amortization (Notes 4 and 8)	<b>18,952</b>	23,659	<b>6,076</b>	8,175
Compensation and benefits (Notes 5 and 21)	<b>15,589</b>	13,184	<b>5,736</b>	5,568
Maintenance (Note 20)	<b>5,299</b>	4,890	<b>1,857</b>	1,604
Financing costs (Notes 5, 8, 17 and 24)	<b>3,857</b>	7,230	<b>679</b>	1,096
Selling and promotions	<b>3,855</b>	3,558	<b>1,357</b>	1,098
Cost of sales (Notes 5, 20 and 22)	<b>3,745</b>	4,006	<b>1,111</b>	1,402
Professional and other contracted services (Notes 5 and 20)	<b>3,468</b>	2,227	<b>1,143</b>	987
Rent (Note 22)	<b>2,168</b>	1,769	<b>757</b>	622
Taxes and licenses (Note 23)	<b>1,715</b>	1,288	<b>427</b>	374
Communication, training and travel	<b>1,307</b>	1,038	<b>421</b>	365
Provisions (Notes 3, 5, 14, 15, 20, 22 and 23)	<b>1,144</b>	872	<b>414</b>	102
Insurance and security services (Note 20)	<b>872</b>	973	<b>286</b>	313
Amortization of intangible assets (Note 11)	<b>286</b>	255	<b>105</b>	115
Equity share in net losses of associates	<b>17</b>		<b>9</b>	
Other expenses (Note 20)	<b>1,214</b>	953	<b>310</b>	265
	<b>63,488</b>	65,902	<b>20,688</b>	22,086
<b>INCOME BEFORE INCOME TAX</b>	<b>39,980</b>	29,498	<b>13,989</b>	10,872
<b>PROVISION FOR INCOME TAX</b> (Notes 2, 4 and 6)	<b>13,028</b>	3,131	<b>4,312</b>	145
<b>NET INCOME FOR THE PERIOD</b>	<b>26,952</b>	26,367	<b>9,677</b>	10,727
<b>ATTRIBUTABLE TO:</b>				
Equity holders of PLDT	<b>26,506</b>	25,744	<b>9,505</b>	10,439
Minority interest	<b>446</b>	623	<b>172</b>	288
	<b>26,952</b>	26,367	<b>9,677</b>	10,727
<b>Earnings Per Common Share</b> (Note 7)				



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Basic	<b>138.71</b>	138.71	<b>49.76</b>	55.69
Diluted	<b>138.27</b>	138.58	<b>49.63</b>	55.58

*See accompanying Notes to Unaudited Consolidated Financial Statements.*

## PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(in million pesos)

	Preferred Stock	Common Stock	Stock Options Issued	Equity Portion of Convertible Preferred Stock	Capital in Excess of Par Value	Retained Earnings	Cumulative Translation Adjustments	Equity Attributable to Equity Holders of the Parent	Minority Interest	Total Equity
Balances at January 1, 2006	4,433	904	67	49	53,918	12,583	1,253	73,207	1,162	74,369
Income for the period						25,744		25,744	623	26,367
Foreign currency translation differences (Note 24)							(69)	(69)	(32)	(101)
Net gains on available-for-sale financial assets (Note 24)							5	5		5
Net losses on cash flow hedges (Note 24)							(1,862)	(1,862)		(1,862)
Total income and expense for the period recognized directly to equity							(1,926)	(1,926)	(32)	(1,958)
<b>Total income and expense for the period</b>						<b>25,744</b>	<b>(1,926)</b>	<b>23,818</b>	<b>591</b>	<b>24,409</b>
<b>Cash dividends</b>						<b>(14,779)</b>		<b>(14,779)</b>		<b>(14,779)</b>
<b>Issuance of capital stock net (Note 16)</b>	<b>(6)</b>	<b>36</b>		<b>(40)</b>	<b>11,846</b>			<b>11,836</b>		<b>11,836</b>
<b>Exercised shares</b>			<b>(24)</b>		<b>81</b>			<b>57</b>		<b>57</b>
<b>Minority interest</b>									<b>8</b>	<b>8</b>
<b>Balances at September 30, 2006 (Unaudited)</b>	<b>4,427</b>	<b>940</b>	<b>43</b>	<b>9</b>	<b>65,845</b>	<b>23,548</b>	<b>(673)</b>	<b>94,139</b>	<b>1,761</b>	<b>95,900</b>

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Balances at January 1, 2007	4,424	942	40	9 66,574	32,784	(1,796)	102,977	1,546	104,523
Income for the period					26,506		26,506	446	26,952
Foreign currency translation differences (Note 24)						(935)	(935)	(44)	(979)
Net gains on available-for-sale financial assets) (Note 24)						31	31		31
Net gains on cash flow hedges (Note 24)						1,477	1,477		1,477
Total income and expense for the period recognized directly to equity						573	573	(44)	529
<b>Total income and expense for the period</b>					<b>26,506</b>	<b>573</b>	<b>27,079</b>	<b>402</b>	<b>27,481</b>
<b>Cash dividends (Note 7)</b>					<b>(28,676)</b>		<b>(28,676)</b>	<b>(12)</b>	<b>(28,688)</b>
<b>Issuance of capital stock net (Note 16)</b>	<b>(6)</b>	<b>1</b>		<b>321</b>			<b>316</b>		<b>316</b>
<b>Exercised shares (Note 21)</b>		<b>1</b>	<b>(30)</b>	<b>103</b>			<b>74</b>		<b>74</b>
<b>Minority interest</b>								<b>(14)</b>	<b>(14)</b>
<b>Balances at September 30, 2007 (Unaudited)</b>	<b>4,418</b>	<b>944</b>	<b>10</b>	<b>9 66,998</b>	<b>30,614</b>	<b>(1,223)</b>	<b>101,770</b>	<b>1,922</b>	<b>103,692</b>

See accompanying Notes to Unaudited Consolidated Financial Statements.

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in million pesos)

	<b>Nine Months Ended September 30, 2007    2006 (Unaudited)</b>	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Income before income tax	<b>39,980</b>	29,498
Adjustments for:		
Depreciation and amortization (Notes 4 and 8)	<b>18,952</b>	23,659
Interest on loans and related items - net of capitalized interest (Note 5)	<b>4,630</b>	5,685
Provision for doubtful accounts (Notes 3 and 5)	<b>1,054</b>	697
Accretion on financial liabilities - net (Note 5)	<b>834</b>	3,045
Amortization of intangible assets (Note 11)	<b>286</b>	255
Loss on derivative transactions - net (Notes 5 and 24)	<b>207</b>	151
Write-down of inventories to net realizable values (Note 5)	<b>62</b>	189
Provisions for assessments (Note 5)	<b>28</b>	(14)
Equity share in net losses (income) of associates (Note 4)	<b>17</b>	(1)
Dividends on preferred stock subject to mandatory redemption (Note 5)	<b>14</b>	113
Interest income (Note 5)	<b>(1,112)</b>	(1,297)
Foreign exchange gains - net (Note 5)	<b>(1,662)</b>	(1,601)
Others	<b>(204)</b>	(624)
Operating income before working capital changes	<b>63,086</b>	59,755
Decrease (increase) in:		
Trade and other receivables	<b>(1,637)</b>	(1,406)
Inventories and supplies	<b>(376)</b>	202
Prepayments	<b>1,165</b>	571
Advances and refundable deposits	<b>(35)</b>	1,238
Increase (decrease) in:		
Accounts payable	<b>3,586</b>	(3,360)
Accrued expenses and other current liabilities	<b>1,829</b>	1,086
Unearned revenues	<b>25</b>	398
Pension and other employee benefits	<b>(4,105)</b>	3,262
Net cash generated from operations	<b>63,538</b>	61,746
Income taxes paid	<b>(8,039)</b>	(5,600)
Net cash provided by operating activities	<b>55,499</b>	56,146
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Additions to property, plant and equipment	<b>(14,130)</b>	(16,444)
Proceeds from disposal of property, plant and equipment	<b>533</b>	792
Interest paid - capitalized to property, plant and equipment (Notes 5 and 8)	<b>(399)</b>	(428)

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Payments for purchase of investments - net of cash acquired (Note 11)	<b>(2,287)</b>	(10,724)
Proceeds from disposal of investment properties	<b>3</b>	26
Decrease (increase) in short-term investments	<b>(3,553)</b>	41
Decrease in investments in notes receivable		90
Increase in investment in debt securities	<b>(264)</b>	
Decrease in investments-held-for-sale	<b>5</b>	
Interest received	<b>901</b>	1,184
Decrease (increase) in advances and refundable deposits	<b>(366)</b>	202
Net cash used in investing activities	<b>(19,557)</b>	(25,261)

**PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)**

(in million pesos)

	<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>
	(Unaudited)	
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from availment of long-term debt (Note 17)	<b>5,429</b>	5,011
Payments of long-term debt (Note 17)	<b>(16,207)</b>	(23,366)
Payments of debt issuance costs	<b>(14)</b>	(21)
Proceeds from notes payable	<b>360</b>	129
Payments of notes payable	<b>(87)</b>	(64)
Payments of obligations under capital lease	<b>(146)</b>	(145)
Interest paid - net of capitalized portion	<b>(4,423)</b>	(5,281)
Settlements of derivatives	<b>(857)</b>	(1,778)
Cash dividends paid	<b>(28,394)</b>	(14,847)
Proceeds from issuance of capital stock	<b>74</b>	59
Redemption of shares	<b>(14)</b>	
Increase (decrease) in:		
Customers deposits	<b>14</b>	12
Other noncurrent liabilities	<b>285</b>	(1,472)
Net cash used in financing activities	<b>(43,980)</b>	(41,763)
<b>EFFECT OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>	<b>(361)</b>	(521)
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(8,399)</b>	(11,399)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<b>16,870</b>	30,059
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>8,471</b>	18,660

*See accompanying Notes to Unaudited Consolidated Financial Statements.*

## PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 1. Corporate Information

The Philippine Long Distance Telephone Company, or PLDT, or Parent Company, was incorporated under the old Corporation Law of the Philippines (Act 1459, as amended) on November 28, 1928, following the merger of four telephone companies under common U.S. ownership. Under its amended Articles of Incorporation, PLDT's corporate term is currently limited through 2028. In 1967, effective control of PLDT was sold by General Telephone and Electronics Corporation (a major shareholder since PLDT's incorporation) to a group of Filipino businessmen. In 1981, in furtherance of the then existing policy of the Philippine government to integrate the Philippine telecommunications industry, PLDT purchased substantially all of the assets and liabilities of the Republic Telephone Company, which at that time was the second largest telephone company in the Philippines. In 1998, First Pacific Company Limited, or First Pacific, and its Philippine and other affiliates, or collectively the First Pacific Group, acquired a significant interest in PLDT. On March 24, 2000, NTT Communications Corporation, or NTT Communications, through its wholly-owned subsidiary NTT Communications Capital (UK) Ltd., or NTTC-UK, became PLDT's strategic partner with approximately 15% economic and voting interest in the issued and outstanding common stock of PLDT. Simultaneous with NTT Communications' investment in PLDT, we acquired 100% of Smart Communications, Inc., or Smart. On March 14, 2006, NTT DoCoMo, Inc., or DoCoMo, acquired from NTT Communications approximately 7% of PLDT's outstanding common shares held by NTT Communications with NTT Communications retaining ownership of approximately 7% of PLDT's common shares. On February 28, 2007, Metro Pacific Asset Holdings, Inc., a Philippine affiliate of First Pacific completed the acquisition of an additional interest of approximately 46% in Philippine Telecommunications Investment Corporation, or PTIC, a shareholder of PLDT. This additional investment in PTIC represents an attributable interest of approximately 6.4% of the issued common shares of PLDT and thereby raised First Pacific Group's beneficial ownership to approximately 28% of PLDT's shares of common stock as at that date.

The common shares of PLDT are listed and traded on the Philippine Stock Exchange, or PSE. On October 19, 1994, an American Depositary Receipt, or ADR, facility was established, pursuant to which Citibank N.A., as the depository, issued ADRs evidencing American Depositary Shares, or ADSs, with each ADS representing one PLDT common share with a par value of Php5 per share. Effective February 10, 2003, PLDT appointed JP Morgan Chase Bank as successor depository for PLDT's ADR facility. The ADSs are listed on the New York Stock Exchange, or NYSE, in the United States and are traded on the NYSE under the symbol PHI. As at December 31, 2006, there were a total of over 37 million ADSs outstanding.

Until recently, the ADSs were also listed on the NYSE Arca. However, on December 18, 2006, PLDT issued a notice of its intent to voluntarily delist its ADSs from NYSE Arca, after determining that doing so is in the best interest of PLDT and its stockholders as it would eliminate the duplicative administrative burdens and costs inherent in dual listing on both the NYSE and NYSE Arca. The actual delisting from the NYSE Arca became effective on February 12, 2007.

PLDT operates under the jurisdiction of the Philippine National Telecommunications Commission, or NTC, which jurisdiction extends, among other things, to approving major services offered by PLDT and certain rates charged by PLDT.

Our registered office address is Ramon Cojuangco Building, Makati Avenue, Makati City , Philippines.

## **2. Summary of Significant Accounting Policies and Practices**

### **Basis of Preparation**

Our unaudited consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of derivative financial instruments, available-for-sale financial assets and investment properties that have been measured at fair values. The carrying values of recognized assets and liabilities that are hedged items in fair value hedges, and are otherwise carried at cost, are adjusted to record changes in the fair values attributable to the risks that are being hedged.

Our unaudited consolidated financial statements have been prepared in conformity with Philippine Financial Reporting Standards, or PFRS.

Our unaudited consolidated financial statements include, in our opinion, adjustments consisting only of normal recurring adjustments, necessary to present fairly the results of operations for the interim periods. The results of operations for the nine months ended September 30, 2007 are not necessarily indicative of the results of operations that may be expected for the full year.

Our unaudited consolidated financial statements are presented in Philippine pesos, PLDT's functional and presentation currency and all values are rounded to the nearest million except when otherwise indicated.



## Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that we have adopted the following new and amendments to existing Philippine Accounting Standards, or PAS, PFRS and Philippine Interpretations of International Financial Reporting Interpretations Committee, or IFRIC, during the year. Our adoption of these new and revised standards and interpretations did not have any effect on our financial statements. Our adoption, however, gave rise to additional disclosures on the following:

- IFRIC 7 Applying the Restatement Approach under PAS 29, Financial Reporting in Hyperinflationary Economies;
- IFRIC 8 Scope of PFRS 2, Share-based Payment;
- IFRIC 9 Reassessment of Embedded Derivatives;
- IFRIC 10 Interim Financial Reporting and Impairment;
- PAS 1 Amendments Presentation of Financial Statements Capital Disclosures; and
- PFRS 7 Financial Instruments Disclosures.

The principal effects of our adoption of the above standards are as follows:

***IFRIC 7, Applying the Restatement Approach under PAS 29, Financial Reporting in Hyperinflationary Economies*** . The Interpretation requires that when a country becomes hyperinflationary, PAS 29 must be applied as if the country had always been hyperinflationary and it provides guidance on calculating deferred taxes and comparatives. As we do not operate in a hyperinflationary economy, this standard has had no impact on our unaudited consolidated financial statements.

***IFRIC 8, Scope of PFRS 2, Share-based Payment*** . The Interpretation clarifies that PFRS 2 applies to share-based payment transactions in which the entity cannot specifically identify some or all of the goods or services received. If the value of the identifiable consideration received (if any) appears to be less than the fair value of the equity instruments granted or the liability incurred, this is an indication of other consideration (i.e., unidentifiable goods or services) has been (or will be) received which should be measured in accordance with PFRS 2. The adoption has had no significant impact on our unaudited consolidated financial statements as at September 30, 2007.

**IFRIC 9, *Reassessment of Embedded Derivatives*** . The Interpretation clarifies when an entity should reassess whether an embedded derivative needs to be separated from the host contract after the initial hybrid contract is recognized. It concludes that reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. The adoption has had no significant impact on our unaudited consolidated financial statements as at September 30, 2007.

**IFRIC 10, *Interim Financial Reporting and Impairment*** . The Interpretations states that any such impairment losses recognized in an interim financial statement must not be reversed in subsequent interim or annual financial statements. The adoption has had no significant impact on our unaudited consolidated financial statements as at September 30, 2007.

**Amendments to PAS 1, *Presentation of Financial Statements* Capital Disclosures** . This amendment requires us to include new disclosures to enable users of the financial statements to evaluate our objectives, policies and processes for managing capital. The adoption has had no significant impact on our unaudited consolidated financial statements as at September 30, 2007 except for additional disclosures as required by the standard.

**PFRS 7, *Financial Instruments Disclosures*** . This introduces new disclosures to improve information about our consolidated financial statements and the nature and extent of risks arising from financial instruments. The revised disclosures on financial instruments provided by this standard are included on our unaudited consolidated financial statements.

## Basis of Consolidation

Our unaudited consolidated financial statements include the financial statements of PLDT and those of the following significant subsidiaries (collectively, the PLDT Group).

Name of Subsidiary	Place of Incorporation	Principal Activity	Percentage of Ownership	
			Direct	Indirect
<b>Wireless</b>				
Smart	Philippines	Cellular mobile services	100.0	
Smart Broadband, Inc., or Smart Broadband	Philippines	Internet broadband distributor		100.0
Wolfpac Mobile, Inc., or Wolfpac	Philippines	Mobile applications developer and service provider		100.0
Pilipino Telephone Corporation, or Piltel	Philippines	Cellular and fixed line services		92.1
Telesat, Inc., or Telesat	Philippines	Satellite communications services	100.0	

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AceS Philippines Cellular Satellite Corporation, or AceS Philippines Mabuhay Satellite Corporation, or Mabuhay Satellite	Philippines	Satellite information and messaging services	88.5	11.5
	Philippines	Satellite communications services	67.0	
<b>Fixed Line</b>				
PLDT Clark Telecom, Inc., or ClarkTel	Philippines	Telecommunications services	100.0	
Subic Telecommunications Company, Inc., or SubicTel	Philippines	Telecommunications services	100.0	
PLDT Global Corporation, or PLDT Global	British Virgin Islands	Telecommunications services	100.0	
Smart-NTT Multimedia, Inc., or SNMI	Philippines	Data and network services	100.0	
PLDT-Maratel, Inc., or Maratel	Philippines	Telecommunications services	97.5	
Bonifacio Communications Corporation, or BCC	Philippines	Telecommunications, infrastructure and related value-added services	75.0	
<b>Information and Communications Technology, or ICT</b>				
ePLDT, Inc., or ePLDT	Philippines	Information and communications infrastructure for Internet-based services, e-commerce, call centers and IT-related services	100.0	
SPi Technologies, Inc., or SPi, and Subsidiaries	Philippines	Business process outsourcing, or BPO, services		100.0
ePLDT Ventus, Inc., or Ventus	Philippines	Call center services		100.0
Vocativ Systems, Inc., or Vocativ	Philippines	Call center services		100.0
Parlance Systems, Inc., or Parlance	Philippines	Call center services		100.0
Infocom Technologies, Inc., or Infocom	Philippines	Internet services		99.6
netGames, Inc., or netGames	Philippines	Publisher of online games		80.0
Digital Paradise, Inc., or Digital Paradise, (formerly Netopia Computer Technologies, Inc.)	Philippines	Internet access services		75.0
Level Up! (Philippines), Inc., or Level Up!	Philippines	Publisher of online games		60.0
Digital Paradise Thailand	Thailand	Internet access services		51.0
Airborne Access Corporation, or Airborne Access	Philippines	Wireless Internet services		51.0

Subsidiaries are fully consolidated from the date when control is transferred to the PLDT Group and cease to be consolidated from the date when control is transferred out of the PLDT Group.

We prepare our unaudited consolidated financial statements using uniform accounting policies for like transactions and other events with similar circumstances. Intercompany balances and transactions, including intercompany profits and unrealized profits and losses, are eliminated.

Minority interests represent the equity interests in Piltel, Level Up!, Mabuhay Satellite, Maratel, BCC, Digital Paradise, Digital Paradise Thailand, netGames, Infocom, and Airborne Access, not held by the PLDT Group.

***ePLDT's Acquisition of Level Up!***

On February 16, 2006, ePLDT acquired a 60% equity interest in Level Up!, a leading publisher of online games in the Philippines. The acquisition of Level Up!, together with netGames, ePLDT's online gaming subsidiary, is aimed to strengthen ePLDT's online gaming business in the Philippines. Post-closing conditions were completed on April 30, 2006. In August 2006, the Shareholders Agreement and Share Purchase Agreement between ePLDT and Level Up! were amended to reflect the removal of earn-out and price adjustment provisions thereby fixing the acquisition for 60% of Level Up! at the original purchase price of US\$7 million.

***ePLDT's Acquisition of SPi***

On July 11, 2006, ePLDT acquired a 100% equity interest in SPi and its direct and indirect Philippine and offshore subsidiaries for a total cash consideration of US\$135 million. As part of the transaction, ePLDT also acquired a US\$7 million debt owed by SPi to the seller at face value. In addition, ePLDT advanced US\$16 million to SPi in order for SPi to fully pay its debt owed to DBS Bank Singapore. ePLDT currently intends to have this debt refinanced by SPi in due course.

***SPi's Acquisition of CyMed, Inc., or CyMed***

On August 11, 2006, SPi in turn acquired a 100% equity interest in CyMed for an aggregate purchase price of US\$35 million, inclusive of certain debt obligations. CyMed is a leading medical transcription company based in Richmond, Virginia, United States of America (USA). It provides medical transcription services and technology products through proprietary processes based on Six Sigma quality management principles.

***SPi's Acquisition of Springfield Service Corporation, or Springfield***

On April 16, 2007, SPi acquired, through a wholly-owned US subsidiary, 100% of Springfield for an aggregate purchase price of US\$35 million, or Php1,664 million, plus possible future earn-out payments with an aggregate fair value at acquisition date of Php962 million. Springfield is one of the largest players in the medical billing and revenue cycle management market. As at September 30, 2007, SPi's total investment in Springfield amounted to Php2,685 million, including fair value of possible future earn-out payments of Php960 million and incidental costs of Php59 million, see *Note 11 Goodwill and Intangible Assets* for related discussion.

### ***Piltel's Equity Restructuring***

On April 20, 2007, the Philippine Securities and Exchange Commission, or Philippine SEC, approved Piltel's request to undergo equity restructuring to eliminate its deficit as at December 31, 2006 amounting to Php22,251 million against its additional paid-in capital. The equity restructuring was approved by Piltel's Board of Directors on March 5, 2007.

### ***Incorporation of SPi Global Solutions Corporation, or SPi Global***

On October 5, 2007, the Philippine SEC approved the incorporation of SPi Global, a wholly-owned subsidiary of ePLDT. SPi Global will be the holding company of the BPO voice and non-voice businesses of ePLDT.

### ***Investments in Associates***

Investment in associates is accounted for using the equity method of accounting. An associate is an entity in which we have significant influence and which is neither a subsidiary nor a joint venture.

Under the equity method, the investment in associate is carried in the balance sheet at cost plus post acquisition changes in our share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortized. Our unaudited consolidated statement of income reflects the share of the results of operations of the associate. Where there has been a change recognized directly in the equity of the associate, we recognize our share in any change and disclose this, when applicable, in our unaudited consolidated statements of changes in equity. Profits and losses resulting from our transactions with and among our associates are eliminated to the extent of the interest in the associate.

Our reporting dates and that of our associates are identical and our associate's accounting policies conform to those used by us for like transactions and events in similar circumstances.

### ***Foreign Currency Translations***

The functional and presentation currency of the PLDT Group (except for Mabuhay Satellite, PLDT Global, Digital Paradise Thailand and SPi and certain of its subsidiaries) is the Philippine peso. Transactions in foreign currencies are initially recorded in the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange prevailing at the balance sheet date. All differences are recognized in the consolidated statement of income except for foreign exchange losses that qualify as capitalizable borrowing costs during the construction period. For income tax purposes, exchange gains or losses are treated as taxable income or deductible expenses in the period such exchange gains or losses are realized.

The functional currency of Mabuhay Satellite, PLDT Global, SPi and certain of its subsidiaries is the U.S. dollar and Digital Paradise Thailand is the Thai baht. As at the reporting date, the assets and liabilities of these subsidiaries are translated into the reporting currency of the PLDT Group at the rate of exchange prevailing at the balance sheet date, and income and expenses of these subsidiaries are translated at the weighted average exchange rate for the period. The exchange differences arising on translation are taken directly to a separate component of equity as cumulative translation adjustments. On disposal of these subsidiaries, the amount of the cumulative translation adjustments recognized in equity relating to subsidiaries are recognized in the consolidated statement of income.

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

Property, plant and equipment, except for land, are stated at cost less accumulated depreciation and amortization and any impairment in value. Land is stated at cost less any impairment in value.

The initial cost of property, plant and equipment comprises its purchase price and any costs directly attributable in bringing the asset to its working condition and location for its intended use. Expenditures incurred after the assets have been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to income in the period 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. Cost also includes asset retirement obligation, interest on borrowed funds used during the construction period and qualified borrowing costs from foreign exchange losses related to foreign currency-denominated liabilities used to acquire such qualifying assets. When assets are sold or retired, their costs and accumulated depreciation, amortization and impairment losses, if any, are eliminated from the accounts and any gain or loss resulting from their disposal is included in the consolidated statement of income of such period.

Depreciation and amortization are calculated on a straight-line basis over the estimated useful lives of the assets.

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 items of property, plant and equipment.

Property under construction is stated at cost. This includes cost of construction, plant and equipment and other direct costs. Property under construction is not depreciated until such time that the relevant assets are completed and substantially available for their intended use.

### ***Borrowing Costs***

Borrowing costs are capitalized if they are directly attributable to the acquisition, construction or production of a qualifying asset. Capitalization of borrowing costs commences when the activities for intended use are in progress and expenditures and borrowing costs are being incurred. Borrowing costs are capitalized until the assets are ready for their intended use. If the resulting carrying amount of the asset exceeds its recoverable amount, an impairment loss is recognized. Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds, as well as exchange differences arising from foreign currency borrowings used to finance these projects to the extent that they are regarded as an adjustment to interest cost.

All other borrowing costs are expensed as incurred.

Borrowing costs are treated as deductible expenses for income tax reporting purposes in the period they are incurred or realized.

### ***Asset Retirement Obligations***

We are legally required under various lease agreements to dismantle the installations on leased sites and restore such sites to their original condition at the end of the lease contract term. We recognized the fair value of the liability for these obligations and capitalized the present value of these costs as part of the balance of the related property, plant and equipment accounts, which are being depreciated on a straight-line basis over the useful lives of the related assets or the contract periods, whichever is shorter.

### ***Investment Properties***

Investment properties are initially measured at cost including 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. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from changes in the fair values of investment properties are included in the consolidated statement of income in the period in which they arise.

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

Transfers are made to or from investment property only when there is a change in use. For a transfer from investment property to owner occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner occupied property becomes an investment property, we account for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

No assets held under operating lease have been classified as investment properties.

### ***Business Combinations and Goodwill***

Business combinations are accounted for using the purchase method of accounting. This involves recognizing identifiable assets (including previously unrecognized intangible assets) and liabilities (including contingent liabilities and excluding future restructuring) of our acquired business at fair value.

Goodwill acquired in a business combination is initially measured at cost, such cost, being the excess of the cost of the business combination over our interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of our cash generating units, or groups of our cash generating units, that are expected to benefit from the synergies of the combination, irrespective of whether our other assets or liabilities are assigned to those units or groups of units. Each unit or group of units to which the goodwill is allocated: (1) represents our lowest level at which the goodwill is monitored for internal management purposes; and (2) is not larger than a segment based on either our primary or secondary reporting format determined in accordance with *PAS 14, Segment Reporting*.

Where goodwill forms part of a cash-generating unit (group of cash generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.



When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and unamortized goodwill is recognized in the consolidated statement of income.

### ***Intangible Assets***

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired from business combinations is initially recognized at fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment loss. The useful lives of intangible assets are assessed at the individual asset level as having either a finite or indefinite life.

Intangible assets with finite lives are amortized over the useful economic life using the straight-line method and assessed for impairment whenever there is an indication that the intangible assets may be impaired. At a minimum, the amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at each financial period end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the consolidated statement of income in the expense category consistent with the function of the intangible asset.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the consolidated statement of income when the asset is derecognized.

Intangible assets created within the business are not capitalized and expenditure is charged against operations in the period in which the expenditure is incurred.

### ***Impairment of Non-Financial Assets***

We assess at each reporting period whether there is an indication that an asset may be impaired. If any such indication exists, or when the annual impairment testing for an asset is required, we make an estimate of the asset's recoverable

amount. An asset's recoverable amount is the higher between an asset's or cash-generating unit's fair value less costs to sell or its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent from those of other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining the fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators.

Impairment losses of continuing operations are recognized in the consolidated statement of income in those expense categories consistent with the function of the impaired asset, except for property previously revalued where the revaluation was taken to equity. In this case, the impairment is also recognized in equity up to the amount of any previous revaluation.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, we make an estimate of recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If this is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior periods. Such reversal is recognized in the consolidated statement of income. After such a reversal, the depreciation charged is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

The following criteria are also applied in assessing impairment of specific assets:

#### *Goodwill*

Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

Impairment is determined for goodwill by assessing the recoverable amount of the cash-generating unit (or group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (or group of cash-generating units) is less than the carrying amount of the cash-generating unit (group of cash-generating units) to which goodwill has been allocated, an impairment loss is recognized. Impairment losses relating to goodwill cannot be reversed in future periods.

#### *Intangible Assets*

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level, as appropriate.

#### *Investments in Associates*

After application of the equity method, we determine whether it is necessary to recognize an additional impairment loss of our investment in associates. We determine at each balance sheet date whether there is any objective evidence that our investment in an associate is impaired. If this is the case, we calculate the amount of impairment as being the difference between the fair value of the investment in associate and the carrying amount and recognize the amount in the consolidated statement of income.

#### *Research and Development Costs*

Research and development costs are expensed as incurred.

#### *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 the date of acquisition and that are subject to an insignificant risk of change in value.

#### *Trade and Other Receivables*

Trade and other receivables are stated at face value, net of allowance for any doubtful accounts.

#### *Allowance for Doubtful Accounts*

The PLDT Group's accounting policy in evaluating any impairment of receivable is discussed under impairment of financial assets section of this Note. Consequently, allowance for doubtful accounts is maintained at a level considered adequate to provide for uncollectible receivables. The level of allowance is based on historical collections, write-off experience, current economic trends, changes in our customer payment terms and other factors that may affect our ability to collect payments. An evaluation of the receivables, designed to identify potential charges to the allowance, is performed on a continuous basis during the period.

*Subscribers.* Full allowance is provided for receivables from permanently disconnected subscribers. Permanent disconnections are made after a series of collection steps following non-payment by subscribers. Such permanent disconnections generally occur within 105 days from the date of payment was due. Partial allowance is provided for active subscribers based on the historical loss experience and aging profile of the receivable.

*Traffic settlement receivables net.* Full allowance is provided for carrier accounts which are considered over-due and after a review of the status of settlement with other carriers.

### ***Inventories and Supplies***

Inventories and supplies which include cellular phone units, materials, spare parts, terminal units and accessories, are valued at the lower of cost and net realizable value.

Cost is determined using the moving average method. Net realizable value is the estimated selling price in the ordinary course of the business less the estimated cost to sell.

### ***Interest-bearing Financial Liabilities***

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.

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

### ***Convertible Preferred Stock***

*Peso-denominated*

The component of our convertible preferred stock that exhibits characteristics of a liability is recognized as a liability in the consolidated balance sheet, net of transaction costs. The corresponding dividends on those shares are charged as interest expense in the consolidated statement of income. On issuance of our convertible preferred stock, the fair value of the liability component is determined using a market rate for an equivalent non-convertible bond and this amount is carried as a long-term liability on the amortized cost basis until extinguished on conversion or redemption.

The remainder of the proceeds is allocated to the conversion option that is recognized and included in the equity section of the consolidated balance sheet, net of transaction costs. The carrying amount of the conversion option is not re-measured in subsequent periods.

Transaction costs are apportioned between the liability and equity components of the convertible preferred stock based on the allocation of proceeds to the liability and equity components when the instruments are first recognized.

*Foreign currency-denominated*

We treated the Series VI and VII Convertible Preferred Stock as debt instruments with embedded call options. The fair value of embedded call options as of issuance date was bifurcated and thereafter accounted for separately at fair value through profit and loss. The residual amount was assigned as a liability component and accreted to the redemption amount up to the call option date using the effective interest rate method.

***Provisions***

We recognize provisions when we have present obligations, legal or constructive, as a result of past events, and when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where we expect some or all of a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statement of income, net of any reimbursements. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as additional provisions.

***Retirement Benefits***

*Defined Benefit Pension*

We have funded retirement plans, administered by our respective Fund s Trustees, covering permanent employees. Retirement costs are actuarially determined using the projected unit credit of accrued benefit valuation method. This method reflects services rendered by employees to the date of valuation and incorporates assumptions concerning employees projected salaries. Retirement costs include current service cost plus amortization of past service cost, experience adjustments and changes in actuarial assumptions. Past service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested. If the benefits are already vested immediately following the introduction of, or changes to, a pension plan, past service cost is recognized immediately. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains and losses are recognized over the expected average remaining working lives of the employees participating in the plan.

The defined benefit asset or liability comprises the present value of the defined benefit obligation less past service cost not yet recognized and less the fair value of plan assets out of which the obligations are to be settled directly. The value of any asset is restricted to the sum of any past service cost not yet recognized and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

Upon our adoption of *PAS 19, Employee Benefits* , in 2004, we opted to amortize our transition liabilities for the three years until December 31, 2006, see *Note 21 Employee Benefits*.

#### *Defined Contribution Plans*

Smart and I-Contacts, Inc., or I-Contacts, record expenses for defined contribution plans for their contribution when the employee renders service to Smart and I-Contacts, respectively, essentially coinciding with their cash contributions to the plans.

#### *Share-Based Payment Transactions*

Certain of our employees (including directors) receive remuneration in the form of share-based payment transactions, whereby employees render services in exchange for shares or rights over shares ( equity-settled transactions ).

#### *Equity-settled transactions*

The cost of equity-settled transactions with employees is measured by reference to the fair value of the stock options at the date at which they are granted. Fair value is determined using an option-pricing model, further details of which are set forth in *Note 21 Employee Benefits*. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of PLDT ( market conditions ).

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ( vesting date ). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the number of awards that will ultimately vest, in the opinion of PLDT's Board of Directors, at that date, based on the best available estimate.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, an expense, at a minimum, is recognized as if the terms had not been modified. An expense is recognized for any increase in the value of the transactions as a result of the modification, as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were modifications of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share, see *Note 7 Earnings Per Common Share*.

#### *Cash-settled transactions*

Our Long-Term Incentive Plan, or LTIP, grants share appreciation rights, or SARs, to our eligible key executives and advisors. Under the LTIP, we recognize the services we receive from our eligible key executives and advisors, and our liability to pay for those services, as the eligible key executives and advisors render services during the vesting period. We measure our liability, initially and at each reporting date until settled, at the fair value of the SARs, by applying an option valuation model, taking into account the terms and conditions on which the SARs were granted, and the extent to which the eligible key executives and advisors have rendered service to date. We recognize any changes in fair value at each reporting date until settled, in the consolidated statement of income for the period.

#### *Leases*

The determination of whether an arrangement contains a lease is based on the substance of the arrangement at the inception date of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the

arrangement conveys a right to use the asset. A reassessment is made after the inception date of the lease only if the following criteria apply: (1) there is a change in the contractual terms, other than a renewal or extension of the arrangement; (2) a renewal option is exercised or an extension is granted, unless the term of the renewal or extension was initially included in the lease term; (3) there is a change in the determination of whether fulfillment is dependent on a specified asset; or (4) there is a substantial change to the asset.

Where a reassessment is made, lease accounting commences or ceases, as the case may be, from the date when the change in circumstances gives rise to the reassessment for scenarios (1), (3) or (4) and at the date of renewal or extension period for scenario (2).

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 requirements of *IFRIC 4, Determining Whether an Arrangement Contains a Lease* .

Lease obligations having provisions for bargain purchase options, or ownership transfer at the end of the lease term, or a lease term equal to 75% or more of the estimated economic life of the leased property, or lease obligations where the present value at the beginning of the lease term of the minimum lease payments (excluding executory costs and taxes to be paid or paid by the lessor and including any profit thereon) equals or exceeds 90% of the fair value of the leased property, are capitalized. The related obligations are recognized as liabilities at fair value. Minimum lease payments are allocated between the finance charges and reduction of the lease liability so as to achieve a constant periodic rate of interest on the remaining balance of the liability.

A capital lease gives rise to a depreciation expense for the asset, as well as a borrowing cost for each period. Finance charges are charged directly to current operations. The depreciation policy for leased assets is consistent with that for depreciable assets that are owned.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term, if there is no reasonable certainty that we will obtain ownership of the leased asset at the end of the lease term.

Leases where the lessor 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 deferred and amortized on a straight-line method over the lease term on the same bases as the lease income. Operating lease payments are recognized as an expense in the consolidated statement of income on a straight-line basis over the lease term. For income tax reporting purposes, expenses that should have been incurred under a lease agreement are considered as deductible expenses.

### ***Revenue Recognition***



Revenues for services are stated at amounts invoiced to customers, net of value-added tax, or VAT, or overseas communication tax, or OCT, if applicable. We provide wireless communication, fixed line communication, and ICT services. We provide such services to mobile, business, residential and payphone customers. Revenues represent the value of fixed consideration that have been received or are receivable. Revenues are recognized when there is evidence of an arrangement, collectibility is reasonably assured, and the delivery of the product or service has occurred. In certain circumstances, revenue is split into separately identifiable components and recognized when the related components are delivered in order to reflect the substance of the transactions. The value of components is determined using verifiable objective evidence. Under certain arrangements where the above criteria are met, but there is uncertainty regarding the outcome of the transaction for which service was rendered, revenue is recognized only to the extent of expenses incurred for rendering the service, and such amount is determined to be recoverable. We do not provide our customers with the right to a refund.

#### *Service revenues*

#### *Subscriptions*

We provide telephone and data communication services under prepaid and postpaid payment arrangements. Revenues, including fees for installation and activation, are accrued upon subscription.

#### *Air time, traffic and value-added services*

Prepaid service revenues collected in advance are deferred and recognized based on the earlier of actual usage or upon expiration of the usage period. Interconnection revenues for call termination, call transit, and network usage are recognized in the period the traffic occurs. Revenues related to local, long distance, network-to-network, roaming and international call connection services are recognized when the call is placed or connection is provided, net of amounts payable to other telecommunication carriers for terminating calls in their territories. Revenues related to products and value-added services are recognized upon delivery of the product or service.

#### *Business Process Outsourcing, or BPO*

Where applicable, supplemental revenues are recognized depending on service levels or achievement of certain performance measurement targets. We recognize these supplemental revenues only after it has achieved the required measurement targets. When these service levels or performance measurement targets are not achieved, we grant service credits as a reduction in fees. Advance customer receipts that have not been recognized as revenue in accordance with its stated policies are recorded as advances from customers and presented as a liability in the consolidated balance sheet. If the fee is not fixed or determinable, revenue is not recognized on those arrangements until the customer payment is received. For arrangements requiring specific customer acceptance, revenue recognition is deferred until the earlier of the end of the deemed acceptance period or until a written notice of acceptance is received from the customer. Revenue on services rendered to customers whose ability to pay is in doubt at the time of performance of services is also not recorded. Rather, revenue is recognized from these customers as payment is received.

*Incentives*

We record insignificant commission expenses based on the number of new subscriber connections initiated by certain dealers. All other cash incentives provided to dealers and customers are recorded as a reduction of revenue. Product-based incentives provided to dealers and customers as part of a transaction are accounted for as multiple element arrangements and recognized when earned.

*Non-service revenues*

*Handset and equipment sales*

Sales of cellular handsets and communication equipment are recognized upon delivery to the customer.

*Interest income*

Interest income is recognized as it accrues on a time proportion basis taking into account the principal amount outstanding and the effective interest rate.

***Income Taxes***

*Current income tax*

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

*Deferred income tax*

Deferred income tax is provided using the balance sheet liability method on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences except: (1) when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss and (2) with respect to taxable temporary differences associated with investments in subsidiaries, associates and

interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is possible that the temporary differences will not reverse in the foreseeable future. Deferred income tax assets are recognized for all deductible temporary differences, carryforward of unused tax credits from excess minimum corporate income tax, or MCIT, and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and carryforward of unused tax credits and unused tax losses can be utilized except: (1) when the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss and (2) with respect to deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax liabilities are not provided on non-taxable temporary differences associated with investments in domestic subsidiaries and associates. With respect to investments in other subsidiaries and associates, deferred tax liabilities are recognized except when the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred income tax assets are 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 income tax asset to be utilized. Unrecognized deferred income 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 income tax asset to be recovered.

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

Deferred income tax relating to items recognized directly in equity is included in the related equity account and not in the consolidated statement of income.

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

***Earnings Per Common Share, or EPS***

Basic EPS is calculated by dividing the consolidated net income for the period attributable to common shareholders (consolidated net income adjusted for dividends on all series of preferred shares except for dividends on preferred stock subject to mandatory redemption) by the weighted average number of common shares outstanding during the period, after giving retroactive effect to any stock dividend declarations.

Diluted EPS is calculated in the same manner assuming that, at the beginning of the period or at the time of issuance during the period, all outstanding options are exercised and convertible preferred shares are converted to common shares, and appropriate adjustments to consolidated net income are effected for the related expenses and income on preferred shares. Outstanding stock options will have a dilutive effect under the treasury stock method only when the average market price of the underlying common share during the period exceeds the exercise price of the option.

Where the effect of the assumed conversion of the preferred shares and the exercise of all outstanding options have an anti-dilutive effect, basic and diluted EPS are stated at the same amount.

If the required dividends to be declared on each series of convertible preferred shares divided by the number of equivalent common shares, assuming such convertible preferred shares are converted to common shares, would decrease the basic EPS, then such convertible preferred shares would be deemed

dilutive. As such, the diluted EPS will be calculated by dividing consolidated net income attributable to common shareholders (consolidated net income, adding back any dividends and/or other charges recognized in the period related to the dilutive convertible preferred shares classified as liability, less dividends on non-dilutive preferred shares except for dividends on preferred stock subject to mandatory redemption) by the weighted average number of common shares including the common share equivalent arising from the conversion of the dilutive convertible preferred shares.

### ***Investments and Other Financial Assets and Liabilities***

Financial assets and liabilities within the scope of PAS 39, *Financial Instruments: Recognition and Measurement*, are classified as either financial assets and liabilities at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets, as appropriate. We determine the classification of our financial assets and liabilities after initial recognition and, where allowed and appropriate, re-evaluates this designation at each balance sheet date. When financial assets and liabilities are recognized initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable to transaction costs. 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 or other valuation models.

All regular way purchases and sales of financial assets are recognized on the trade date, which is the date that we commit to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets with the period generally established by regulation or convention in the market place.

*Financial assets and liabilities at fair value through profit or loss*

Financial assets and liabilities at fair value through profit or loss includes financial assets and liabilities held for trading and financial assets and liabilities designated upon initial recognition as at fair value through profit and loss.

Financial assets and liabilities are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments or liabilities held for trading are recognized in profit and loss.

Where a contract contains one or more embedded derivatives, the entire hybrid contract may be designated as a financial asset and financial liability at fair value through profit or loss, except where the embedded derivative does not significantly modify the cash flows or it is clear that separation of the embedded derivative is prohibited.

Financial assets and liabilities may be designated at initial recognition as at fair value through profit or loss if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets and liabilities or recognizing gains or losses on them on a different basis; or (ii) the assets and liabilities are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial assets and liabilities contains an embedded derivative that would need to be separately recorded.

*Held-to-maturity investments*

Held-to-maturity investments are non-derivative financial assets which carry fixed or determinable payments and fixed maturities and which we have the positive intention and ability to hold to maturity. After initial measurement, held-to-maturity investments are measured at amortized cost in the consolidated balance sheet. This cost is computed as the amount initially recognized minus principal repayments, plus or minus the cumulative amortization using the effective interest rate method of any difference between the initially recognized amount and the maturity amount, less allowance for impairment. This calculation includes all fees and amounts paid or received between parties to the contract that are an integral part of the effective interest rate method, transaction costs and all other premiums and discounts. Gains and losses are recognized in the consolidated statement of income when the investments are derecognized or impaired, as well as through the amortization process.

*Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are subsequently carried at amortized cost in the consolidated balance sheet using the effective interest rate method less any allowance for impairment. Amortized cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate method and transaction costs. Gains and losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

#### *Available-for-sale financial assets*

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial measurement, available-for-sale financial assets are measured at fair value in the consolidated balance sheet with unrealized gain or loss being recognized directly in equity in the cumulative translation adjustments except when the financial asset is impaired. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognized in the consolidated statement of income. Interest earned or paid on the investments is reported as interest income or expense using the effective interest rate method. Dividends earned on investments are recognized in the consolidated statement of income when the right of payment has been established.

We consider whether a contract contains an embedded derivative, when the entity first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

#### *Impairment of Financial Assets*

We assess at each balance sheet date whether a financial asset or group of financial assets is impaired.

#### *Assets carried at amortized cost*

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 expected 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 is reduced through an allowance account. The amount of the loss is recognized in the consolidated statement of income.

We first assess 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.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that we will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through an allowance account. Impaired debts are derecognized when they are assessed as uncollectible.

#### *Available-for-sale financial assets*

If an available-for-sale 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 available-for-sale 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.

#### ***Derecognition of Financial Assets and Liabilities***

##### *Financial assets*

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognized when: (1) the rights to receive cash flows from the asset have expired; (2) we retain the right to receive cash flows from the asset, but have assumed an obligation to pay them in full without material delay to a third party under a pass through arrangement; or (3) we have transferred our right to receive cash flows from the asset and either (a) have transferred substantially all the risks and rewards of the asset, or (b) have neither transferred nor retained substantially all the risks and rewards of the asset, but have transferred control of the asset.

Where we have transferred our right to receive cash flows from an asset and have 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 our continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of

consideration that we could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of our continuing involvement is the amount of the transferred asset that we may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of our continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

#### *Financial liabilities*

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

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.

#### *Derivative Financial Instruments and Hedging*

We use derivative financial instruments such as long-term currency swaps, foreign-currency options, forward currency contracts and interest rate swaps to hedge our risks associated with interest rate and foreign currency fluctuations. Such derivative financial instruments are initially recognized at fair value on the date on which a derivative contract is entered into 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.

Any gains or losses arising from changes in fair value on derivatives during the period that do not qualify for hedge accounting are taken directly to the consolidated statement of income.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of long-term currency swaps, foreign currency options and interest rate swap contracts is determined by reference to market values for similar instruments.

For the purpose of hedge accounting, hedges are classified as: (1) fair value hedges when hedging the exposure to changes in the fair value of a recognized financial asset or liability or an unrecognized firm commitment (except for foreign-currency risk); or (2) cash flow hedges when hedging exposure to variability in cash flows that is either



attributable to a particular risk associated with a recognized financial asset or liability or a highly probable forecast transaction or the foreign-currency risk in an unrecognized firm commitment; or (3) hedges of a net investment in a foreign operation.

At the inception of a hedge relationship, we formally designate and document the hedge relationship to which we wish to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an on-going basis to determine that they actually have been highly effective throughout the financial reporting periods for which they are designated.

Hedges which meet the strict criteria for hedge accounting are accounted for as follows:

*Fair value hedges*

The change in the fair value of a hedging derivative is recognized in the consolidated statement of income. The change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item and is also recognized in the consolidated statement of income.

For fair value hedges relating to items carried at amortized cost, the adjustment to carrying value is amortized through the consolidated statement of income over the remaining term to maturity. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest rate method is used is amortized through the consolidated statement of income.

Amortization may begin as soon as an adjustment exists, beginning no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

If the hedge item is derecognized, the unamortized fair value is recognized immediately in the consolidated statement of income.

When an unrecognized firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognized as financial asset or liability with a corresponding gain or loss recognized in the consolidated statement of income. The changes in the fair value of the hedging instrument are also recognized in the consolidated statement of income.

*Cash flow hedges*

The effective portion of the gain or loss on the hedging instrument is recognized directly in equity, while any ineffective portion is recognized immediately in the consolidated statement of income.

Amounts taken to equity are transferred to the consolidated statement of income when the hedged transaction affects the consolidated statement of income, such as when the hedged financial income or financial expense is recognized or when a forecast sale occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognized in equity are transferred to the consolidated statement of income. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognized in equity remain in equity until the forecast transaction or firm commitment occurs.

*Hedges of a net investment*

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, are accounted for in a way similar to cash flow hedges. Gains or losses on the hedging instrument relating to the effective portion of the hedge are recognized directly in equity while any gains or losses relating to the ineffective portion are recognized in the consolidated statement of income. On disposal of the foreign operation, the cumulative value of any such gains or losses recognized directly in equity is transferred to the consolidated statement of income.

**New Accounting Standards Subsequent to September 2007**

Following are the new PFRS and IFRIC, which will be effective subsequent to September 30, 2007:

***IFRIC 11, PFRS 2, Group and Treasury Share Transactions*** . This will become effective for annual periods beginning on or after March 31, 2007. This Interpretation addresses issues whether transactions should be accounted for as equity-settled or as cash-settled under PFRS 2 and issues the concerning share-based payment arrangement involving entities within the same group.

***IFRIC 12, Service Concession Arrangements*** . This will become effective on January 1, 2008. This interpretation, which covers contractual arrangements arising from entities providing public services, is not relevant to our current

operations.

**PFRS 8, *Operating Segments*** . The standard is effective beginning January 1, 2009 and will replace PAS 14 and adopts a management approach to reporting segment information. The requirements of this standard will be included on our consolidated financial statements when the standard is adopted.

We expect that the adoption of the pronouncements listed above will have no significant impact on our consolidated financial statements in the period of our initial application.

### **3. Management's Use of Judgments, Estimates and Assumptions**

The preparation of our unaudited consolidated financial statements in conformity with PFRS requires us to make judgments, estimates and assumptions that affect the reported amounts of our assets and liabilities and disclosure of contingent assets and liabilities at the date of our unaudited consolidated financial statements, and the reported amounts of revenues and expenses during the period reported and related notes. In preparing our unaudited consolidated financial statements, we have made our best judgments, estimates and assumptions of certain amounts, giving due consideration to materiality. We believe the following represents a summary of these significant judgments, estimates and assumptions and related impacts and associated risks to our unaudited consolidated financial statements.

#### *Estimating useful lives of property, plant and equipment*

We estimate the useful lives of our property, plant and equipment based on the periods over which our assets are expected to be available for use. Our estimation of the useful lives of our property, plant and equipment is based on our collective assessment of industry practice, internal technical evaluation and experience with similar assets. The estimated useful lives of our property, plant and equipment are reviewed at least annually and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limitations on the use of our assets. It is possible, however, that future results of operations could be materially affected by changes in our estimates brought about by changes in the factors mentioned above. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of our property, plant and equipment would increase our recorded operating expenses and decrease our noncurrent assets.

Total carrying values of property, plant and equipment, net of accumulated depreciation and amortization amounted to Php159,288 million and Php164,190 million as at September 30, 2007 and December 31, 2006, respectively, see *Note 8 Property, Plant and Equipment*.

#### *Goodwill and intangible assets*

Purchase accounting requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair market values of the acquiree's identifiable assets and liabilities at the acquisition date. It also requires the acquiree to recognize goodwill. Our business acquisitions have resulted in goodwill and intangible assets, which are subject to periodic impairment test and amortization, respectively, see *Note 11 Goodwill and Intangible Assets*.

Total carrying values of goodwill and intangible assets as at September 30, 2007 and December 31, 2006 amounted to Php13,701 million and Php12,214 million, respectively. We have no impairment losses recognized for the nine months ended September 30, 2007 and 2006.

#### *Asset impairment*

PFRS requires that an impairment review be performed when certain impairment indicators are present. In the case of goodwill, at a minimum, such asset is subject to a yearly impairment test and whenever there is an indication that such asset may be impaired. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires us to make an estimate of the expected future cash flows from the cash-generating unit and to choose a suitable discount rate in order to calculate the present value of those cash flows.

Determining the fair values of property, plant and equipment, investments and intangible assets, which requires the determination of future cash flows expected to be generated from the continued use and ultimate disposition of such assets, requires us to make estimates and assumptions that can materially affect our unaudited consolidated financial statements. Future events could cause us to conclude that property, plant and equipment, investments and intangible assets associated with an acquired business are impaired. Any resulting impairment loss could have a material adverse impact on our financial condition and results of operations.

The preparation of estimated future cash flows involves significant judgments and estimations. While we believe that our assumptions are appropriate and reasonable, significant changes in our assumptions may materially affect our assessment of recoverable values and may lead to future additional impairment charges under PFRS. We have no impairment losses recognized for the nine months ended September 30, 2007 and 2006.

*Investment properties*

We have adopted the fair value approach in determining the carrying value of our investment properties. We have opted to rely on independent appraisers in determining the fair values of our investment properties, and such fair values were determined based on recent prices of similar properties, with adjustments to reflect any changes in economic conditions since the date of those transactions. The amounts and timing of recorded changes in fair value for any period would differ if we made different judgments and estimates or utilized a different basis for determining fair value.

Total carrying values of investment properties as at September 30, 2007 and December 31, 2006 amounted to Php580 million and Php587 million, respectively, see *Note 10 Investment Properties*.

*Realizability of deferred income taxes*

We review the carrying amounts of deferred income tax assets at each balance sheet date and reduce these to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred income tax assets to be utilized. Our assessment on the recognition of deferred income tax assets on deductible temporary differences is based on the forecasted taxable income of the subsequent reporting periods. This forecast is based on our past results and future expectations on revenues and expenses. As management believes, it will have no sufficient future taxable income to utilize the benefits of deductible temporary differences. However, there is no assurance that we will generate sufficient taxable income to allow all or part of our deferred income tax assets to be utilized.

Total unrecognized deferred income tax assets as at September 30, 2007 and December 31, 2006 amounted to Php322 million and Php299 million, respectively, see *Note 6 Income Tax*.

*Determination of fair values of financial assets and liabilities*

We carry certain of our financial assets and liabilities at fair value, which requires extensive use of accounting estimates and judgments. In addition, certain liabilities acquired through debt exchange and restructuring are required to be carried at fair value at the time of the debt exchange and restructuring, see *Note 24 Financial Assets and Liabilities*. While significant components of fair value measurement were determined using verifiable objective evidence (i.e., foreign exchange rates, interest rates, volatility rates), the amount of changes in fair value would differ if we utilized a different valuation methodology. Any change in fair value of these financial assets and liabilities would directly affect our consolidated statement of income and equity.

Total fair value of financial assets and liabilities as at September 30, 2007 amounted to Php30,822 million and Php90,922 million, respectively, while the total fair value of financial assets and liabilities as at December 31, 2006 amounted to Php35,952 million and Php106,301 million, respectively, see *Note 24 Financial Assets and Liabilities*.

#### *Estimating allowance for doubtful accounts*

We estimate the allowance for doubtful accounts related to our trade receivables based on two methods. The amounts calculated using each of these methods are combined to determine the total amount we reserve. We evaluate specific accounts where we have information that certain customers are unable to meet their financial obligations. In these cases, we use judgment based on the best available facts and circumstances, including but not limited to, the length of our relationship with the customer and the customer's current credit status based on third party credit reports and known market factors, to record specific reserves for customers against amounts due in order to reduce our receivables to amounts that we expect to collect. These specific reserves are re-evaluated and adjusted as additional information received affects the amounts estimated. Full allowance is provided for receivables from permanently disconnected subscribers and carriers. Such permanent disconnections generally occur within 105 days from the date of payment was due. Partial allowance is provided for active subscribers and carriers based on the age status of receivables.

The amounts and timing of recorded expenses for any period would differ if we made different judgments or utilized different estimates. An increase in our allowance for doubtful accounts would increase our recorded operating expenses and decrease our current assets.

Provision for doubtful accounts amounted to Php1,054 million and Php697 million for the nine months ended September 30, 2007 and 2006, respectively. Trade and other receivables, net of allowance for doubtful accounts, amounted to Php10,245 million and Php10,158 million as at September 30, 2007 and December 31, 2006, respectively, see *Note 5 Income and Expenses* and *Note 14 Trade and Other Receivables*.

#### *Asset retirement obligations*

Asset retirement obligations are recognized in the period in which they are incurred if a reasonable estimate of fair value can be made. This requires an estimation of the cost to restore/dismantle on a per square meter basis, depending on the location, and is based on the best estimate of the expenditure required to settle the obligation at the balance sheet date, discounted using a pre-tax rate that reflects the current market assessment of the time value of money and, where appropriate, the risk specific to the liability. Total provision for asset retirement obligations amounted to Php909 million and Php831 million as at September 30, 2007 and December 31, 2006, respectively, see *Note 8 Property, Plant and Equipment* and *Note 18 Other Noncurrent Liabilities*.

*Revenue recognition*

Our revenue recognition policies require us to make use of estimates and assumptions that may affect the reported amounts of our revenues and receivables.

Our agreements with domestic and foreign carriers for inbound and outbound traffic subject to settlements require traffic reconciliations before actual settlement is done, which may not be the actual volume of traffic as measured by us. Initial recognition of revenues is based on our observed traffic adjusted by our normal experience adjustments, which historically are not material to our unaudited consolidated financial statements. Differences between the amounts initially recognized and the actual settlements are taken up in the accounts upon reconciliation. However, there is no assurance that such use of estimates will not result in material adjustments in future periods.

Revenues under a multiple element arrangement specifically applicable to our wireless business are split into separately identifiable components and recognized when the related components are delivered in order to reflect the substance of the transaction. The fair value of components is determined using verifiable objective evidence. Revenue for handset sales has been quantified and identified separately using the residual value method from our cellular service revenue.

Under certain arrangements with our BPO services, if there is uncertainty regarding the outcome of the transaction for which service was rendered, revenue is recognized only to the extent of expenses incurred for rendering the service and such amount is determined to be recoverable.

*Estimation of pension cost and other retirement benefits*

The determination of our obligation and cost for pension and other retirement benefits is dependent on our selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are described in *Note 21 Employee Benefits* and include, among other things, discount rates, expected returns on plan assets and rates of compensation increases. In accordance with PFRS, actual results that differ from our assumptions are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceed 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. While we believe that our assumptions are reasonable and appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our pension and other retirement obligations.

Unrecognized net actuarial loss as at September 30, 2007 and December 31, 2006 amounted to Php4,561 million and Php4,657 million, respectively. The accrued benefit cost as at September 30, 2007 and December 31, 2006 amounted to Php2,651 million and Php2,888 million, respectively, see *Note 21 Employee Benefits*.

#### *Share-based payment transactions*

Our LTIP grants share appreciation rights, or SARs, to our eligible key executives and advisors. Under the LTIP, we recognize the services we receive from the eligible key executives and advisors, and our liability to pay for those services, as the eligible key executives and advisors render services during the vesting period. We measure our liability, initially and at each reporting date until settled, at the fair value of the SARs, by applying an option valuation model, taking into account the terms and conditions on which the SARs were granted, and the extent to which the eligible key executives and advisors have rendered service to date. We recognize any changes in fair value at each reporting date until settled, in the results of operations for the period. The assumptions and estimates are described in *Note 21 Employee Benefits* and include, among other things, annual stock volatility, risk free interest rate, remaining life, and the fair value of common stock. While management believes that the assumptions and estimates used are reasonable and appropriate, significant differences in our actual experience or significant changes in the assumptions may materially affect the stock compensation costs charged to operations. The fair value of the LTIP recognized as an expense for the nine months ended

September 30, 2007 (under the 2007 to 2009 LTIP) and 2006 (under the 2004 to 2006 LTIP) amounted to Php1,100 million and Php2,677 million, respectively. As at September 30, 2007 and December 31, 2006, total LTIP liability amounted to Php1,175 million and Php5,030 million, respectively, see *Note 5 Income and Expenses* and *Note 21 Employee Benefits*.

#### *Legal contingencies*

We are currently involved in various legal proceedings. Our estimate of the probable costs for the resolution of these claims has been developed in consultation with outside counsel handling our defense in these matters and is based upon an analysis of potential results. We currently do not believe these proceedings will have a material adverse effect on our unaudited consolidated financial statements. It is possible, however, that future results of operations could be materially affected by changes in our estimates or in the effectiveness of our strategies relating to these proceedings, see *Note 23 Provisions and Contingencies*.

#### *Determination of functional currency*

Based on the economic substance of the underlying circumstances relevant to the PLDT Group, the functional and presentation currency of the PLDT Group (except for Mabuhay Satellite, PLDT Global, Digital Paradise Thailand and SPi and certain of its subsidiaries) is the Philippine peso. Transactions in foreign currencies are initially recorded in the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange prevailing at the balance sheet date. All



differences are taken to the consolidated statement of income except for foreign exchange losses that qualify as capitalizable borrowing costs during the construction period. For income tax purposes, exchange gains or losses are treated as taxable income or deductible expenses in the period such gains or losses are realized.

The functional currency of Mabuhay Satellite, PLDT Global, SPi and certain of its subsidiaries is the U.S. dollar and Digital Paradise Thailand is the Thai baht. As at the reporting date, the assets and liabilities of these subsidiaries are translated into the reporting currency of the PLDT Group at the rate of exchange prevailing at the balance sheet date and its income and expenses are translated at the weighted average exchange rate for the period. The exchange differences arising on translation are taken directly to a separate component of equity as cumulative translation adjustments. On disposal of these subsidiaries, the amount of deferred cumulative translation adjustments recognized in equity relating to subsidiaries is recognized in the consolidated statement of income.

The functional currencies of the Group are the currency of the primary economic environment in which each entity operates. It is the currency that mainly influences the revenue and cost of rendering services.

#### **4. Segment Information**

Operating segments are components of PLDT that engage in business activities from which they may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of PLDT), whose operating results are regularly reviewed by the enterprise's chief operating decision-maker to make decisions about how resources are to be allocated to the segment and assess their performances, and for which discrete financial information is available. The accounting policies of the reportable segments are the same as those described in *Note 2 Summary of Significant Accounting Policies and Practices*.

We have organized our business into three main segments:

- **Wireless** - wireless telecommunications services provided through our cellular service providers namely, Smart and Piltel; Smart Broadband, our wireless broadband provider; Wolfpac, our wireless content operator; Mabuhay Satellite, ACeS Philippines and Telesat, our satellite and very small aperture terminal, or VSAT operators;
- **Fixed Line** - fixed line telecommunications services are primarily provided through PLDT. We also provide fixed line services through PLDT's subsidiaries: ClarkTel, SubicTel, Maratel, Piltel, BCC, PLDT Global and SNMI, which together account for approximately 3% of our consolidated fixed line subscribers; and

- ICT - information and communications infrastructure and services for internet applications, internet protocol-based solutions and multimedia content delivery provided by PLDT's subsidiary ePLDT; BPO provided services by SPi Group (consolidated on July 11, 2006); call center services provided under the umbrella brand name *ePLDT Ventus*, include Ventus, Parlance and Vocativ; internet access and online gaming services provided by ePLDT's subsidiaries, namely, Infocom, Digital Paradise, Digital Paradise Thailand, netGames, Airborne Access and Level Up!; and e-commerce and IT-related services provided by other investees of ePLDT, as described in *Note 9 Investments in Associates*.

Transfer prices between business segments are set on an arm's-length basis in a manner similar to transactions with third parties. Segment revenue, segment expense and segment result include transfers between business segments. These transfers are eliminated in consolidation.

The segment assets as at September 30, 2007 and December 31, 2006 and results of operations of our reportable segments for the nine months ended September 30, 2007 and 2006 are as follows:

	Wireless	Fixed Line	ICT	Inter-segment Transactions	Total
	(in million pesos)				
<i>As at and for the nine months ended September 30, 2007 (Unaudited)</i>					
<b>Income</b>					
Service revenues	64,059	35,664	7,416	(6,669)	100,470
Non-service revenues	1,630	119	200	(89)	1,860
Other income	718	459	27	(66)	1,138
Segment income	66,407	36,242	7,643	(6,824)	103,468
<b>Result</b>					
Income (loss) before income tax	34,068	5,978	(66)		39,980
Provision for (benefit from) income tax	11,121	1,980	(73)		13,028
Net income for the period	22,947	3,998	7		26,952
<b>Assets and liabilities</b>					
Segment assets	82,559	172,848	19,456	(60,700)	214,163
Deferred income tax assets	1,113	12,545	150		13,808
Total assets	83,672	185,393	19,606	(60,700)	227,971
Segment liabilities	47,379	79,822	6,067	(9,512)	123,756
Deferred income tax liabilities			523		523
Total liabilities	47,379	79,822	6,590	(9,512)	124,279
<b>Other segment information</b>					
Capital expenditures	7,085	7,049	395		14,529

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Depreciation and amortization	8,907	9,330	715	18,952
Provisions	272	857	15	1,144
Interest on loans and related items - net of capitalized interest	1,081	3,525	24	4,630
Interest income	860	238	14	1,112

*As at December 31, 2006 (Audited) and for the nine months ended September 30, 2006 (Unaudited)*

**Income**

Service revenues	58,016	35,901	3,788	(5,702)	92,003
Non-service revenues	1,842	71	339	(92)	2,160
Equity share in net income of associates			1		1
Other income	630	657	18	(69)	1,236
Segment income	60,488	36,629	4,146	(5,863)	95,400

**Result**

Income before income tax	28,833	647	18		29,498
Provision for (benefit from) income tax	3,076	60	(5)		3,131
Net income for the period	25,757	587	23		26,367

**Assets and liabilities**

Segment assets	86,905	184,096	17,431	(66,198)	222,234
Deferred income tax assets	4,991	14,608	59		19,658
Total assets	91,896	198,704	17,490	(66,198)	241,892

Segment liabilities	48,751	91,192	3,396	(6,372)	136,967
Deferred income tax liabilities	6		396		402
Total liabilities	48,757	91,192	3,792	(6,372)	137,369

**Other segment information**

Capital expenditures	9,152	6,983	737		16,872
Depreciation and amortization	7,948	15,248	463		23,659
Provisions	397	478	(3)		872
Interest on loans and related items - net of capitalized interest	1,069	4,603	13		5,685
Interest income	911	373	13		1,297

**5. Income and Expenses**

*Non-service Revenues*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Sale of computers, cellular handsets and SIM-packs	<b>1,749</b>	1,913
Point-product sales	<b>111</b>	247
	<b>1,860</b>	2,160

*Compensation and Benefits*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Salaries and benefits	<b>12,723</b>	9,643
Pension (Note 21)	<b>1,180</b>	760
Incentive plan (Notes 3 and 21)	<b>1,100</b>	2,677
Manpower rightsizing program	<b>586</b>	104
	<b>15,589</b>	13,184

*Financing Costs*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Interest on loans and related items	<b>5,029</b>	6,113
Hedge costs (Note 24)	<b>908</b>	1,090
Accretion on financial liabilities net (Notes 2, 17 and 24)	<b>834</b>	3,045
Loss on derivative transactions net (Notes 2 and 24)	<b>207</b>	151
Financing charges	<b>38</b>	44

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Dividends on preferred stock subject to mandatory redemption (Note 7)	<b>14</b>	113
Capitalized interest (Notes 2 and 8)	<b>(399)</b>	(428)
Interest income	<b>(1,112)</b>	(1,297)
Foreign exchange gains net (Notes 17 and 24)	<b>(1,662)</b>	(1,601)
	<b>3,857</b>	7,230

Interest expense for short-term borrowing for the nine months ended September 30, 2007 and 2006 amounted to Php23 million and Php10 million, respectively.

*Cost of Sales*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Cost of computers, cellular handsets and SIM-packs sold	<b>3,439</b>	3,567
Cost of point-product sales	<b>184</b>	293
Cost of satellite air time and terminal units (Notes 20 and 22)	<b>122</b>	146
	<b>3,745</b>	4,006

*Professional and Other Contracted Services*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Technical and consultancy fees (Note 20)	<b>1,979</b>	1,306
Contracted services	<b>1,265</b>	711
Legal and audit fees	<b>129</b>	158
Others	<b>95</b>	52
	<b>3,468</b>	2,227

*Provisions*

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Doubtful accounts (Notes 3 and 14)	<b>1,054</b>	697
Write-down of inventories to net realizable values (Note 15)	<b>62</b>	189
Assessments (Notes 20, 22 and 23)	<b>28</b>	(14)
	<b>1,144</b>	872

**6. Income Tax**

The net components of deferred income tax assets (liabilities) recognized in the consolidated balance sheets are as follows:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
	(in million pesos)	
Net assets	<b>13,808</b>	19,658
Net liabilities	<b>(523)</b>	(402)

The components of the consolidated net deferred income tax assets and liabilities are as follows:

<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
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(in million pesos)

Net assets		
Net operating loss carryover, or NOLCO	<b>6,555</b>	4,983
Accumulated provision for doubtful accounts	<b>4,662</b>	4,746
Unearned revenues	<b>2,620</b>	2,076
Derivative financial instruments	<b>1,968</b>	1,878
Pension and other employee benefits	<b>1,151</b>	2,568
Unamortized past service pension costs	<b>1,018</b>	871
Asset impairment	<b>933</b>	5,432
Provision for unrealized assets	<b>639</b>	732
Leases	<b>333</b>	304
Accumulated write-down of inventories to net realizable values	<b>294</b>	321
Asset retirement obligation net of capitalized asset	<b>226</b>	191
Unrealized foreign exchange losses	<b>143</b>	2,632
Executive stock option plan	<b>31</b>	106
Excess of fair value over cost of investment properties	<b>(78)</b>	(77)
Preferred stock subject to mandatory redemption	<b>(84)</b>	(109)
Intangible assets and fair value adjustments on assets acquired	<b>(332)</b>	(391)
Capitalized taxes and duties	<b>(393)</b>	(446)
Capitalized foreign exchange differential	<b>(822)</b>	(988)
Gain on debt exchange and debt restructuring transactions	<b>(1,378)</b>	(1,650)
Undepreciated capitalized interest charges	<b>(4,300)</b>	(4,607)
Others	<b>622</b>	1,086
	<b>13,808</b>	19,658
Net liabilities		
Unearned revenues	<b>(1)</b>	(1)
Excess of fair value over cost of investment properties	<b>(68)</b>	(38)
Intangible assets and fair value adjustments on assets required	<b>(454)</b>	(357)
Unrealized foreign exchange gains		(6)
	<b>(523)</b>	(402)

Provision for corporate income tax consists of:

	<b>Nine Months</b>	
	<b>Ended</b>	
	<b>September 30,</b>	
	<b>2007</b>	<b>2006</b>
	(Unaudited)	
	(in million	
	pesos)	
Current	<b>7,271</b>	7,222
Deferred	<b>5,757</b>	(4,091)
	<b>13,028</b>	3,131

The reconciliation between the provision for income tax at the applicable statutory tax rates and the actual provision for corporate income tax is as follows:

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Provision for corporate income tax at the applicable statutory tax rates	<b>13,993</b>	10,324
Tax effects of:		
Non-deductible expenses	<b>256</b>	65
Equity share in net loss of investees	<b>6</b>	
Income subject to lower tax rate	<b>(386)</b>	(176)
Income subject to final tax	<b>(398)</b>	(433)
Income not subject to tax	<b>(443)</b>	(1,095)
Net movement in deferred income tax		(5,554)
Actual provision for corporate income tax	<b>13,028</b>	3,131

Mabuhay Satellite and SubicTel are registered as Subic Bay Freeport Enterprises while ClarkTel is registered as a Clark Special Economic Zone Enterprise under Republic Act No. 7227, or R.A. 7227, otherwise known as the Bases Conversion and Development Act of 1992. As registrants, Mabuhay Satellite, SubicTel and ClarkTel are entitled to all the rights, privileges and benefits established thereunder including tax and duty-free importation of capital equipment and a special income tax rate of 5% of gross income, as defined in R.A. 7227.

On December 22, 2000, the Philippine Board of Investments, or BOI, approved ePLDT's registration as a new information technology, or IT, service firm in the field of services related to its internet data center on a pioneer status. As such, ePLDT enjoys, among other incentives, a six-year income tax holiday, or ITH, starting January 2001.

On January 3, 2007, the BOI approved ePLDT's application for pioneer status for its new data center facility as a new IT service firm in the field of services related to Internet Data Center. ePLDT was granted a six-year ITH on its new data center facility from January 2007 or actual start of operations, whichever comes first. ePLDT started commercial operations of its new data center facility in February 2007.

On August 13, 2007, ePLDT received approval from the Philippine Economic Zone Authority, or PEZA, to declare the Vitro Data Center Building as a PEZA-registered IT Building EcoZone facility enabling prospective clients to apply for fiscal incentives should they qualify as a PEZA-registered entity. However, ePLDT as a developer/operator of Vitro Data Center Building shall not be entitled to PEZA incentives under R.A. No. 7916, or R.A. 7916, otherwise known as The Special Economic Zone Act of 1995, as amended by Republic Act No. 8748, or R.A. 8748.



Parlance is registered with the BOI as a new IT export service firm in the field of customer interaction center on a pioneer status. Under this registration, Parlance is entitled to certain tax incentives, including an ITH for six years starting in June 2002. Parlance is required to comply with specific terms and conditions stated in its BOI registration.

iPlus Intelligent Network, Inc., or iPlus, is a wholly-owned subsidiary of ePLDT and is registered with the BOI as a new IT service firm in the field of application service provider on a pioneer status. Under such registration, iPlus is entitled to a six-year ITH incentive from the actual start of commercial operations until January 1, 2009.

Vocativ is registered with the PEZA as an Ecozone Export Enterprise to develop and operate a call center business that serves overseas clients by providing customer relationship management services. As a registered enterprise, Vocativ is entitled to certain tax and non-tax incentives which include, among other things, tax and duty-free importations, exemption from local tax and an ITH for four years from start of commercial operations. After the ITH period, Vocativ is liable for a final tax, in lieu of all taxes, of 5% gross income less allowable deductions as defined under R.A. 7916. The 5% final tax must be paid and remitted in accordance with the amendments contained in R.A. 8748, as follows: (a) 3% to the National Government; and (b) 2% which will be directly remitted by the business establishments to the treasurer's office of the municipality or city where the enterprise is located.

On December 5, 2005, Vocativ received approval from PEZA for the adjustment of the start of its commercial operations, effectively extending the ITH to end of March 2006. On June 30, 2006, PEZA approved Vocativ's ITH extension for another year which extends the ITH until April 2007. On September 3, 2007, PEZA approved Vocativ's ITH extension for another year which extends the ITH until March 2008.

mySecureSign, Inc., or mSSI, is a wholly-owned subsidiary of ePLDT and is registered with the BOI as a new IT service firm in the field of services related to public key infrastructure on a pioneer status. Under such registration, mSSI enjoys, among other incentives, a six-year ITH from August 1, 2001 or the actual start of commercial operations, whichever comes first. mSSI started commercial operations on January 1, 2002.

Ventus is registered with the BOI as a new IT export service firm in the field of customer interaction center on a pioneer status. Under this registration, Ventus is entitled to certain tax incentives such as an ITH for six years starting March 2005. In relation to this, Ventus is required to comply with specific terms and conditions stated in the BOI registration.

Two of Ventus' call center projects are registered with the BOI as a new IT export service firm in the field of customer interaction center on a pioneer status. Under this registration, Ventus' Iloilo and Pasig call center projects are entitled to certain tax incentives such as an ITH for six years starting March 2005 and August 2006, respectively. In relation to this, Ventus is required to comply with specific terms and conditions stated in its BOI registration.

Digital Paradise is registered with the BOI as a new IT service firm in the field of community access on a non-pioneer status. Under the provisions of the registration, Digital Paradise's sales generated from its own community access activity and franchise fees are entitled to an ITH for a period of four years beginning December 2002. In December 2006, the BOI approved Digital Paradise's application for a status upgrade from non-pioneer to pioneer, accordingly extending the ITH period for another two years starting January 2007.

Level Up! was originally registered with the BOI as a new IT service firm in the field of application service provider on a non-pioneer status. Under such registration, Level Up! is entitled to certain tax incentives, which includes a four-year ITH from January 2003 and a tax credit for taxes on duties on materials used in export products for ten years starting January 2003. In April 2004, the BOI approved Level Up!'s request for upgrading its status from non-pioneer to pioneer in connection with its IT service activity in the field of application service provider for entertainment and educational project. Accordingly, the ITH period was extended from four years to six years.

In September 2006, PEZA approved SPi's application for registration as an ecozone information technology enterprise to provide IT enabled services with emphasis on the creation of electronic discovery, presentation of content in electronic information formats, data analysis, capture, abstracting and data processing, design, development and implementation of healthcare documentation solutions. As a registered enterprise, SPi is entitled to certain tax and non-tax incentives which include, among other things, tax and duty-free importations, exemption from local tax and an ITH for four years. After the ITH period, SPi is liable for a final tax, in lieu of all taxes. The final tax is computed at 5% of gross income less allowable deductions as defined under R.A. 7916 and will be paid and remitted in accordance with the amendments contained in R.A. 8748, as follows: (a) 3% to the National Government; and (b) 2% which will be directly remitted by the business establishments to the treasurer's office of the municipality or city where the enterprise is located.

Wolfpac is registered with the BOI as a new operator of service provider applications. Under the terms of its registration, it is entitled to certain tax and non-tax incentives which include, among other things, an ITH for four years starting February 2004.

Smart Broadband has three registered activities with the BOI on a pioneer status, namely: (i) a new operator of telecommunications systems (inter-exchange carrier for data services); (ii) new information technology service firm in the field of providing internet services; and (iii) a new operator of telecommunications facilities (nationwide broadband wireless access). Under the terms of these registrations, Smart Broadband is entitled to certain tax and non-tax incentives which include, among other things, an ITH for six years from February 2001, August 2001 and July 2005, respectively.

The first two registered activities (new operator of telecommunications systems and new information technology service firm in the field of providing internet services) have expired in February 2007 and September 2007, respectively. The remaining registered activity, which is the new operator of telecommunications facilities (nationwide broadband wireless access) will expire in August 2011.

Income derived from non-registered activities with the BOI is subject to the normal income tax rate enacted as at the balance sheet date.

Consolidated tax incentives that we availed for the nine months ended September 30, 2007 and 2006 amounted to Php377 million and Php157 million, respectively.

On May 24, 2005, the president of the Philippines signed into law Republic Act No. 9337, or R.A. 9337, amending certain sections of the National Internal Revenue Code, which took effect on November 1, 2005. R.A. 9337, among others, introduced the following changes:

- a. The regular corporate income tax rate for domestic corporations and resident/non-resident foreign corporations increased from 32% to 35% effective November 1, 2005 and will be reduced to 30% effective January 1, 2009.
- b. The VAT rate increased from 10% to 12% effective February 1, 2006.
- c. The input VAT on capital goods should be spread evenly over the estimated useful life or sixty months, whichever is shorter, if the acquisition cost, excluding the VAT component thereof, exceeds Php1 million.

Our deferred income tax assets have been recorded to the extent that such deferred income tax assets are expected to be utilized against sufficient future taxable profit. We had unrecognized deferred income tax assets of Php322 million and Php299 million largely pertaining to asset impairment as at September 30, 2007 and December 31, 2006, respectively.

Our unaudited consolidated unutilized NOLCO as at September 30, 2007 is as follows:

<b>Year Incurred</b>	<b>Year Expiring (in million pesos)</b>	
2004	2007	15
2005	2008	8,742
2006	2009	5,600
2007	2010	4,379
		18,736
Tax benefit		6,558

Unrecognized deferred income tax assets from NOLCO as at September 30, 2007 (Unaudited)	(3) 6,555
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Our unaudited consolidated MCIT as at September 30, 2007 is as follows:

<b>Year Incurred Year Expiring (in million pesos)</b>		
2005	2008	484
2006	2009	499
2007	2010	532
		1,515

## 7. Earnings Per Common Share

The following table presents information necessary to calculate the earnings per common share:

	<b>Nine Months Ended September 30,</b>			
	<b>2007</b>		<b>2006</b>	
	<b>Basic</b>	<b>Diluted</b>	Basic	Diluted
	(Unaudited)			
	(in million pesos)			
Consolidated net income attributable to equity holders of PLDT	<b>26,506</b>	<b>26,506</b>	25,744	25,744
Dividends on preferred shares	<b>(341)</b>	<b>(341)</b>	(342)	(37)
Dividends on dilutive preferred stock subject to mandatory redemption charged to interest expense for the period		<b>13</b>		
Accretion of preferred stock subject to mandatory redemption		<b>106</b>		
Foreign exchange gain on preferred stock subject to mandatory redemption		<b>(98)</b>		
Consolidated net income applicable to common shares	<b>26,165</b>	<b>26,186</b>	25,402	25,707

(in thousands, except per share amounts)

Outstanding common shares at beginning of period	<b>188,435</b>	<b>188,435</b>	180,789	180,789
Effect of issuance of common shares during the period	<b>197</b>	<b>197</b>	2,342	2,342
Average incremental number of shares under ESOP during the period		<b>41</b>		92
Common shares equivalent of preferred shares deemed dilutive:				

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Preferred Stock Series A to EE (Note 16)				2,284
Preferred Stock Series VI (Note 17)			<b>706</b>	
Weighted average number of common shares for the period	<b>188,632</b>	<b>189,379</b>	183,131	185,507
Earnings per common share	<b>Php138.71</b>	<b>Php138.27</b>	Php138.71	Php138.58

Series VI Convertible Preferred Stocks in 2007 and Series A to EE Convertible Preferred Stocks in 2006 were deemed dilutive based on a calculation of the required dividends on these preferred shares divided by the number of equivalent common shares assuming such preferred shares are converted into common shares, including the effect of shares under ESOP, and compared against the basic EPS. Since the amount of dividends on the Series A to EE and Series V Convertible Preferred Stocks in 2007 and Series V and VI Convertible Preferred Stocks in 2006 over its equivalent number of common shares increased the basic EPS, these Convertible Preferred Stocks were anti-dilutive.

**Dividends Declared For The Nine Months Ended September 30, 2007**

Class	Date			Per Share	Total (in million pesos)
	Approved	Record	Payable		
<b>Preferred Stock Subject to Mandatory Redemption</b>					
Series V	March 6, 2007	March 20, 2007	April 15, 2007	Php4.675	
	June 12, 2007	June 28, 2007	July 15, 2007	4.675	
	September 14, 2007	September 28, 2007	October 15, 2007	4.675	
Series VI	March 6, 2007	March 20, 2007	April 15, 2007	US\$0.09925	4
	June 12, 2007	June 28, 2007	July 15, 2007	0.09925	3
	September 14, 2007	September 28, 2007	October 15, 2007	0.09925	3
Charged to income					10
<b>10% Cumulative Convertible Preferred Stock</b>					
Series CC	January 30, 2007	February 28, 2007	March 30, 2007	Php1.00	17
	January 31, 2007	February 15, 2007	February 28, 2007	1.00	2
Series DD	March 27, 2007	April 26, 2006	May 31, 2007	1.00	
Series A, I, R, W, AA and BB	July 10, 2007	August 1, 2007	August 31, 2007	1.00	129
		September 3, 2007	September 28, 2007	1.00	91
Series B, F, Q, V and Z	August 7, 2007	September 14, 2007	October 31, 2007	1.00	44
Series E, K, O and U		October 4, 2007		1.00	57
Series C, D, J, T and X				1.00	
					<b>133</b>

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	September 14, 2007	October 14, 2007	November 27, 2007		340
<b>Cumulative Non-Convertible Redeemable Preferred Stock</b>					
Series IV*	January 30, 2007	February 23, 2007	March 15, 2007	Php	12
	May 8, 2007	May 25, 2007	June 15, 2007		13
	July 10, 2007	August 9, 2007	September 15, 2007		12
					37
<b>Common Stock</b>					
Regular Dividend	March 6, 2007	March 20, 2007	April 20, 2007	Php50.00	9,429
	August 7, 2007	August 24, 2007	September 24, 2007	60.00	11,322
Special Dividend	August 7, 2007	August 24, 2007	September 24, 2007	40.00	7,548
					28,299
Charged to retained earnings					28,676

\* Dividends are declared based on total amount paid up

**Dividends Declared After September 30, 2007**

Class	Approved	Date		Payable	Per Share	Amount Total (in million pesos)
		Record				
<b>Cumulative Non-convertible Redeemable Preferred Stock</b>						
Series IV*	November 6, 2007	November 23, 2007	December 15, 2007		Php	12
<b>10% Cumulative Convertible Preferred Stock</b>						
Series G, N, P and S	November 6, 2007	December 6, 2007	December 28, 2007		Php1.00	27
						39

\* Dividends are declared based on total amount paid up

**8. Property, Plant and Equipment**

This account consists of:

	Cable and wire facilities	Central office equipment	Cellular facilities	Buildings	Vehicles, furniture, and other network equipment	Communications satellite	Information origination and equipment	Land and land improvements	Property under construction	T
	(in million pesos)									
<b>September 31, 2006 (Audited)</b>	112,621	84,604	64,423	20,376	31,039	9,834	9,140	2,685	12,686	3
Accumulated depreciation and amortization	(46,594)	(58,292)	(32,889)	(6,235)	(25,461)	(7,678)	(5,800)	(269)		(18
Book value	66,027	26,312	31,534	14,141	5,578	2,156	3,340	2,416	12,686	1
<b>9 months Ended September 30, 2007 (Unaudited)</b>										
Book value at beginning of period	66,027	26,312	31,534	14,141	5,578	2,156	3,340	2,416	12,686	1
Acquisitions/Transfers	2,876	2,075	1,337	203	1,362		1,539	2	5,093	
Disposals/Retirements	(137)	(46)	(47)	(8)	(41)			(14)	(27)	
Impairment charges charged to cumulative impairment	(2)	(4)		(10)	(5)	(274)			(10)	
Disposals through business combination and reclassifications	868	(156)	3,407	6	938		(1,750)		(3,300)	
Depreciation and amortization (Note 4)	(4,997)	(3,900)	(5,366)	(874)	(2,569)	(427)	(816)	(3)		(1
Book value at end of period	64,635	24,280	30,865	13,471	5,426	1,455	2,313	2,401	14,442	1
<b>September 30, 2007 (Unaudited)</b>	115,236	86,301	67,001	20,567	32,739	9,098	8,149	2,672	14,442	3
Accumulated depreciation and amortization	(50,601)	(62,021)	(36,136)	(7,096)	(27,313)	(7,643)	(5,836)	(271)		(19
Book value	64,635	24,280	30,865	13,471	5,426	1,455	2,313	2,401	14,442	1

Substantially all our telecommunications equipment is purchased from outside the Philippines. Our significant sources of financing for such purchases are foreign loans requiring repayment in currencies other than Philippine pesos, principally in U.S. dollars, see *Note 17 Interest-bearing Financial Liabilities*. Interest, using an average capitalization rate of 10%, and net foreign exchange losses capitalized to property, plant and equipment qualified as borrowing costs for the nine months ended September 30, 2007 and 2006 were as follows:

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Interest	<b>399</b>	428
Foreign exchange loss (gains)	<b>(63)</b>	239

As at September 30, 2007 and December 31, 2006, the undepreciated capitalized net foreign exchange losses which qualified as borrowing costs amounted to Php2,064 million and Php2,646 million, respectively.

The consolidated useful lives of the assets are estimated as follows:

Buildings	25 years
Cable and wire facilities	10 25 years
Central office equipment	10 20 years
Communications satellite	15 years
Information origination and termination equipment	3 15 years
Land improvements	10 years
Vehicles, furniture and other network equipment	3 10 years
Cellular facilities	3 10 years

We recognized additional depreciation charge of Php1,100 million and Php5,823 million for the nine months ended September 30, 2007 and 2006, respectively, due to a change in the estimated useful lives of certain of our network assets owing to continuing network upgrade and expansion.



*Asset Impairment Review*

Piltel carries out annual impairment tests on its fixed line assets based on the net present value, or NPV, of future cash flows from the continued use of these assets. For the impairment review in 2006, a discount factor of 6.25% on a pre-tax basis was used for both E.O. 109 and RTS business, applied on cash flow projections from 2007 until such year when the bulk of assets are fully depreciated. Cash flow assumptions for E.O. 109 averaged Php64 million per year from 2007 to 2017 and for RTS averaged Php271 million per year from 2007 to 2013. The resulting NPV of the total cash flow projections was higher than the carrying value of both the E.O. 109 and RTS assets.

Management believes that due to Mabuhay Satellite's difficulty in generating cash flows with the satellite nearing its end-of-life and other events affecting its business, Mabuhay Satellite's Agila II transponder is considered impaired. This impairment review is based on the NPV of future cash flows from the continued use of this asset using the discount factor of 10% as applied on cash flow projections from 2007 until 2010. An impairment loss of Php1,391 million was applied to the carrying value of this satellite as at December 31, 2006 and included in the accumulated depreciation and amortization account in the unaudited consolidated balance sheet as at September 30, 2007 and December 31, 2006.

Property, plant and equipment include the following amounts for capitalized leases as at September 30, 2007 and December 31, 2006:

	September 30, 2007 (Unaudited)			December 31, 2006 (Audited)		
	Central office equipment	Vehicles, furniture and other network equipment	Total	Central office equipment	Vehicles, furniture and other network equipment	Total
Cost	354	1,187	1,541	354	1,183	1,537
Less accumulated depreciation	327	1,088	1,415	310	950	1,260
	27	99	126	44	233	277

(in million pesos)

The following table summarizes all changes to the liabilities on asset retirement obligations as at September 30, 2007 and December 31, 2006:

	September 30, 2007 (Unaudited)	December 31, 2006 (Audited)
Asset retirement obligations at beginning of period	831	752
Accretion expenses	62	87
Additional liability recognized during the period	21	45

(in million pesos)

Settlement of obligations	(5)	(53)
Asset retirement obligations at end of period (Notes 3 and 18)	<b>909</b>	831

## 9. Investments in Associates

This account consists of:

	<b>September 30,</b> <b>2007</b> <b>(Unaudited)</b>	December 31, 2006 <b>(Audited)</b>
	(in million pesos)	
ACeS International Limited	<b>1,614</b>	1,614
Mabuhay Space Holdings Limited	<b>859</b>	937
Blue Ocean Wireless	<b>724</b>	
Philweb Corporation	<b>712</b>	712
Stradcom International Holdings, Inc.	<b>616</b>	616
BayanTrade Dotcom, Inc.	<b>97</b>	97
ePDS, Inc.	<b>6</b>	6
	<b>4,628</b>	3,982
Less accumulated impairment losses and equity share in net losses of associates	<b>3,285</b>	3,346
	<b>1,343</b>	636

### *Investment of ACeS Philippines in ACeS International Limited, or AIL*

As at September 30, 2007 and December 31, 2006, ACeS Philippines had a 36.99% and 20% investment in AIL, respectively, a company incorporated under the laws of Bermuda. AIL owns the Garuda I Satellite and the related system control equipment in Batam, Indonesia.

AIL has incurred recurring significant operating losses, negative operating cash flows, and significant levels of debt. The financial condition of AIL was partly due to the National Service Providers, or NSPs, inability to generate the amount of revenues originally expected as the growth in subscriber numbers has been significantly lower than budgeted. These factors raise substantial doubt about AIL's ability to continue as a going concern. On this basis, we recognized a full impairment provision in respect of our investment in AIL amounting to Php1,614 million in 2003.

For further details as to the contractual relationships in respect of AIL, see *Note 20 Related Party Transactions*.

***Investment of Mabuhay Satellite in Mabuhay Satellite Space Holdings Limited, or MSHL***

In 1996, Mabuhay Satellite entered into a Joint Venture Agreement, or JVA, with Space Systems/Loral Inc., or SS/L, to form MSHL for the purpose of providing high-power Ku-Band satellite transmission services using the payload which was added by SS/L to the Agila II Satellite. Under the terms of the JVA, SS/L is required to convey title to the additional payload service to MSHL in consideration for SS/L's 35% equity interest in MSHL, and Mabuhay Satellite is required to pay SS/L US\$19 million for a 65% equity interest in MSHL.

In 2000, SS/L filed a Notice of Default and Termination against Mabuhay Satellite arising from the latter's alleged failure to amicably resolve its unpaid obligation to SS/L under the JVA. In 2002, the arbitration panel handed down its decision and provided for payment by Mabuhay Satellite to SS/L of the principal amount of US\$10 million plus accrued interest at 9% per annum. On June 30, 2003, Mabuhay Satellite and SS/L concluded a US\$15 million settlement agreement under which Mabuhay Satellite leased two transponders under a transponder agreement on a life-term basis to SS/L and offset the lease charges due from SS/L and its receivables from Loral Skynet Network Services, Inc. (formerly known as the Loral Cyberstar, Inc.), among other things, for a full and final settlement of the arbitration decision. The agreement was subsequently approved by Mabuhay Satellite's creditors in March 2004.

In accordance with the settlement agreement, Mabuhay Satellite and SS/L shall proceed to dissolve the joint venture under a separate agreement, for which each of the parties will receive title over a number of transponders owned by the joint venture in proportion to their respective interests. On the basis of the joint venture dissolution, we recognized an impairment provision in respect of our investment in MSHL of Php431 million in 2004.

***Investment of Smart in Blue Ocean Wireless, or BOW***

On August 3, 2007, Smart has agreed to acquire a 30% equity interest in Blue Ocean Wireless, or BOW, a Dublin-based company delivering GSM communication capability for the merchant maritime sector. Total acquisition cost amounted to US\$15.9 million, or Php724 million, of which Php601 million was paid in cash and Php123 million will be paid in kind. BOW provides the world's first GSM network on the seas through Altobridge, a patented GSM platform that supports full voice and text services, thus providing an important complementary service to Smart's prepaid wireless satellite phone service, *SMARTLink*.

***Investment of ePLDT in Philweb Corporation, or Philweb***

In May 2006, ePLDT subscribed newly issued common shares of Philweb, an internet-based online gaming company, equivalent to 20% of the total outstanding capital stock of Philweb at a price of Php0.020 per share or an aggregate amount of Php502 million. Of the total subscription price, Php427 million was paid by ePLDT on the closing date. The portion of the unpaid subscription price amounting to Php25 million will be paid by ePLDT at the same time as the Philweb majority stockholders pay the remaining unpaid portion of the subscription pursuant to a general call on subscription to be made by Philweb's board of directors. The balance of Php50 million will be paid upon the lapse of certain post-closing price adjustment periods. The unpaid subscription of Php75 million was recorded as part of accrued expenses and other current liabilities in the unaudited balance sheet.

In October 2006, ePLDT acquired an additional 8,037,692,308 shares of Philweb at a price of Php0.026 per share or an aggregate amount of Php209 million. This represents an additional 6.2% of the outstanding shares of Philweb, raising ePLDT's total equity stake to 25.5% as at December 31, 2006.

Philweb is primarily engaged in internet-based online gaming, through its appointment as Principal Technology Service Provider under the Marketing Consultancy Agreement for Internet Sports Betting and Internet Casino with the Philippine Amusement and Gaming Corporation, or PAGCOR. As of the end of September 2007, Philweb offers Internet Sports Betting in over 239 PAGCOR Internet Sports Betting Stations and over 60 Internet Casino Stations nationwide. As at September 30, 2007, the market value of ePLDT's investments in Philweb amounted to Php1,741 million.

***Investment of ePLDT in Stradcom International Holdings, Inc., or SIHI***

ePLDT has a 22.5% interest in convertible securities of SIHI, the parent company of Stradcom Corporation, which has an existing concession agreement with the Philippine Government for the modernization of the Philippine Land Transportation Office, including the computerization of driver's license issuance, vehicle registration and traffic adjudication systems. SIHI has been incurring losses from the start of operations due to Stradcom Corporation's continuous losses and recurring excess of current liabilities over current assets. On this basis, we recognized an impairment provision in respect of our investment in SIHI of Php616 million in 2004.

In 2007, Stradcom Corporation entered into a Lenders' Agreement for the issuance of Asset-Backed Bonds amounting to Php1.6 billion intended for debt refinancing and general corporate purposes, including working capital and investments.

***Investment of ePLDT in BayanTrade Dotcom, Inc., or BayanTrade***

BayanTrade was incorporated and registered with the Philippine Securities and Exchange Commission, or Philippine SEC, on August 8, 2000 to provide: (a) a business-to-business electronic purchasing market place to link buyers and suppliers of goods and services over the internet; (b) electronic catalogue purchasing facilities over the internet to buyers and suppliers; (c) link-up with similar horizontal markets and vertical markets across the Asia-Pacific Region and the world; and (d) facilitating services incidental to the business. BayanTrade is an e-procurement joint venture established together with six of the Philippines' leading conglomerates. ePLDT's initial shareholding in BayanTrade was 20.5%, which was subsequently diluted to 19.17% in August 2004 due to an equity call to which ePLDT did not subscribe.

In September 2005, ePLDT received 4,794,615 bonus warrants from BayanTrade which entitles ePLDT to purchase 2,794,615 common shares at a price of Php0.50 per share at any time on or before August 31, 2010. We did not account for the value of bonus warrants because the value is not material.

***Investment of ePLDT in ePDS, Inc., or ePDS***

On June 30, 2003, ePLDT signed a joint venture agreement with DataPost Pte Ltd., or DataPost, a subsidiary of Singapore Post, and G3 Worldwide ASPAC, or Spring, pursuant to which the parties formed ePDS, a bills printing company which does laser printing and enveloping services for statements, bills and invoices, and other value-added services for companies in the Philippines. ePLDT has a 50% interest in ePDS, while DataPost has a 30% interest. Spring, the largest international mail services provider, owns the remaining 20%. ePDS has an initial paid-up capital of Php11 million.

In October 2005, ePDS' Board of Directors approved the declaration of a 100% stock dividend on its common stock equivalent to Php11 million. The stock dividends were issued from the increase in authorized capital stock of ePDS which was approved by the Philippine SEC in June 2006.

***Summarized Financial Information of Equity Investees***

The following table presents summarized financial information in conformity with PFRS for equity investees for which we have significant influence as at September 30, 2007 and December 31, 2006 and for the nine months ended September 30, 2007 and 2006.

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Noncurrent assets	<b>1,458</b>	1,333

Current assets	<b>914</b>	1,122
Capital deficiency	<b>(8,935)</b>	(9,618)
Noncurrent liabilities	<b>10,251</b>	10,029
Current liabilities	<b>1,056</b>	2,044

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Revenues	<b>726</b>	624
Revenues less cost of revenues	<b>431</b>	483
Expenses	<b>601</b>	390
Net loss	<b>(170)</b>	(321)

## 10. Investment Properties

	<b>September 30, 2007 December 31, 2006 (Unaudited) (Audited) (in million pesos)</b>	
Balance at beginning of period	<b>587</b>	701
Disposals	<b>(7)</b>	(112)
Net loss from fair value adjustments		(2)
Balance at end of period (Note 3)	<b>580</b>	587

Investment properties are stated at fair values, which have been determined based on the latest valuations performed by an independent firm of appraisers, which is an industry specialist in valuing these types of investment properties. The valuation undertaken was based on an open market value, supported by a market evidence in which assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's-length transaction at the date of valuation, in accordance with international valuation standards.

**11. Goodwill and Intangible Assets**

Movements in goodwill and intangible assets during the periods are as follows:

	<b>September 30, 2007 (Unaudited)</b>			December 31, 2006 (Audited)		
	<b>Goodwill</b>	<b>Intangible assets</b>	<b>Total</b>	<b>Goodwill</b>	<b>Intangible assets</b>	<b>Total</b>
	(in million pesos)					
Cost:						
Balance at beginning of period	<b>10,137</b>	<b>3,456</b>	<b>13,593</b>	1,942	1,991	3,933
Additions during the period	<b>2,266</b>	<b>338</b>	<b>2,604</b>	8,498	1,540	10,038
Translation adjustments	<b>(725)</b>	<b>(120)</b>	<b>(845)</b>	(303)	(75)	(378)
Balance at end of period	<b>11,678</b>	<b>3,674</b>	<b>15,352</b>	10,137	3,456	13,593
Accumulated amortization and impairment:						
Balance at beginning of period	<b>438</b>	<b>941</b>	<b>1,379</b>	438	446	884
Amortization during the period		<b>286</b>	<b>286</b>		450	450
Translation adjustments		<b>(14)</b>	<b>(14)</b>		(5)	(5)
Impairment during the period					50	50
Balance at end of period	<b>438</b>	<b>1,213</b>	<b>1,651</b>	438	941	1,379
Net balance (Note 3)	<b>11,240</b>	<b>2,461</b>	<b>13,701</b>	9,699	2,515	12,214

In relation to SPi's acquisition of Springfield, the fair value of Springfield's net assets, determined provisionally, was assessed to be equal to its book value, which resulted in goodwill amounting to

Php2,266 million. Intangible assets pertaining to Springfield's customer relationship and customer contracts were initially determined at Php338 million with estimated useful life of five and ten years, respectively. Valuation of intangible assets by independent appraiser is ongoing which is expected to be completed by fourth quarter of 2007.

Other intangible assets consist of:

	<b>Estimated Useful Lives</b>	<b>September 30, 2007 (Unaudited)</b>		December 31, 2006 (Audited)	
		<b>Gross Carrying Amount</b>	<b>Net Accumulated Amortization</b>	<b>Gross Carrying Amount</b>	<b>Net Accumulated Amortization</b>
		(in million pesos)			
Customer list	<b>10 years</b>	<b>1,551</b>	<b>347</b>	1,332	195
Spectrum	<b>15 years</b>	<b>1,205</b>	<b>248</b>	1,205	187
	<b>4 years</b>	<b>600</b>	<b>504</b>	601	471
			<b>96</b>		130

Technology  
application

Licenses	5	17 years	318 3,674	114 204 1,2132,461	318 3,456	88 230 9412,515
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As at December 2006, ePLDT has provided an impairment in value of its intangible assets in Level Up! amounting to Php50 million, representing a write-down of such intangible assets to recoverable amounts using the value-in-use approach. The impairment was a result of projected decline on revenues related to certain license agreements. Market value-in-use was based on the discounted cash flow projections using the most recent financial forecast approved by our management.

The future amortization of other intangible assets as at September 30, 2007 are as follows:

	(in million pesos)
2007(1)	49
2008	418
2009	403
2010	365
2011	296
2012 and onwards	930
Balance at end of period	2,461

(1) October 1, 2007 through December 31, 2007

### ***Impairment Testing of Goodwill***

#### *Goodwill from Acquisition of Smart Broadband*

The test for recoverability of Smart's goodwill was applied to an asset group, representing the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities.

Although revenue streams may be segregated between Smart and Smart Broadband through subscribers availing themselves of their respective cellular and wireless broadband services, the cost items and cash flows are difficult to carve out, largely due to the significant portion of shared and common-used networks/platforms. In the case of Smart Broadband, it provides broadband wireless access to its subscribers using Smart's cellular base stations, fiber optic and



IP backbone. With the common use of wireless assets with Smart in providing wireless services, the lowest asset group for Smart Broadband for which cash flows could be clearly identified from other groups of assets will be Smart's wireless business segment.

Our wireless business segment has been our largest revenue and cash flow contributor since 2003. As such, there is no impairment of our wireless business segment. As at December 31, 2006, the recoverable amount of this segment is determined on the basis of value in use calculations using cash flow projections based on the financial budgets approved by Smart's Management covering a 5-year period from 2007 to 2011. The pre-tax discount rate applied to cash flow projections is 10.6% and cash flows beyond the 5-year period are determined using a 2.5% growth rate that is the same as the long-term average growth rate for the telecommunications industry.

The calculation of value in use for Smart's wireless business segment was based on the following assumptions: (a) usage revenues for 2007 were based on the annualized actual year-to-date results available at the time the budget was prepared in 2006; (b) usage revenues were assumed to grow at an average rate of 5% per annum from 2007 to 2011; (c) average capital expenditures per year were assumed at Php8.6 billion from 2007 to 2011; (d) the discount rate used was the weighted average cost of capital; and (e) the growth rate used for cash flows beyond the budget period was based on published industry research.

Annual update in the impairment testing will be completed at year-end.

*Goodwill from Acquisition of SPi and its Subsidiary, CyMed*

The goodwill acquired through the SPi and CyMed transactions was allocated for impairment testing to each of the cash generating units of those businesses namely: healthcare, litigation and publishing.

As at December 31, 2006, we determined that there would be no impairment loss recognized for each of the cash generating units since the recoverable amount exceeded the carrying amount of the individual assets. The recoverable amount of goodwill was determined using the value in use approach. Value in use was based on the cash flow projections of the most recent financial budgets/forecasts approved by management, which management believes are reasonable and are management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.

In determining the appropriate discount rate to be applied, our weighted average cost of capital was used and adjusted for the difference in currency and specific risks associated with the assets or business of a cash-generating unit.

Management assessed the reasonableness of the assumptions by examining the causes of differences between actual 2006 cash flow and budgeted/projected cash flows, with a particular emphasis on the observed trends towards the last quarter of 2006.

Annual update in the impairment testing will be completed at year-end.

## 12. Notes Receivable

### *Investment of ePLDT in Debt Securities of Technology Support Services, Inc., or TSSI (formerly First Advance Multi-Media Entertainment Corp., or FAME)*

On June 1, 2004, ePLDT and FAME entered into an agreement whereby ePLDT granted a seven-year zero-coupon loan to FAME amounting to US\$3.1 million. Based on agreement, upon maturity of the loan, which is at the end of seven years from issuance, ePLDT may require FAME to redeem or pay the loan at a redemption value amounting to US\$6.1 million. At any time during the life of the outstanding loan, ePLDT may convert the loan into 20% of the total outstanding capital stock of FAME.

On August 20, 2004, FAME changed its corporate name to TSSI.

On September 14, 2004, ePLDT entered into a second agreement with TSSI whereby ePLDT granted another seven-year zero coupon loan to TSSI amounting to US\$3.1 million with the same terms and features as the first loan. As at September 30, 2007 and December 31, 2006, the aggregate loans of ePLDT to TSSI amounted to Php346 million.

TSSI has been incurring losses from the start of operations due to delays in its projects. On this basis, we recognized a full impairment provision in respect of our notes receivable from TSSI amounting to Php346 million in December 2006.

**13. Cash and Cash Equivalents**

This account consists of:

	<b>September 30,</b>	December 31, 2006
	<b>2007</b>	
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Cash on hand and in banks	<b>2,986</b>	3,416
Temporary cash investments	<b>5,485</b>	13,454
	<b>8,471</b>	16,870

Cash in banks earns interest at prevailing bank deposit rates. Temporary cash investments are made for varying periods of up to three months depending on our immediate cash requirements, and earn interest at the prevailing short-term deposit rates. Due to the short-term nature of such transactions, the carrying value approximates the fair value of our temporary cash investments.

**14. Trade and Other Receivables**

This account consists of receivables from:

	<b>September 30,</b>	December 31, 2006
	<b>2007</b>	
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Customers and carriers	<b>24,650</b>	25,349
Others (Notes 20, 22 and 23)	<b>1,641</b>	1,579
	<b>26,291</b>	26,928
Less allowance for doubtful accounts	<b>16,046</b>	16,770
	<b>10,245</b>	10,158

Movements in the allowance for doubtful accounts are as follows:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
	(in million pesos)	
Balance at beginning of period	<b>16,770</b>	18,525
Provisions for the period (Notes 3 and 5)	<b>1,054</b>	736
Translation adjustments	<b>(39)</b>	(24)
Write-offs	<b>(1,739)</b>	(1,813)
Reversals		(654)
Balance at end of period	<b>16,046</b>	16,770

On October 10, 2002, PLDT entered into a Receivables Purchase Deed, or RPD, with a foreign financial institution, or the Purchaser, under which PLDT agreed (1) to sell its receivables from certain eligible foreign carriers up to September 30, 2007 for an advance payment of US\$50 million and (2) to service, administer and collect the receivables on behalf of the Purchaser. Under the RPD, the Purchaser has no recourse against PLDT should an eligible carrier fail or refuse to settle the assigned/purchased receivables, except when PLDT commits a breach of its representations and warranties under the RPD.

Sale of receivables under the RPD amounted to US\$4 million, or Php167 million, and US\$4 million, or Php213 million, for the nine months ended September 30, 2007 and 2006, respectively. Loss on sale of receivables under the RPD amounted to US\$1 million, or Php6 million, and US\$1 million, or Php22 million, for the nine months ended September 30, 2007 and 2006, respectively.

## 15. Inventories and Supplies

This account consists of:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
	(in million pesos)	
Terminal and cellular phone units:		
At net realizable value	<b>808</b>	556
At cost	<b>933</b>	719
Spare parts and supplies:		

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At net realizable value	<b>684</b>	514
At cost	<b>1,527</b>	1,397
Others:		
At net realizable value	<b>149</b>	160
At cost	<b>150</b>	161
At lower of cost or net realizable value	<b>1,641</b>	1,230

## 16. Equity

The movement of PLDT's capital accounts as at December 31, 2006 and September 30, 2007 are as follows:

	<b>Preferred Stock</b>			<b>Common Stock</b>	
	Php10 par value per share			Php5 par value per share	
	<b>Series</b>	<b>Total Preferred Stock</b>		<b>No. of Shares</b>	<b>Amount</b>
	<b>A to EE IV</b>	<b>No. of Shares</b>	<b>Amount</b>	<b>No. of Shares</b>	<b>Amount</b>
			(in millions)		
<b>Authorized</b>			823	234	Php1,170
<b>Outstanding</b>					
Balance at January 1, 2006	407	36	443	181	Php904
Conversion	(1)		(1)	7	38
Issuance			2		
Balance at December 31, 2006 (Audited)	406	36	442	188	Php942
Balance at January 1, 2007	406	36	442	188	Php942
Conversion	(1)		(1)		1
Issuance			1	1	1
Balance at September 30, 2007 (Unaudited)	405	36	441	189	Php944

### *Preferred Stock*

The preferred stock is non-voting, except as specifically provided by law, and is preferred as to liquidation.

The Series A to EE 10% Cumulative Convertible Preferred Stocks earn cumulative dividends at an annual rate of 10%. After the lapse of one year from the last day of the year of issuance of a particular series of 10% Cumulative Convertible Preferred Stock, any holder of such series may convert all or any of the shares of 10% Cumulative Convertible Preferred Stock held by him into fully paid and non-assessable shares of Common Stock of PLDT, at a conversion price equivalent to 10% below the average of the high and low daily sales price of a share of Common Stock on the PSE, or if there have been no such sales on the PSE on any day, the average of the bid and the asked prices of a share of Common Stock of PLDT at the end of such day on such Exchange, in each such case averaged over a period of 30 consecutive trading days prior to the conversion date, but in no case shall the conversion price be less than the price set by the Board of Directors which, as at September 30, 2007, was Php5.00 per share. The number of shares of Common Stock issuable at any time upon conversion of one share of the subscriber investment plan, or SIP, or the 10% Cumulative Convertible Preferred Stock is determined by dividing Php10.00 by the then applicable conversion price.

In case the shares of Common Stock at anytime outstanding are subdivided into a greater or consolidated into a lesser number of shares, then the minimum conversion price per share of Common Stock will be proportionately decreased or increased, as the case may be, and in the case of a stock dividend, such price will be proportionately decreased, provided, however, that in every case the minimum conversion price shall not be less than the par value per share of Common Stock. In the event the relevant effective date for any such subdivision or consolidation of shares or stock dividend occurs during the period of 30 trading days preceding the presentation of any shares of 10% Cumulative Convertible Preferred Stock for conversion, a similar adjustment will be made in the sales prices applicable to the trading days prior to such effective date utilized in calculating the conversion price of the shares presented for conversion.

In case of any other reclassification or change of outstanding shares of Common Stock, or in case of any consolidation or merger of PLDT with or into another corporation, the Board of Directors shall make such provisions, if any, for adjustment of the minimum conversion price and the sales price utilized in calculating the conversion price as the Board of Directors, in its sole discretion, shall be deemed appropriate.

At PLDT's option, the Series A to EE 10% Cumulative Convertible Preferred Stocks are redeemable at par value plus accrued dividends five years after the year of issuance.

On January 30, 2007, the Board of Directors designated 150,000 shares of serial preferred stock as Series HH 10% Cumulative Preferred Stock for issuance from January 1, 2007 up to December 31, 2009.

The issuance of SIP Series FF, GG and HH is an exempt transaction under Section 10.2 of the Securities Regulation Code, as confirmed by the Philippine SEC on April 2, 2007.

On October 24, 2005, PLDT issued to JPMorgan, as depositary, and to the holders of the Series III Convertible Preferred Stock a notice of mandatory conversion of all of its outstanding 4,616,200 shares of Series III Convertible

Preferred Stock into shares of PLDT Common Stock. The conditions for mandatory conversion under the terms of the Series III Preferred Stock have been satisfied, including:

(i) that the average closing price of PLDT's ADSs for the 30-day period ending seven days prior to the date in which notice of the mandatory conversion was given was above US\$29.19 a share; (ii) that there were no dividends in arrears on any shares of the Series III Convertible Preferred Stock; and (iii) that PLDT had sufficient distributable reserves to pay the fixed preferential dividends on the shares of Series III Convertible Preferred Stock, calculated down to and including the mandatory conversion date.

In November 2005, PLDT issued 710,891 shares of common stock on account of the voluntary conversion of 415,023 shares of Series III Convertible Preferred Stock.

As at December 19, 2005, as a result of PLDT's issuance of a notice of mandatory conversion, all of the outstanding shares of Series III Convertible Preferred Stock were voluntarily and mandatorily converted into shares of PLDT Common Stock wherein each share of Series III Convertible Preferred Stock was converted into 1.7129 shares of Common Stock. A total of 7,907,032 shares of PLDT's Common Stock were issued as a result of the voluntary and mandatory conversions of all of the Series III Convertible Preferred Stock.

The Series IV Cumulative Non-Convertible Redeemable Preferred Stock earns cumulative dividends at an annual rate of 13.5% based on the paid-up subscription price. It is redeemable at the option of PLDT at any time one year after subscription and at the actual amount paid for such stock, plus accrued dividends. On February 26, 2002, the Board of Directors called for the payment of a portion of the balance of the subscription price of the Series IV Cumulative Non-Convertible Redeemable Preferred Stock amounting to Php72 million, which was paid on March 5, 2002. On March 22, 2002, PLDT redeemed 60 million shares out of the 360 million subscribed shares of its Series IV Cumulative Non-Convertible Preferred Stock and paid Php72 million, representing the redemption price plus unpaid dividends up to the date of redemption.

The provisions of certain subscription agreements involving preferred stock have an effect on the ability of PLDT to, without written consent, sell certain assets and pay cash dividends unless all dividends for all past quarterly dividend periods have been paid, and provision has been made for the currently payable dividends.

## **17. Interest-bearing Financial Liabilities**

This account consists of the following:

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
<b>Long-term portion of interest-bearing financial liabilities - net of current portion:</b>		
Long-term debt (Note 24)	57,273	63,769
Obligations under capital lease (Notes 8 and 24)	26	106
Preferred stock subject to mandatory redemption (Note 24)		1,369
	<b>57,299</b>	65,244
<b>Current portion of interest-bearing financial liabilities:</b>		
Notes payable	487	201
Long-term debt maturing within one year (Note 24)	6,965	16,184
Obligations under capital lease maturing within one year (Notes 8 and 24)	911	924
Preferred stock subject to mandatory redemption (Note 24)	1,114	
	<b>9,477</b>	17,309

Unamortized debt discount, representing debt issuance costs and any difference between the fair value of consideration given or received on initial recognition, included in the financial liabilities are as follows:

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Long-term debt	4,976	5,953
Obligations under capital lease (Notes 8 and 24)	504	540
Preferred stock subject to mandatory redemption	91	260
Total unamortized debt discount at end of period (Note 24)	<b>5,571</b>	6,753

The following table describes all changes to unamortized debt discount as at September 30, 2007 and December 31, 2006.

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Unamortized debt discount at beginning of period	6,753	13,347
Additions during the period	15	48
Settlements and conversions during the period	(42)	(2,733)
Revaluations during the period	(357)	(595)
Accretion during the period charged to interest expense (Notes 5 and 24)	(798)	(3,314)
Unamortized debt discount at end of period (Note 24)	<b>5,571</b>	6,753



**Long-term Debt**

Long-term debt consists of:

Description	Interest Rates	September 30, 2007		December 31, 2006	
		(Unaudited)		(Audited)	
(in millions)					
<i>U.S. Dollar Debt:</i>					
Export Credit Agencies-Supported Loans:					
Kreditanstalt für Wiederaufbau, or KfW	5.65% - 7.58% and US\$ LIBOR + 0.55% - 2.5% in 2007 and 2006	US\$153	Php6,896	US\$201	Php9,877
Finnvera, Plc, or Finnvera	US\$ LIBOR + 0.05% in 2007 and 7.53% - 7.75% and US\$ LIBOR + 0.05% in 2006	49	2,219	69	3,381
Nippon Export and Investment Insurance of Japan, or NEXI	US\$ LIBOR + 1% in 2007 and in 2006			25	1,215
Others	6.60% and US\$ LIBOR + 0.15% - 0.65% and GOVCO's cost + 0.20% in 2007 and 5.83% - 6.6% and US\$ LIBOR + 0.15% - 1.60% and GOVCO's Cost + 0.20% in 2006	5	206	10	508
Fixed Rate Notes	7.85% - 11.375% in 2007 and 2006	207	9,321	305	14,981
Term Loans:		676	30,410	835	40,971
Debt Exchange Facility	2.25% and US\$ LIBOR + 1% in 2007 and 2006	184	8,288	176	8,615
GSM Network Expansion Facilities	4.49% - 4.70% and US\$ LIBOR + 0.815% in 2007 and 4.49% - 4.70% and US\$ LIBOR + 0.815% - 3.25% in 2006	154	6,944	194	9,509
Others	US\$ LIBOR + 0.40% and 6% - 10% in 2007 and US\$ LIBOR + 0.40% - 3.625% and 1.75% - 10% in 2006	4	167	10	487
Satellite Acquisition Loans	5.66% and US\$ LIBOR + 1.75% - 2.75% in 2007 and 2006	30	1,342	42	2,083
		<b>US\$1,255</b>	<b>56,472</b>	<b>US\$1,562</b>	<b>76,646</b>
<i>Philippine Peso Debt:</i>					
Peso Fixed Rate Corporate Notes	5.625% - 15% in 2007 and 15% - 15.816% in 2006		4,988		808
Term Loans:					
Secured Term Loans	7.09%, MART1 + 5.70% and 90-day PHILBOR + 3% in 2007 and 7.09% 15% and 90-day		6		11

	PHILBOR + 3% in 2006		
Other Unsecured Term Loans	6.125% and MART1 + 0.75% in 2007 and MART1 + 0.75% in 2006	<b>2,772</b>	2,488
		<b>7,766</b>	3,307
		<b>64,238</b>	79,953
Less portion maturing within one year		<b>6,965</b>	16,184
Total long-term debt		<b>Php57,273</b>	Php63,769

*Note: Amounts presented are net of unamortized debt discount and debt issuance costs.*

The scheduled maturities of our outstanding consolidated long-term debt at nominal values as at September 30, 2007 are as follows:

Year	U.S. Dollar Loans		Php Loans		Total
	In U.S. Dollar	In Php	In Php	In Php	In Php
	(in millions)				
2007(1)	40	1,803	139	1,942	
2008	147	6,608	558	7,166	
2009	263	11,830	570	12,400	
2010	71	3,183	568	3,751	
2011	15	668	568	1,236	
2012 and onwards	830	37,335	5,384	42,719	
	1,366	61,427	7,787	69,214	

*(1) October 1, 2007 through December 31, 2007*

#### ***U.S. Dollar Debt:***

#### **Export Credit Agencies-Supported Loans**

In order to obtain imported components for our network infrastructure in connection with our expansion and service improvement programs, we obtained loans extended and/or guaranteed by various export credit agencies. These financings account for a significant portion of our indebtedness.

*Kreditanstalt für Wiederaufbau, or KfW*

KfW, a German state-owned development bank, is PLDT's largest single creditor. As at September 30, 2007, we owed US\$153 million, or Php6,896 million, aggregate principal amount of debt to KfW, as follows:

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- US\$113 million provided under various export credit agency-backed facilities, of which US\$18 million was in connection with our expansion and service improvement programs, and US\$95 million in connection with the US\$149 million refinancing facility discussed below; and
- US\$40 million provided for the 15% downpayment portion and credit facilities without guarantee/insurance cover from the export credit agencies, of which US\$26 million was in connection with the US\$149 million refinancing facility discussed in the following paragraphs.

On January 25, 2002, PLDT signed two loan agreements with KfW, which provided PLDT with a US\$149 million facility to refinance in part the repayment installments under its existing loans from KfW due from January 2002 to December 2004. The facility is composed of a nine-year loan, inclusive of a three-year disbursement period and a two-year grace period during which no principal is payable. It partly enjoys the guarantee of HERMES, the export credit agency of the Federal Republic of Germany. We have drawn US\$140 million, or Php6,295 million, under this facility as at September 30, 2007. PLDT waived further disbursements under this refinancing facility effective September 1, 2004. Thus, the undrawn portion of US\$9 million was cancelled.

Of the amounts outstanding under these KfW loans, US\$24 million will mature on various dates between October 1, 2007 and December 4, 2007, US\$55 million will mature in 2008, US\$43 million will mature in 2009 and US\$31 million will mature in 2010. Principal amortizations on these loans are generally payable in equal semi-annual installments.

*Finnvera, Plc, or Finnvera*

As at September 30, 2007, US\$50 million (US\$49 million, net of unamortized discount of US\$1 million), or Php2,249 million (Php2,219 million, net of unamortized discount of Php30 million), principal amount of Smart's debt was provided by various banks under an export credit agency-backed facility in connection with Smart's GSM expansion program. This facility is covered by a guaranty from Finnvera, the Finnish Export Credit Agency, for 100% of political and commercial risk for the refinancing facility of GSM Phases 5A and 5B. Other Finnvera-guaranteed GSM loan facilities were fully paid in the aggregate amount of US\$17 million for GSM Phases 3 and 4 loan facilities on April 28, 2006.

Of the amount outstanding under the remaining Finnvera guaranteed loan, US\$20 million will mature in 2008, US\$20 million will mature in 2009 and US\$10 million will mature in 2010. Principal amortization on this loan is payable in equal semi-annual installments.

*Nippon Export and Investment Insurance of Japan, or NEXI*

On November 28, 2002, Smart signed a US\$100 million term loan facility supported by NEXI, of which US\$60 million was drawn on November 28, 2003 and US\$40 million on April 5, 2004. This loan is payable semi-annually over four years in eight equal installments starting May 28, 2004 with final repayment due in November 2007. The outstanding balance was fully paid in the amount of US\$25 million on May 25, 2007.

*Other Export Credit Agency Supported Loans*

PLDT has also obtained loans extended and/or guaranteed by other export credit agencies, including the Export-Import Bank of the United States, and the respective export credit agencies of France and Italy, in the aggregate outstanding principal amount of US\$4 million, or Php173 million, as at September 30, 2007. Smart, likewise, obtained loans guaranteed by the export credit agencies of Norway and Italy with outstanding balance of US\$1 million, or Php33 million, as at September 30, 2007. Of the amounts outstanding under these loans, US\$4 million will mature on various dates between October 1, 2007 and December 15, 2007 and US\$1 million will mature in 2008.

Fixed Rate Notes

PLDT has the following non-amortizing fixed rate notes outstanding as at September 30, 2007 and December 31, 2006:

Principal Amount	Interest Rate	Maturity Date	September 30, 2007		December 31, 2006	
			(Unaudited)	(Unaudited)	(Audited)	(Audited)
		March 6, 2017	<b>US\$296</b>	<b>Php13,326</b>	US\$296	Php14,523
US\$300,000,000	8.350%					
US\$250,000,000	11.375%	2012	<b>245</b>	<b>10,998</b>	244	11,963
US\$135,886,000	10.500%		<b>135</b>	<b>6,086</b>	166	8,148

		April 15, 2009		
		May 15, 2007		
US\$ 19,310,000	10.625%	March 6, 2007	19	941
US\$110,068,000	7.850%	2007	110	5,396
			<b>US\$676</b>	<b>Php30,410</b>
			US\$835	Php40,971

***Consent Solicitation for the US\$250 Million 11.375% Notes due 2012, and Consent Solicitation for the US\$175 Million 10.5% Notes due 2009 and US\$300 Million 8.35% Notes due 2017***

On November 6, 2007, PLDT commenced a solicitation of consents from holders of its outstanding 11.375% Notes due 2012, or the 2012 Notes, to effect certain proposed amendments relating to the limitation on restricted payments and limitation on dividends and a solicitation of consents from holders of its outstanding 10.5% Notes due 2009, or the 2009 Notes, and 8.35% Notes due 2017, or the 2017 Notes, to effect certain proposed amendments relating to the limitation on dividends.

Specifically, the proposed amendments, once effective, would give PLDT greater flexibility to make certain restricted payments, amend limitations on PLDT paying dividends or distributions, and reduce PLDT's permitted leverage ratios pursuant to the terms of the notes.

PLDT's key financial indicators including revenues, profitability and operating cash flows have improved over time compared to when the notes were issued. PLDT is focused on maintaining its market leadership, investing in new growth areas to boost its core telecommunications business and diversifying its revenue sources. PLDT is also focused on pursuing an efficient capital structure by adjusting its dividend and distribution policy to maintain an optimal level of cash on its balance sheet. PLDT believes that the existing Limitation on Restricted Payments and the existing Limitation on Dividends, constrain its ability to pursue these objectives. To demonstrate its continued commitment to maintaining a prudent capital structure, PLDT will simultaneously tighten its debt capacity.

*Term Loans*

*US\$283 Million Term Loan Facility, or Debt Exchange Facility*

On July 2, 2004, Smart acquired from Piltel's creditors approximately US\$289 million, or 69.4%, in the aggregate of Piltel's outstanding restructured debt at that time, in exchange for Smart debt and a cash payment by Smart. In particular, Smart paid an amount in cash of US\$1.5 million, or Php84 million and issued new debt of US\$283.2 million, or Php15,854 million, at fair value of Php8,390 million, net of debt discount amounting to Php7,464 million.

The breakdown of the total amount of Smart debt issued to participating Piltel creditors is as follows:

- 2007 Facility in the amount of US\$0.2 million payable in full in December 2007;
- 2008 Facility in the amount of US\$2.9 million payable in full in December 2008; and
- 2014 Facility in the amount of US\$280.1 million payable in full in June 2014.

As at September 30, 2007, outstanding balance of these loans amounted to US\$283 million (US\$184 million, net of unamortized discount of US\$99 million), or Php12,739 million (Php8,288 million, net of unamortized discount of Php4,451 million).

Interest for the above facilities is payable every quarter at a floating rate of three months US\$ LIBOR plus 1.00% for the 2007 and 2008 facilities, and a fixed rate of 2.25% per annum for the 2014 facility. Furthermore, a portion of the 2014 facility amounting to US\$144 million has a variable yield option whereby the creditors have an option to elect for an early repayment at a discount either in December 2007 at 52.5% of the relevant debt amount or in December 2008 at 57.5% of the relevant debt amount.

#### *GSM Network Expansion Facilities*

On September 13, 2004, Smart signed a US\$104 million 5-year term loan facility to finance the related Phase 7 GSM Equipment and services. The facility was awarded to ABN AMRO Bank, Banque National de Paribas, Calyon, DBS Bank and Sumitomo Mitsui Banking Corporation as the Lead Arrangers with Finnish Export Credit, Plc as the Lender. The full amount of the facility was drawn on November 22, 2004, of which US\$52 million remained outstanding as at September 30, 2007. The loan is payable over five years in ten equal semi-annual payments starting May 2005 with final repayment in November 2009.

On August 8, 2005, Smart signed a US\$30 million commercial facility with NIB to partly finance the related Phase 8 GSM equipment and services contracts. The facility is a 5-year term loan payable semi-annually in ten equal installments commencing six months from the first drawdown date at a floating rate of US\$ LIBOR plus 0.815% margin per annum. The facility was drawn on July 11, 2006 for the full amount of US\$30 million at a floating interest of 6.445% (5.63% US\$ LIBOR plus 0.815% per annum margin). The first installment payment commenced on

January 11, 2007. US\$24 million amount remained outstanding as at September 30, 2007.

On August 10, 2005, Smart signed a loan facility for its GSM Phase 8 financing in the amount of US\$70 million. The facility was awarded to the Bank of Tokyo Mitsubishi Ltd., Mizuho Corporate Bank Ltd., Standard Chartered Bank and Sumitomo Mitsui Banking Corporation as the Lead Arrangers, with FEC as the Lender. Smart opted to utilize only a total of US\$67 million which was drawn on February 15, 2006 and March 13, 2006 for US\$10 million and US\$57 million, respectively. The undrawn balance of US\$3 million was cancelled. The facility is a 5-year term loan payable in 10 equal semi-annual installments with final repayment on September 1, 2010. Interest is payable semi-annually at a fixed rate of 4.515% per annum. As at September 30, 2007, US\$44 million remained outstanding.

On July 31, 2006, Smart signed a U.S. Dollar Term Loan Facility for US\$44.2 million to partly finance the related Phase 9 GSM equipment and services contracts. The Lender is FEC with ABN AMRO Bank N.V., Standard Chartered Bank and Sumitomo Mitsui Banking Corporation and Mizuho Corporate Bank Ltd. as the Lead Arrangers. The facility is a 5-year term loan payable in 10 equal semi-annual installments commencing six months from the drawdown date at a CIRR Fixed rate of 4.05% per annum. The facility was drawn on November 10, 2006 for the full amount of US\$44.2 million. The first installment commences on January 16, 2007 with final repayment on July 15, 2011. As at September 30, 2007, the US\$35 million loan remains outstanding.

As at September 30, 2007, the aggregate outstanding balance of these loans amounted to US\$155 million (US\$154 million, net of unamortized discount of US\$1 million), or Php6,981 million (Php6,944 million, net of unamortized discount of Php37 million).

#### *Other Term Loan*

On July 1, 2004, CyMed availed of a 5-year non-interest-bearing advance from certain of its officers to fund its operating expenses, including salaries and other incidental expenses. The outstanding balance of this loan as at September 30, 2007 amounted to US\$1 million, or Php30 million, which is payable quarterly until July 31, 2009.

#### *Undrawn Facility*

On October 16, 2006, Smart signed a U.S. Dollar Term Loan Facility with Metropolitan Bank and Trust Company to finance the related Phase 9 GSM Facility for an amount of US\$50 million. The facility is a five-year loan payable in 18 equal and consecutive quarterly installments commencing on the third quarter from the date of the first drawdown. Interest rate is floating at three-month US\$ LIBOR plus 0.75% per annum margin. The loan facility was fully drawn on October 10, 2007.

Restructured Loans

On June 5, 2006, Piltel made a partial voluntary prepayment of principal under its Peso bank facility, US Dollar bank facility, various Trade Creditor facilities and Notes Indenture. The voluntary prepayment was made in lieu of depositing excess cash flow from the operations of Piltel's business into a Sinking Fund Account. The aggregate voluntary prepayment amount was Php9,325 million (Php6,393 million to Smart and Php2,932 million to third party creditors), or US\$176 million (US\$121 million to Smart and US\$55 million to third party creditors), which was applied proportionally to the various debt facilities as set out in the Intercreditor Agreement dated June 4, 2001 (the Intercreditor Agreement).

On December 4, 2006, Piltel prepaid the outstanding balance of its principal debt under its Peso bank facility, US Dollar bank facility, Peso Term Note facility, various Trade Creditor facilities and Notes Indenture in the aggregate amount of Php11,631 million (Php8,061 million to Smart and Php3,570 million to third party creditors), or US\$233 million (US\$161 million to Smart and US\$72 million to third party creditors). Piltel obtained approval from the Bangko Sentral ng Pilipinas to source dollar payment from authorized agent banks.

On March 30, 2007, Piltel paid the remaining convertible bonds with principal amount of US\$0.7 million.

*Satellite Acquisition Loans*

Mabuhay Satellite has an existing Credit Agreement with the Export-Import Bank of the United States, or Ex-Im Bank, to finance a portion of the cost of purchasing the Agila II Satellite. In 2004, Ex-Im Bank approved, in principle, the re-profiling of Mabuhay Satellite's US\$42 million debt with them by extending the maturity of the loan by 1½ years to July 15, 2007 and reducing the interest rate by 1% to 5.6%. The revised repayment terms have been approved by the majority of the local creditor banks. On July 16, 2007, the outstanding balance was fully paid in the amount of US\$5 million (Php236 million).

Mabuhay Satellite also has an existing Omnibus Agreement with a syndicate of local banks, or the Banks, which includes issuance of irrevocable standby Letters of Credit in favor of Ex-Im Bank, as security under the Credit Agreement and a term loan to Mabuhay Satellite in the aggregate amount of US\$30 million (Php1,342 million), which will mature on various dates from 2006 to 2009. The Omnibus Agreement was cancelled on July 16, 2007.

Mabuhay Satellite has constituted in favor of the Banks: (a) a first mortgage on its leasehold rights under a lease agreement entered into with the Subic Bay Metropolitan Authority and the components of the satellite system; (b) an assignment of its rights under its purchase contract for the satellite system; (c) an assignment of its rights under the transponder lease contracts to be entered into with its shareholders and other parties and the revenues therefrom; and (d) an assignment of the applicable proceeds of insurance to be taken on the satellite system.



In 2006, the Banks have approved Mabuhay's request to extend the maturity of the loan under the Omnibus Agreement by two years to October 20, 2009, with a 1% increase in the margin on the deferred amount.

***Philippine Peso Debt:***

*Php2,770 Million Peso Fixed Rate Corporate Notes*

In connection with PLDT's service improvement and expansion programs, PLDT has entered into two loan agreements, pursuant to each of which PLDT issued fixed rate corporate notes in three tranches.

Under the first loan agreement, PLDT borrowed an aggregate amount of Php1,500 million, of which Php230 million was repaid on November 11, 2002, Php500 million was repaid on November 9, 2004 and Php770 million was repaid on November 9, 2006.

Under the second loan agreement, PLDT borrowed an aggregate amount of Php1,270 million, of which Php360 million was repaid on June 9, 2003, Php100 million was repaid on June 9, 2005 and Php810 million was repaid on June 12, 2007.

*Php5 Billion Peso Fixed Rate Corporate Notes*

On February 15, 2007, Smart issued Php5 billion unsecured fixed rate corporate notes, made up of Series A notes amounting to Php3.8 billion and Series B notes amounting to Php1.2 billion with five and ten year terms, respectively. Series A notes were priced at 5.625%, while Series B notes were priced at 6.500%. Funds raised from the issuance of these notes will be used primarily for Smart's capital expenditures for network improvement and expansion.

*Term Loans*

*Secured Term Loans*

*Php100 Million Term Loan Facility*

On March 15, 2004, ePLDT entered into a three-year term loan facility with Asia United Bank amounting to Php100 million for the payment of its outstanding short-term bank loan facility and for other working capital requirements. The loan facility was fully drawn as at December 31, 2004. The loan is to be repaid in nine equal quarterly installments starting March 2005 with final repayment in March 2007. Interest on the loan is equivalent to 90-day PHIBOR plus 3% per annum payable quarterly in arrears. The loan is secured by a Mortgage Trust Indenture Agreement, or MTIA, dated March 15, 2004, with Asia United Bank Trust and Investments Group, on a parcel of land with a carrying value of Php279 million as at December 31, 2004. This loan was fully paid as at March 31, 2007.

*Php149 Million Term Loan Facility*

In January 2006, Vocativ, a wholly-owned call center subsidiary of ePLDT, partially prepaid Php89 million out of its outstanding five-year term loan facility of Php109 million with Asia United Bank for the payment of its additional capital expenditures and working capital requirements. Under the terms of the loan, principal payment is to be paid in 14 equal quarterly installments starting April 2006 with final repayment in July 2009. Interest on the loan is equivalent to 90-day PHIBOR plus 3% per annum payable quarterly in arrears. The loan is secured by a Mortgage Participation Certificate against the MTIA between ePLDT and Asia United Bank Corporation Trust and Investments Group dated March 15, 2004 on a parcel of land, which excludes the buildings and improvements. The remaining balance of Php20 million was pre-terminated in April 2006.

*Unsecured Term Loans*

*Php2,500 Million Term Loan Facility*

On August 14, 2006, Smart signed a Peso Term Loan Facility with Metropolitan Bank and Trust Company to finance the related Phase 9 GSM facility for an amount of Php2,500 million. The facility is a five-year loan payable in 18 equal consecutive quarterly installments commencing on the third quarter from the date of the first drawdown. Interest rate is floating at three-month MART plus 0.75% per annum margin. The facility was drawn on December 11, 2006 for the full amount of Php2,500 million at a floating interest of 6.0232% (5.2732% three-month MART1 plus 0.75% per annum margin). The first installment will commence on September 11, 2007 with final repayment on December 9, 2011. The outstanding balance of this loan as at September 30, 2007 amounted to Php2,361 million (Php2,352 million, net of unamortized discount of Php9 million).

*Php400 Million and Php20 Million Refinancing Loans*

On May 22, 2007, PLDT signed loan agreements with The Philippine American Life and General Insurance Company for Php400 million and The Philam Bond Fund, Inc. for Php20 million to refinance their respective participations in the Ten-Year Note under the Php1,270 million Peso Fixed Rate Corporate Notes which were repaid on June 12, 2007. Interest is payable quarterly. Both loans will mature on June 12, 2014.

### *Debt Covenants*

Our debt instruments contain restrictive covenants, including covenants that could prohibit us from paying dividends on common stock under certain circumstances, and require us to comply with specified financial ratios and other financial tests, calculated in conformity with PFRS, at relevant measurement dates, principally at the end of each quarterly period. We have complied with all of our maintenance financial ratios as required under our loan covenants and other debt instruments.

The principal factors that can negatively affect our ability to comply with these financial ratios and other financial tests are depreciation of the Philippine peso relative to the U.S. dollar, poor operating performance of PLDT and its consolidated subsidiaries, impairment or similar charges in respect of investments or other long-lived assets that may be recognized by PLDT and its consolidated subsidiaries and increases in our interest expenses. Interest expense may increase as a result of various factors including issuance of new debt, the refinancing of lower cost indebtedness by higher cost indebtedness, depreciation of the Philippine peso, the lowering of PLDT's credit ratings or the credit ratings of the Philippines, increase in reference interest rates, and general market conditions. Since approximately 89% of PLDT's total consolidated debts are denominated in foreign currencies, principally in U.S. dollars, many of these financial ratios and other tests are negatively affected by any weakening of the peso.

PLDT's debt instruments contain a number of other negative covenants that, subject to certain exceptions and qualifications, restrict PLDT's ability to take certain actions without lenders' approval, including: (a) incurring additional indebtedness; (b) prepaying other debt; (c) making investments; (d) extending loans; (e) extending guarantees or assuming the obligations of other persons; (f) paying dividends or other distributions or redeeming, repurchasing or otherwise acquiring shares of PLDT's capital stock; (g) disposing of all or substantially all of its assets or of assets in excess of specified thresholds of its tangible net worth; (h) creating any lien or security interest; (i) permitting set-off against amounts owed to PLDT; (j) merging or consolidating with any other company; (k) entering into transactions with stockholders and affiliates; and (l) entering into sale and leaseback transactions.

Further, certain of PLDT's debt instruments contain provisions wherein PLDT may be required to repurchase or prepay certain indebtedness in case of change in control of PLDT.

PLDT's debt instruments also contain customary and other default provisions that permit the lender to accelerate amounts due or terminate their commitments to extend additional funds under the debt instruments. These default provisions include: (a) cross-defaults and cross-accelerations that permit a lender to declare a default if PLDT is in

default under another debt instrument; in some cases, the cross-default provision is triggered upon a payment or other default permitting the acceleration of PLDT's debt, whether or not the defaulted debt is accelerated. In other cases, the cross-default provision requires the defaulted loan to be accelerated. In some debt instruments, the cross-default provision will be triggered only if the principal amount of the defaulted indebtedness exceeds a threshold amount specified in these debt instruments; (b) failure by PLDT to meet certain financial ratio covenants referred to above; (c) the occurrence of any material adverse change in circumstances that a lender reasonably believes materially impairs PLDT's ability to perform its obligations under its debt instrument with the lender; (d) the revocation, termination or amendment of any of the permits or franchises of PLDT in any manner unacceptable to the lender; (e) the abandonment, termination or amendment of the project financed by a loan in a manner unacceptable to the lender; (f) the nationalization or sustained discontinuance of all or a substantial portion of PLDT's business; and (g) other typical events of default, including the commencement of bankruptcy, insolvency, liquidation or winding up proceedings by PLDT.

Smart's debt instruments contain certain restrictive covenants, including covenants that prohibit Smart from paying dividends, redeeming preferred shares, making contributions to PLDT or otherwise providing funds that require Smart to comply with specified financial ratios and other financial tests at semi-annual measurement dates. The loan facilities that contain restrictions in dividend payments and redemption of preferred stocks have been paid in April 2006. The financial tests under Smart's loan agreements include compliance with a debt to equity ratio of not more than 1.5:1.0, a debt to EBITDA ratio of not more than 3:1 and a debt service coverage ratio of not less than 1.5:1.0. As at September 30, 2007, Smart has maintained compliance with all of its financial covenants. The agreements also contain customary and other default provisions that permit the lender to accelerate amounts due under the loans or terminate their commitments to extend additional funds under the loans. These default provisions include: (a) cross-defaults and cross-accelerations that permit a lender to declare a default if Smart is in default under another loan agreement. These cross-default provisions are triggered upon a payment or other default permitting the acceleration of Smart debt, whether or not the defaulted debt is accelerated; (b) failure by Smart to comply with certain financial ratio covenants; (c) any reduction in PLDT's ownership of Smart's capital stock below 51% of the total of each class of issued shares; (d) any reduction in First Pacific's and Metro Pacific Corporation's collective direct and/or indirect ownership of PLDT's common stock below 17.5% of the total common stock outstanding or 17.5% of the voting power of PLDT's total common stock outstanding; and (e) the occurrence of any material adverse change in circumstances that the lender reasonably believes materially impairs Smart's ability to perform its obligations or impair guarantors' ability to perform their obligations under its loan agreements.

The Credit and Omnibus Agreements of Mabuhay Satellite impose several negative covenants which, among other things, restrict material changes in Mabuhay Satellite's nature of business and ownership structure, any lien upon or with respect to any of its assets or to any right to receive income, acquisition of capital stock, declaration and payment of dividends, merger, consolidation and sale with another entity and incurring or guaranteeing additional long-term debt beyond prescribed amounts.

ePLDT's loan agreement imposes negative covenants which, among other things, restrict ePLDT in regard to payment of cash dividends or any other income or any capital distribution to PLDT, voluntary suspension of its entire business operations for a period of 60 consecutive days, dissolution of its legal existence, and creation of any encumbrances on the shares pledged. One of ePLDT's loan agreements also requires ePLDT to comply with specified financial ratios and other financial tests at quarterly measurement dates. The agreement also contains customary and other default provisions that permit the lender to accelerate amounts due under the loan or terminate their commitments to extend additional funds under the loan. As at December 31, 2006, ePLDT was in compliance with all of its financial

covenants.

### Obligations Under Capital Lease

The future minimum payments for capitalized leases as at September 30, 2007 are as follows:

<b>Year</b>	(in million pesos)
2007	1,378
2008	50
2009	12
2010	1
Total minimum lease payments (Note 22)	1,441
Less amount representing interest	504
Present value of net minimum lease payments	937
Less obligations under capital lease maturing within one year (Notes 8 and 24)	911
Long-term portion of obligations under capital lease (Notes 8 and 24)	26

### *Municipal Telephone Projects*

In 1993, PLDT entered into two lease agreements with the Philippine Department of Transportation and Communications, or DOTC, covering telecommunications facilities in the province of Bohol and Batangas established under the Municipal Telephone Act. Under these agreements, PLDT was granted the exclusive right to provide telecommunications management services, to expand services, and to promote the use of the DOTC-contracted facilities in certain covered areas for a period of 15 years. Title to the properties shall be transferred to PLDT upon expiration of the lease term. As at September 30, 2007, PLDT's aggregate remaining obligation under this agreement was approximately Php858 million. In case of cancellation, PLDT is liable to pay Php100 million under each of the two contracts as liquidated damages.

On June 1, 2004, PLDT served the DOTC a notice of termination of the lease agreement in respect of the telecommunications system in Bohol which state of deterioration, obsolescence and disrepair has made it impossible for PLDT to continue managing, operating, and maintaining the system. Since 2002, PLDT has been advising the DOTC of the need to review the viability of the system as PLDT has infused more than Php200 million for upgrades and maintenance to keep the system operable. Further, the enactment of Public Telecommunications Policy Act, or R.A. No. 7925, which negated the DOTC's warranty to grant PLDT the exclusive right to provide telecommunication services in the areas stipulated, prevented PLDT from achieving the originally projected profitability, thereby rendering it impossible for PLDT to continue fulfilling its obligation under the lease agreement. Although several discussions have been held since then, no mutually acceptable agreement has been reached. On June 30, 2004, the DOTC advised PLDT that the request for termination of the lease agreement in Bohol has been referred to the Department of Justice, or DOJ, as government agencies are required to refer all interpretation of contracts and

agreements to the DOJ secretary as attorney-general of the national government. On May 5, 2005, PLDT received a letter from the DOTC stating that PLDT is in default for failure to remit to the DOTC the quarterly installments under the lease agreement. Due to the failure of the parties to amicably settle their dispute, on September 28, 2005, PLDT demanded that the dispute be referred to arbitration and that the parties agree on the composition of the arbitration committee. In response, the DOTC, in a letter dated October 17, 2005, informed PLDT that pursuant to Executive Order No. 269, Series of 2004, dated January 12, 2004, the existing communications programs and projects implemented by DOTC were transferred to the Commission on Information and Communications Technology, or CICT, and that the DOTC had forwarded to CICT PLDT's letter dated September 28, 2005. In a letter dated March 24, 2006, the CICT informed PLDT that the CICT poses no objection on PLDT's stated intentions and preference to refer the unresolved and outstanding issues to the Philippine Dispute Resolution Center, Inc., or PDRCI, per the arbitration clause of the lease agreement. On June 27, 2006, a Request for Arbitration dated June 1, 2006 was filed by PLDT with the PDRCI. On November 15, 2006, DOTC has filed its Answer to the said Request for Arbitration. After PDRCI took cognizance of the case, PLDT and DOTC filed their amended pleadings. DOTC filed a Supplemental Answer with Prayer for Interim Relief, which prayed for, among others, the remittance to DOTC of the amount PLDT allegedly deposited in a separate account for the benefit of the former.

On June 1, 2007, the PDRCI issued a Final Partial Award (On the Request for Interim Relief), granting DOTC's prayer. PLDT was ordered to release to DOTC the amount of Php149 million subject to the posting by DOTC of a surety bond. PLDT has taken issue with the Final Partial Award, or Award, and filed before the Court of Appeals a Petition for Review under Rule 43 of the Rules of Court to review the Award.

In the meantime, DOTC filed an Application/Motion for Confirmation of Final Partial Award before the Regional Trial Court of Mandaluyong, which is currently pending.

The Arbitration proceedings between DOTC and PLDT pertaining to lease agreement of the Bohol Telecommunications System continue to this day. As at September 30, 2007, the net book value of the telecommunications system in Bohol, including PLDT's additional capital expenditure relating to the telecommunications system, and corresponding capital lease obligation amounted to Php3 million and Php735 million, respectively.

Piltel also entered into an agreement for the financial lease of the Palawan Telecommunications System of the Municipal Telephone Public Office with the DOTC on September 3, 1994. The Municipal Telephone Public Office Contract is a 30-year contract for Piltel to lease facilities for public call office stations in the Palawan area, with revenues going to Piltel. In consideration, Piltel pays the DOTC an escalating annual lease fee. The total lease payment for thirty years is Php483 million. As at September 30, 2007, Piltel's aggregate remaining obligation under this agreement was approximately Php43 million.

#### *Other Long-term Capital Lease Obligations*

The PLDT Group has various long-term lease contracts for a period of three years covering various office equipment. In particular, PLDT, Smart and ePLDT have capital lease obligations in the aggregate amount of Php540 million as at September 30, 2007 in respect of office equipment.

Under the terms of certain loan agreements and other debt instruments, PLDT may not create, incur, assume or permit or suffer to exist any mortgage, pledge, lien or other encumbrance or security interest over the whole or any part of its assets or revenues or suffer to exist any obligation as lessee for the rental or hire of real or personal property in connection with any sale and leaseback transaction.

### Preferred Stock Subject to Mandatory Redemption

The movements of PLDT's preferred stock subject to mandatory redemption as at September 30, 2007 and December 31, 2006 are as follows:

	September 30, 2007 (Unaudited)			December 31, 2006 (Audited)			
	Series V	Series VI	Total	Series V	Series VI	Series VII	Total
	(in million pesos)						
Balance at beginning of period	61	1,308	1,369	272	6,321	5,381	11,974
Accretion	8	106	114	13	481	282	776
Revaluation		(98)	(98)		(241)	(120)	(361)
Conversion	(17)	(254)	(271)	(224)	(5,253)	(5,543)	(11,020)
Balance at end of period	52	1,062	1,114	61	1,308		1,369

As at September 30, 2007, PLDT had issued 3 million shares of Series V Convertible Preferred Stock, 5 million shares of Series VI Convertible Preferred Stock and 4 million shares of Series VII Convertible Preferred Stock in exchange for a total of 58 million shares of Series K Class I Convertible Preferred Stock of Piltel, pursuant to the debt restructuring plan of Piltel adopted in June 2001. As discussed below, as at December 31, 2006, all Series VII Convertible Preferred Stock had been converted. Shares of Series V and VI Convertible Preferred Stock are entitled to receive annual dividends of Php18.70 per share and US\$0.397 per share, respectively. Each share of Series V and VI Convertible Preferred Stock is convertible at any time at the option of the holder into one PLDT common share. On the date immediately following the seventh anniversary of the issue date of the Series V and Series VI Convertible Preferred Stock, the remaining outstanding shares under these series will be mandatorily converted into PLDT common shares. Under a put option exercisable for 30 days, holders of common shares received, on mandatory conversion of the Series V and VI Convertible Preferred Stock, will be able to require PLDT to purchase such PLDT common shares for Php1,700 per share and US\$36.132 per share, respectively.

The Series V Convertible Preferred Stock was designated as a compound instrument consisting of liability and equity components. The fair value of the Convertible Preferred Stock was determined on the issue date, of which the fair

value of the liability component as at date of issuance is recorded as Preferred Stock Subject to Mandatory Redemption and is included under the Interest-bearing Financial Liabilities account in the consolidated balance sheets. The residual amount was assigned as the equity component.

The cost of each foreign currency component of the Convertible Preferred Stock Series VI and VII, was designated as a debt instrument with embedded call options. The fair value of the Convertible Preferred Stock was determined on the issue date, of which the fair value of embedded call options was bifurcated and accounted for separately, see *Note 2 Summary of Significant Accounting Policies and Practices* and *Note 24 Financial Assets and Liabilities*. The residual amount was assigned as liability components and recorded as Preferred Stock Subject to Mandatory Redemption and is included under the Interest-bearing Financial Liabilities account in the unaudited consolidated balance sheets.

The difference between the amount designated as liability components of the Series V, VI and VII Convertible Preferred Stock at issue date and the aggregate redemption value is accreted over the period up to the put option date using the effective interest rate method. Accretions added to Preferred Stock Subject to Mandatory Redemption and charged to interest for the nine months ended September 30, 2007 and 2006 amounted to Php114 million and Php739 million, respectively.

Preferred Stock Subject to Mandatory Redemption amounted to Php1,114 million and Php1,369 million as at September 30, 2007 and December 31, 2006, respectively, after revaluation of Series VI and VII Convertible Preferred Stock to the exchange rates at balance sheet dates and after giving effect to the above accretions, conversions and additional issuances. As at September 30, 2007 and December 31, 2006, 11,118,350 shares and 10,937,309 shares, respectively, of the Convertible Preferred Stock have been voluntarily converted into PLDT common shares. On August 18, 2006, all 3,842,000 shares of Series VII Convertible Preferred Stock have been voluntarily converted into PLDT common shares. The outstanding shares of Series V and VI Convertible Preferred Stock as at September 30, 2007 were 33,950 shares and 706,244 shares, respectively. The aggregate redemption value of the outstanding Series V and VI Convertible Preferred Stock amounted to Php1,205 million and Php1,629 million as at September 30, 2007 and December 31, 2006, respectively.

The corresponding dividends on these shares charged as interest expense amounted to Php14 million and Php113 million for the nine months ended September 30, 2007 and 2006, respectively.

## Notes Payable

In 2006, SPi obtained unsecured dollar-denominated short-term notes payable from various local commercial banks amounting to US\$4.09 million. In 2007, additional short-term unsecured dollar-denominated notes payable were obtained from various banks totaling US\$4.8 million. Interest on the notes range from 6.9% to 7.5% of the outstanding balance per annum and the notes are payable within 90 to 360 days from the availment date. The outstanding balance of US\$8.9 million, or Php400 million, as at September 30, 2007 will mature in various dates from



October 17, 2007 to August 8, 2008.

In 2006, Cymed obtained two-year interest bearing notes payable amounting to US\$3.4 million from its previous shareholders. Interest on the notes payable is 6.2% per annum. The outstanding balance of US\$1.6 million, or Php70 million, as at September 30, 2007 will mature in August 2008.

On June 1, 2007, SPi America LLC obtained short-term interest-bearing notes payable amounting to US\$0.5 million, or Php22 million in payment for software license. The loan is payable within one year in four equal quarterly payments of principal and interest commencing on September 1, 2007. Interest on the loan is 5% per annum. The outstanding balance of US\$0.4 million, or Php17 million, as at September 30, 2007 will mature in various dates from December 1, 2007 to June 1, 2008.

## 18. Other Noncurrent Liabilities

This account consists of:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
	(in million pesos)	
Accrual of capital expenditures under long-term financing	<b>6,135</b>	5,646
Future earn-out payments (Note 2)	<b>999</b>	
Asset retirement obligations (Notes 3 and 8)	<b>909</b>	831
Unearned revenues	<b>5</b>	63
Prepayments received under receivable purchase facility (Note 14)		205
Others	<b>837</b>	836
	<b>8,885</b>	7,581

## 19. Accrued Expenses and Other Current Liabilities

This account consists of:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
	(in million pesos)	
Accrued utilities and related expenses (Note 20)	<b>8,615</b>	8,078
Accrued employee benefits (Note 21)	<b>3,781</b>	7,474
Accrued interest and other related costs (Notes 17 and 20)	<b>1,609</b>	1,768
Accrued taxes and related expenses (Notes 22 and 23)	<b>856</b>	756
Payable in installment purchase of equity investment (Note 11)	<b>123</b>	
Others	<b>949</b>	1,026
	<b>15,933</b>	19,102

## 20. Related Party Transactions

### *a. Air Time Purchase Agreement between PLDT and AIL and Related Agreements*

PLDT is a party to a Founder NSP Air Time Purchase Agreement, or ATPA, entered into with AIL in March 1997, which was amended in December 1998 (as amended, the Original ATPA), under which PLDT was granted the exclusive right to sell AIL services as national service provider, or NSP, in the Philippines. In exchange, the Original ATPA required PLDT to purchase from AIL a minimum of US\$5 million worth of air time (the Minimum Air Time Purchase Obligation) annually over ten years commencing on January 1, 2002 (the Minimum Purchase Period), the purported date of commercial operations of the Garuda I Satellite. In the event that AIL's aggregate billed revenue was less than US\$45 million in any given year, the Original ATPA also required PLDT to make supplemental air time purchase payments not to exceed US\$15 million per year during the Minimum Purchase Period (the Supplemental Air Time Purchase Obligation).

Under the Original ATPA, the Minimum Air Time Purchase Obligation and the Supplemental Air Time Purchase Obligation terminated upon the earlier of (i) the expiration of the Minimum Purchase Period and (ii) the date on which all indebtedness incurred by AIL to finance the AIL System has been repaid. AIL indebtedness consists of: (1) loans with several financial institutions (the Banks) under the Credit Agreement dated March 12, 1997, as amended from time to time, including the amendment through the rescheduling agreement, dated September 30, 2002, which extended the principal repayment dates to agreed periods with the final maturity date on January 31, 2012 (collectively, the Amended Credit Agreement); and (2) amounts owing to MMOC under the Spacecraft Contract dated August 28, 1995, as amended on December 30, 1998.

AIL has incurred recurring significant operating losses, negative operating cash flows, and significant levels of debt. The financial condition of AIL was partly due to the NSPs inability to generate the amount of revenues originally expected as the growth in subscriber numbers has been significantly lower than budgeted.

On September 1, 2006, AIL, PT Asia Cellular Satellite, a 95% owned subsidiary of AIL, and Inmarsat Global Limited, or Inmarsat, reached an agreement to pool their resources to develop powerful and novel product and service offerings in the Asian region, founded on their respective mobile satellite communications networks, with (a) Inmarsat performing the role of satellite and network operator and wholesale product and services developer and (b) AIL performing the role of wholesale and retail distributor of products and services.

Inmarsat operates a constellation of geostationary satellites that extend mobile phone, fax and data communications to nearly every part of the world through the services it offers to end users through its established chain of distribution partners and satellite communications service providers.

On September 1, 2006, PLDT entered into a gateway services agreement with Inmarsat, under which PLDT committed to provide gateway infrastructure in Subic Bay up to a maximum amount of US\$5 million. In exchange, PLDT will earn US\$0.015 per minute for interconnection services to be provided to Inmarsat distribution partners for traffic going through the gateway facility in Subic Bay.

On September 1, 2006, AIL and PT Asia Cellular Satellite entered into a term sheet, as amended on October 20, 2006 and further amended on November 20, 2006 (the Bank Term Sheet), with a majority of the banks used as the basis for negotiations between the parties thereto with a view to enter into an agreement to further amend the Amended Credit Agreement with AIL's bank creditors. Under the Banks Term Sheet, a majority of the banks agreed, subject to satisfaction of certain conditions, among other things, to amend the Original ATPA as set forth in an attachment to the Banks Terms Sheet and to restructure AIL's indebtedness. Pursuant to the business collaboration arrangements between AIL and Inmarsat, on September 1, 2006, Inmarsat made the first payment of US\$4 million to AIL which was used to pay principal and interest payable to the banks in accordance with the Banks Term Sheet.

On February 1, 2007, the parties to the Original ATPA entered into an amendment to the Original ATPA on substantially the terms attached to the Bank Terms Sheet (the Amended ATPA). Under the Amended ATPA, the Minimum Air Time Purchase Obligation was amended and replaced in its entirety with an obligation of PLDT (the Amended Minimum Air Time Purchase Obligation) to purchase from AIL a minimum of US\$500,000 worth of air time annually over a period ending upon the earlier of (i) the expiration of the Minimum Purchase Period and (ii) the date on which all indebtedness incurred by AIL to finance the AIL System is repaid. Furthermore, the Amended ATPA unconditionally released PLDT from any obligations arising out of or in connection with the Original ATPA prior to the date of the Amended ATPA, except for obligations to pay for billable units used prior to such date. Moreover, pursuant to a letter of confirmation, dated February 1, 2007, the banks released and discharged PLDT and ACeS Philippines and their respective subsidiaries from any and all obligations and liabilities under the Original ATPA and related agreements.

Moreover, in accordance with the above contractual arrangements, ACeS Philippines acquired (i) from LMGT Holdings (ACeS), Inc., or LMGT, 50% of its equity interest in AIL for a consideration of US\$0.75 million pursuant to a sale and purchase agreement entered into on February 1, 2007 and (ii) from Tera Global Investment Ltd., or TGIL, for a nominal consideration 50% of TGIL's interest in a promissory note issued by AIL, which 50% interest represents an aggregate amount of US\$44 million, or the Transferred AIL Note, together with related security interests pursuant to sale agreement entered into on February 1, 2007. Immediately thereafter, a portion of the Transferred AIL Note was converted into shares of AIL and the balance was converted into non-interest bearing convertible bonds of AIL. As a result of these transactions, ACeS Philippines owned 36.99% of AIL as at the date of this report.

*b. Transactions with Major Stockholders, Directors and Officers*

Transactions to which PLDT or any of its subsidiaries is a party, in which a director, key officer or owner of more than 10% of the outstanding common stock of PLDT, or any member of the immediate family of a director, key officer or owner of more than 10% of the outstanding common stock of PLDT had a direct or indirect material interest, as at September 30, 2007 (unaudited) and December 31, 2006 (audited) and for the nine months ended September 30, 2007 and 2006 (unaudited) are as follows:

*1. Cooperation Agreement with First Pacific and certain affiliates, or the FP Parties, NTT Communications and DoCoMo*

In connection with the transfer by NTT Communications of approximately 12.6 million shares of PLDT's common stock to DoCoMo pursuant to a Stock Sale and Purchase Agreement dated January 31, 2006 between NTT Communications and DoCoMo, the FP Parties, NTT Communications and DoCoMo entered into a Cooperation Agreement, dated January 31, 2006. Under the Cooperation Agreement, the relevant parties extended certain rights of NTT Communications under the Stock Purchase and Strategic Investment Agreement dated September 28, 1999, as amended, and the Shareholders Agreement dated March 24, 2000, to DoCoMo, including:

- certain contractual veto rights over a number of major decisions or transactions; and
- rights relating to the representation on the board of directors of PLDT and Smart, respectively, and any committees thereof.

Moreover, key provisions of the Cooperation Agreement pertain to, among other things:

- *Restriction on Ownership of Shares of PLDT by NTT Communications and DoCoMo.* Each of NTT Communications and DoCoMo has agreed not to beneficially own, directly or indirectly, in the aggregate with their respective subsidiaries and affiliates, more than 21% of then issued and outstanding shares of PLDT's common stock. If such event does occur, the FP Parties, as long as they own in the aggregate not less than 21% of then issued and outstanding shares of PLDT's common stock, have the right to terminate their respective rights and obligations under the Cooperation Agreement, the Shareholders Agreement and the Stock Purchase and Strategic Investment Agreement.
- *Limitation on Competition.* NTT Communications, DoCoMo and their respective subsidiaries are prohibited from investing in excess of certain thresholds in businesses competing with PLDT in respect of customers principally located in the Philippines and from using their assets in the Philippines in such businesses. Moreover, if PLDT, Smart or any of Smart's subsidiaries intends to enter into any contractual arrangement relating to certain competing businesses, PLDT is required to provide, or to use reasonable efforts to procure that Smart or any of Smart's subsidiaries provide, NTT Communications and DoCoMo with the same opportunity to enter into such agreement with PLDT or Smart or Smart's subsidiaries, as the case may be.
- *Business Cooperation.* PLDT and DoCoMo agreed in principle to collaborate with each other on the business development, roll-out and use of a wireless-code division multiple access mobile communication network. In addition, PLDT agreed, to the extent of the power conferred by its direct or indirect shareholding in Smart, to procure that Smart will (i) become a member of a strategic alliance group for international roaming and corporate sales and services and (ii) enter into a business relationship concerning preferred roaming and inter-operator tariff discounts with DoCoMo.
- *Additional Rights of DoCoMo.* Upon NTT Communications, DoCoMo and their subsidiaries owning in the aggregate 20% or more of the shares of PLDT's common stock and for as long as NTT Communications, DoCoMo and their subsidiaries continue to own in the aggregate 17.5% of the shares of PLDT's common stock then outstanding, DoCoMo will be entitled to certain additional rights under the Cooperation Agreement.
- *Change in Control.* Each of NTT Communications, DoCoMo and the FP Parties agreed that to the extent permissible under applicable laws and regulations of the Philippines and other jurisdictions, subject to certain conditions, to cast its vote as a shareholder in support of any resolution proposed by the Board of Directors of PLDT for the purpose of safeguarding PLDT from any Hostile Transferee. A *Hostile Transferee* is defined under the Cooperation Agreement to mean any person (other than NTT Communications, DoCoMo, First Pacific or any of their respective affiliates) determined to be so by the PLDT Board of Directors and includes, without limitation, a person who announces an intention to acquire, seeking to acquire or acquires 30% or more of PLDT common shares then issued and outstanding from time-to-time or having (by itself or together with itself) acquired 30% or more of the PLDT common shares announces an intention to acquire, seeking to acquire or acquires a further 2% of such PLDT common shares: (a) at a price per share which is less than the fair market value as determined by the board of directors of PLDT as advised by a professional financial advisor; (b) which is subject to conditions which are subjective or which could not reasonably be satisfied; (c) without making an offer for all PLDT common shares not held by it and/or its affiliates and/or persons who, pursuant to an agreement or understanding (whether formal or informal), actively cooperate to obtain or consolidate control over PLDT; (d) whose offer for the PLDT common shares is unlikely to succeed or (e) whose intention is otherwise not *bona fide*; provided that, no person will be deemed a

Hostile Transferee unless prior to making such determination, the board of directors of PLDT has used reasonable efforts to discuss with NTT Communications and DoCoMo in good faith whether such person should be considered a Hostile Transferee.

- *Termination.* If NTT Communications, DoCoMo or their respective subsidiaries cease to own, in the aggregate, full legal and beneficial title to at least 10% of the shares of PLDT's common stock then issued and outstanding, their respective rights and obligations under the Cooperation Agreement and the Shareholders Agreement will terminate and the Strategic Arrangements (as defined in the Stock Purchase and Strategic Investment Agreement) will terminate. If the FP Parties and their respective subsidiaries cease to have, directly or indirectly, effective voting power in respect of shares of PLDT's common stock representing at least 18.5% of the shares of PLDT's common stock then issued and outstanding, their respective rights and obligations under the Cooperation Agreement, the Stock Purchase and Strategic Investment Agreement, and the Shareholders Agreement will terminate.

#### *2. Integrated i-mode Services Package Agreement between DoCoMo and Smart*

An Integrated i-mode Services Package Agreement was entered into by Smart and DoCoMo on February 15, 2006, under which DoCoMo agreed to grant Smart, on an exclusive basis within the territory of the Philippines for a period of five years, an integrated i-mode services package including a non-transferable license to use the licensed materials and the i-mode brand, as well as implementation support and assistance and post-commercial launch support from DoCoMo. Pursuant to this agreement, Smart is required to pay an initial license fee and running royalty fees based on the revenue arising from i-mode subscription fees and data traffic. Outstanding obligation under this agreement amounted to Php53 million as at December 31, 2006. Smart has no outstanding obligation under this agreement as at September 30, 2007.

#### *3. Advisory Services Agreement between DoCoMo and PLDT*

An Advisory Services Agreement was entered into by DoCoMo and PLDT on June 5, 2006, in accordance with the Cooperation Agreement dated January 31, 2006. Pursuant to the Advisory Services Agreement, DoCoMo will provide the services of certain key personnel in connection with certain aspects of the business of PLDT and Smart. Also, said agreement governs the terms and conditions of the appointments of such key personnel and the corresponding fees related thereto. Total fees under this agreement amounted to Php56 million and Php25 million for the nine months ended September 30, 2007 and 2006, respectively. Outstanding liability under this agreement amounted to Php18 million and Php32 million as at September 30, 2007 and December 31, 2006, respectively.

#### *4. Other Agreements with NTT Communications and/or its Affiliates*

PLDT is a party to the following agreements with NTT Communications and/or its affiliates:

- *Advisory Services Agreement.* On March 24, 2000, PLDT entered into an agreement with NTT Communications, as amended on March 31, 2003, March 31, 2005 and June 16, 2006, under which NTT Communications provides PLDT with technical, marketing and other consulting services for various business areas of PLDT starting April 1, 2000;
- *Arcstar Licensing Agreement and Arcstar Service Provider Agreement.* On March 24, 2000, PLDT entered into an agreement with NTT Worldwide Telecommunications Corporation under which PLDT markets managed data and other services under NTT Communications Arcstar brand to its corporate customers in the Philippines. PLDT also entered into a Trade Name and Trademark Agreement with NTT Communications under which PLDT has been given the right to use the tradename Arcstar and its related trademark, logo and symbols, solely for the purpose of PLDT's marketing, promotional and sales activities for the Arcstar services within the Philippines; and
- *Conventional International Telecommunications Services Agreement.* On March 24, 2000, PLDT entered into an agreement with NTT Communications under which PLDT and NTT Communications agreed to cooperative arrangements for conventional international telecommunications services to enhance their respective international businesses.

Total fees under these agreements amounted to Php83 million and Php144 million for the nine months ended September 30, 2007 and 2006, respectively. As at September 30, 2007 and December 31, 2006, outstanding obligations of PLDT under these agreements amounted to Php18 million.

5. *Agreement between Smart and Asia Link B.V., or ALBV.* Smart has an existing Technical Assistance Agreement with ALBV, a subsidiary of the First Pacific Group, for the latter's provision of technical support services and assistance in the operations and maintenance of cellular business for a period of five years, subject to renewal upon mutual agreement between the parties. The agreement provides for quarterly payments of technical service fees equivalent to 2% of the net revenues of Smart. In January 2004, the agreement was amended, reducing the technical service fees to be paid by Smart to ALBV to 1% of net revenues effective January 1, 2004. On February 18, 2004, Smart and ALBV entered into a renewal of the Technical Assistance Agreement extending the effectivity of the terms thereof to February 23, 2008. Furthermore, in view of the acquisition by Smart of ownership of 92.1% of the outstanding common stock of Piltel held by PLDT, the parties agreed to make the consolidated net revenues of Smart the basis for the computation of the 1% technical service fees payable by Smart to ALBV, effective January 1, 2005. Total service fees charged to operations under this agreement amounted to Php449 million and Php398 million for the nine months ended September 30, 2007 and 2006, respectively. As at September 30, 2007, Smart had advanced the payment of service fees to ALBV amounting to Php151 million. As at December 31, 2006, Smart had an outstanding liability to ALBV of Php128 million.

Smart also has an existing Services Agreement with ALBV for a period of 25 years starting January 1, 1999, which will automatically expire unless renewed by mutual agreement of both parties. Under the agreement, ALBV provides advice and assistance to Smart in sourcing capital equipment and negotiating with

international suppliers, arranging international financing and other services therein consistent with and for the furtherance of the objectives of the services. Service agreement fees were paid for the whole 25-year period. Outstanding prepaid management fees as at September 30, 2007 and December 31, 2006 amounted to Php830 million and Php869 million, respectively. Financing service fee charged to operations amounted to Php38 million each for the nine months ended September 30, 2007 and 2006.

*6. Agreements Relating to Insurance Companies.* Gotuaco del Rosario and Associates, or Gotuaco, acts as the broker for certain insurance companies to cover certain insurable properties of the PLDT Group. Insurance premiums are remitted to Gotuaco and the broker's fees are settled between Gotuaco and the insurance companies. In addition, PLDT has an insurance policy with Malayan Insurance Co., Inc., or Malayan, wherein premiums are directly paid to Malayan. Total insurance expenses under these agreements amounted to Php168 million and Php189 million for the nine months ended September 30, 2007 and 2006, respectively. Two directors of PLDT have direct/indirect interests in or serve as a director/officer of Gotuaco and Malayan.

***Compensation of Key Management Personnel of the PLDT Group***

PLDT Group's compensation of key management personnel by benefit type follows:

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Short-term employee benefits	<b>557</b>	464
Share-based payments (Note 21)	<b>214</b>	812
Post-employment benefits	<b>43</b>	26
	<b>814</b>	1,302

Each of the directors, including the members of the advisory board of PLDT, is entitled to a director's fee in the amount of Php125,000 for each meeting of the board attended. Each of the members or advisors of the audit, executive compensation, governance and nomination and finance committees is entitled to a fee in the amount of Php50,000 for each committee meeting attended.

There are no agreements between PLDT Group and any of its key management personnel providing for benefits upon termination of employment, except for such benefits to which they may be entitled under PLDT Group's retirement



and incentive plans.

## 21. Employee Benefits

### *Executive Stock Option Plan, or ESOP*

On April 27, 1999 and December 10, 1999, the Board of Directors and stockholders, respectively, approved the establishment of an ESOP and the amendment of the Seventh Article of the Articles of Incorporation of PLDT denying the pre-emptive right of holders of common stock to subscribe for any issue of up to 1,289,745 common stock pursuant to the ESOP. The ESOP covers management executives, which include officers with rank of Vice President up to the President, executives with the rank of Manager up to Assistant Vice President, and advisors/consultants engaged by PLDT. The ESOP seeks to motivate option holders to achieve PLDT's goals, reward option holders for the creation of shareholder value, align the option holders' interests with those of the stockholders of PLDT, and retain the option holders to serve the long-term interests of PLDT. The ESOP is administered by the Executive Compensation Committee of the Board of Directors. About 1.3 million shares of common stock of PLDT had been reserved as underlying option shares under the ESOP in 1999.

Movements in the number of stock options outstanding under the ESOP are as follows:

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
Balance at beginning of period	<b>119,034</b>	197,500
Exercised shares*	<b>(89,876)</b>	(78,466)
Balance at end of period	<b>29,158</b>	119,034

\* *Based on date of payment of exercised shares.*

As at September 30, 2007, there are 840,692 shares exercised by certain officers and executives at an exercise price of Php814 per share.

The fair value of the ESOP was estimated at the date of grant using an option pricing model, which considered annual stock volatility, risk-free interest rate, expected life of the option, exercise price of Php814 per share, and a weighted

average price of Php870 and Php315 per share for the 1999 and 2002 Grants, respectively, as at valuation date. Total fair value of shares granted amounted to Php359 million as at September 30, 2007 and December 31, 2006. No fair value of options were recognized as an expense for the nine months ended September 30, 2007 and 2006.

### ***LTIP***

On August 3, 2004, PLDT's Board of Directors approved the establishment of a Long-term Incentive Plan, or Original LTIP, for eligible key executive officers and advisors of PLDT and its subsidiaries, which is administered by the Executive Compensation Committee. The Original LTIP was a four-year cash-settled share based plan covering the period from January 1, 2004 to December 31, 2007, or the Performance Cycle. The payment was intended to be made at the end of the Performance Cycle (without interim payments) and contingent upon the achievement of an approved target increase in PLDT's common share price by the end of the Performance Cycle and a cumulative consolidated net income target for the Performance Cycle.

On August 28, 2006, PLDT's Board of Directors approved, in principle, the broad outline of the PLDT Group's strategic plans for 2007 to 2009 focusing on the development of new revenue streams to drive future growth while protecting the existing core communications business. To ensure the proper execution of the three-year plan, particularly with respect to the manpower resources being committed to such plans, a new LTIP, or New LTIP, upon endorsement of the Executive Compensation Committee, was approved by the Board of Directors to cover the period from January 1, 2007 to December 31, 2009, or New Performance Cycle. As a result of the establishment of the New LTIP, the Board also approved the early vesting of the Original LTIP by the end of 2006 for those of its participants who were invited to join the New LTIP and chose to join. Participants in the Original LTIP who were not invited to join the New LTIP, or who were invited but chose not to join, remained subject to the Original LTIP and its original vesting schedule.

Total number of shares appreciation rights remained outstanding under the existing 2004 to 2006 LTIP as at September 30, 2007 was 34,112 which is expected to be paid in May 2008. Total number of share appreciation rights awarded under the new 2007 to 2009 LTIP as at September 30, 2007 was 4,272,306, which will be paid in 2010.

The fair value of the LTIP was estimated using an option pricing model, which considered annual stock volatility, risk-free interest rates, the remaining life of options and the share price capped at Php2,300 as at December 31, 2006 for 2004 to 2006 LTIP and share price of Php2,910 as at September 30, 2007 for 2007 to 2009 LTIP. Incentive cost per share as at September 30, 2007 for the existing 2004 to 2006 LTIP and for the new 2007 to 2009 LTIP amounted to Php1,350 and Php1,068, respectively. The fair value of the LTIP recognized as an expense for the nine months ended September 30, 2007 (under the 2007 to 2009 LTIP) and 2006 (under the 2004 to 2006 LTIP) amounted to Php1,100 million and Php2,677 million, respectively. As at September 30, 2007 and December 31, 2006, total LTIP liability amounted to Php1,175 million and Php5,030 million, respectively, see *Note 3 Management's Use of Judgments, Estimates and Assumptions*.

**Pension***Defined Benefit Pension Plans*

We have defined benefit pension plans, covering substantially our permanent and regular employees, excluding those of Smart and its subsidiary, I-Contacts, which require contributions to be made to separate administrative funds.

Our actuarial valuation is done on an annual basis. Based on the latest actuarial valuation, the actual present value of accrued liabilities, net of pension cost and average assumptions used in developing the valuation are as follows:

	(in million pesos)
Benefit obligation as at December 31, 2006	13,314
Fair value of plan assets as at December 31, 2006	5,768
Funded status	7,546
Unrealized net transition obligation	(1)
Unrecognized net actuarial loss	(4,657)
Accrued benefit cost as at December 31, 2006 (Audited)	2,888
Accrual of pension cost during the period	1,081
Contributions	(1,318)
Accrued benefit cost as at September 30, 2007 (Unaudited)	2,651

Net pension cost was computed as follows:

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Components of net periodic benefit cost:		
Interest cost	<b>797</b>	670
Current service cost	<b>633</b>	376
Amortizations of unrecognized net actuarial loss	<b>96</b>	37
Recognition of transitional liability	<b>6</b>	
Expected return on plan assets	<b>(451)</b>	(406)
Net periodic benefit cost	<b>1,081</b>	677

The weighted average assumptions used to determine pension benefits as at September 30, 2007 and December 31, 2006 are as follows:

Discount rate	8%
Rate of increase in compensation	9%
Expected rate of return on plan assets	10%

As at September 30, 2007 and December 31, 2006, the assets of the beneficial trust fund established for the PLDT's pension plan include investments in shares of stocks of PLDT and Piltel with fair values aggregating Php2,464 million and Php2,185 million, which represent about 32% and 35%, respectively, of such beneficial trust fund's net assets available for plan benefits.

The Board of Trustees of the beneficial trust fund uses an investment approach of mixed equity and fixed income investments to maximize the long-term expected return of plan assets. The investment portfolio has been structured to achieve the objective of regular income with capital growth and out-performance of benchmarks. A majority of the investment portfolio consists of fixed income debt securities and various equity securities, while the remaining portion consists of multi-currency investments.

The allocation of the fair value of the beneficial trust fund's assets for the PLDT pension plan follows:

	<b>September 30, 2007 (Unaudited)</b>	December 31, 2006 (Audited)
Investments in equity securities	<b>57%</b>	52%
Investments in debt and fixed income securities	<b>22%</b>	23%
Investments in real estate	<b>8%</b>	10%
Investments in mutual funds	<b>6%</b>	8%
Investments in temporary placements	<b>7%</b>	7%
	<b>100%</b>	100%

Total contribution of PLDT to its pension plan for the nine months ended September 30, 2007 amounted to Php1,309 million.

*Defined Contribution Plan*

Contributions to the plan are made based on the employee's years of tenure and range from 5% to 10% of the employee's monthly salary. Additionally, employee has an option to make a personal contribution to the fund, at an amount not exceeding 10% of his monthly salary. The employer then provides an additional contribution to the fund ranging from 10% to 50% of the employee's contribution based on the latter's years of tenure.

The Plan's investment portfolio seeks to achieve regular income and long-term capital growth and consistent performance over its own portfolio benchmark. In order to attain this objective, the trustee's mandate is to invest in a diversified portfolio of bonds and equities, both domestic and international. The portfolio mix is kept at 60% to 90% for fixed income securities while 10% to 40% is allotted to equity securities.

The allocation of the fair value of plan assets for Smart as at September 30, 2007 (unaudited) and as at December 31, 2006 (audited) follows:

Investments in debt securities	68%
Investments in equity securities	29%
Others	3%
	100%

Smart currently expects to make approximately Php109 million of cash contributions to its pension plan in 2007.

*Pension Benefit Cost*

Total pension benefit cost follows:

	<b>Nine Months Ended September 30, 2007</b>	2006
	(Unaudited)	
	(in million pesos)	
Expense recognized for defined benefit plans	<b>1,081</b>	677
Expense recognized for defined contribution plans	<b>99</b>	83

Total (Note 5)

**1,180** 760**22. Contractual Obligations and Commercial Commitments***Contractual Obligations*

The following table discloses our unaudited consolidated contractual obligations outstanding as at September 30, 2007:

	<b>Payments Due by Period</b>				
	<b>Total</b>	<b>2-3</b>		<b>4-5</b>	
		<b>Within 1 year</b>	<b>years</b>	<b>Years</b>	<b>After 5 years</b>
	(in million pesos)				
Long-term debt(1)	69,214	7,073	17,617	16,861	27,663
Long-term lease obligations:					
Operating lease	3,511	620	1,241	827	823
Capital lease	1,441	1,414	26	1	
Unconditional purchase obligations(2)	796	71	45	242	438
Other long-term obligations	1,205	1,205			
<b>Total contractual obligations</b>	<b>76,167</b>	<b>10,383</b>	<b>18,929</b>	<b>17,931</b>	<b>28,924</b>

(1) Before deducting unamortized debt discount and debt issuance costs.

(2) Based on the Amended ATPA with AIL.

*Long-term Debt*

For a detailed discussion of our long-term debt, see *Note 17 Interest-bearing Financial Liabilities*.

*Long-term Operating Lease Obligations*

*Digital Passage Service Contracts.* PLDT has existing Digital Passage Service Contracts with foreign telecommunication administrations for several dedicated circuits to various destinations for 10 to 25 years expiring at various dates. As at September 30, 2007, PLDT's aggregate remaining obligation under these contracts amounted to approximately Php4 million.

*License Agreement with Mobius Management Systems (Australia) Pty Ltd., or Mobius.* PLDT entered into a license agreement with Mobius pursuant to which Mobius has granted PLDT a non-exclusive, non-assignable and non-transferable license for the use of computer software components. Under this agreement, Mobius is also required to provide maintenance services for a period of one year at no additional maintenance charge. PLDT may purchase maintenance services upon expiration of the first year for a fee of 15% of the current published license fee. As at September 30, 2007, PLDT's aggregate remaining obligation under this agreement was approximately Php20 million.

*Other Long-term Operating Lease Obligations.* The PLDT Group has various long-term lease contracts for periods ranging from two to ten years covering certain offices, warehouses, cell sites telecommunication equipment locations and various office equipment. In particular, Smart has lease obligations amounting to Php3,181 million as at September 30, 2007 in respect of office and cell site rentals with over 3,000 lessors nationwide, PLDT has lease obligations amounting to Php78 million as at September 30, 2007 in respect of office and lot rentals with over 175 lessors nationwide, ePLDT has lease obligations amounting to Php183 million as at September 30, 2007 in respect of certain office space rentals and PLDT Global has lease obligations amounting to Php45 million as at September 30, 2007 in respect of certain office space rentals.

*Long-term Capital Lease Obligations*

For the detailed discussion of our long-term capital lease obligations, see *Note 17 Interest-bearing Financial Liabilities*.

*Unconditional Purchase Obligations*

For a detailed discussion of PLDT's obligation under the amended ATPA, see *Note 20 Related Party Transactions*.

As at September 30, 2007, PLDT's aggregate remaining minimum obligation under the amended ATPA was approximately Php796 million.

*Other Long-term Obligations*

*Mandatory Conversion and Purchase of Shares.* As discussed in *Note 17 Interest-bearing Financial Liabilities*, as at September 30, 2007, PLDT had issued a total of 3 million shares of Series V Convertible Preferred Stock, 5 million shares of Series VI Convertible Preferred Stock and 4 million shares of Series VII Convertible Preferred Stock in exchange for a total of 58 million shares of Series K Class I Convertible Preferred Stock of Piltel, pursuant to the debt restructuring plan of Piltel adopted in June 2001. As at September 30, 2007, 2,687,490 shares of Series V Convertible Preferred Stock, 4,588,860 shares of Series VI Convertible Preferred Stock and 3,842,000 shares of Series VII Convertible Preferred Stock had been voluntarily converted to PLDT common shares. As at September 30, 2007, 33,950 shares of Series V and 706,244 shares of Series VI Convertible Preferred Stocks remained outstanding.

Each share of Series V and VI Convertible Preferred Stocks is convertible at any time at the option of the holder into one PLDT common share. On the date immediately following the seventh anniversary of the issue date of the Series V and Series VI Convertible Preferred Stocks, the remaining outstanding shares under these series will be mandatorily converted to PLDT common shares. Under a put option exercisable for 30 days, holders of common shares received on mandatory conversion of the Series V and VI Convertible Preferred Stocks will be able to require PLDT to purchase such PLDT common shares for Php1,700 per share and US\$36.132 per share, respectively.

The aggregate value of the put option based on outstanding shares as at September 30, 2007 was Php1,205 million which is puttable on June 4, 2008, if all of the outstanding shares of Series V and VI Convertible Preferred Stocks were mandatorily converted and all the common shares were put to PLDT at that time. The market value of the underlying common shares was Php2,154 million, based on the market price of PLDT common shares of Php2,910 per share as at September 30, 2007.

*Commercial Commitments*

As at September 30, 2007, our outstanding commercial commitments, in the form of letters of credit, amounted to Php1,846 million. These commitments will expire within one year.

**23. Provisions and Contingencies**



As discussed below, we currently expect that going forward, we will pay local franchise taxes on an annual basis and based on the gross receipts received or collected for services rendered within the jurisdiction of the respective taxing authority. For this reason, we have made the appropriate provisions in our unaudited consolidated financial statements as at September 30, 2007.

*NTC Supervision and Regulation Fees, or SRF*

Since 1976, PLDT has received assessments from NTC for permit, SRF and other charges pursuant to Section 40 of Commonwealth Act 146, otherwise known as the Public Service Act. As at September 30, 2007, PLDT had paid, since 1994, a total amount of Php2,541 million in SRF, of which Php2,251 million was paid under protest.

PLDT is contesting the manner by which these assessments were calculated and the basis for such calculations. The case is now with the Supreme Court and upon the rules and practice of court, stands submitted for decision.

*Local Business and Franchise Tax Assessments*

PLDT is presently a party to several cases involving the issue of exemption of PLDT from local franchise and business taxes. PLDT believes, based on the opinion of its legal counsel, that it is exempt from payment of local franchise and business taxes.

The Local Government Code of 1991, or Republic Act (R.A.) 7160, which took effect on January 1, 1992, extended to local government units, or LGUs, the power to tax businesses within their territorial jurisdiction granted under Batas Pambansa 337, and withdrew tax exemptions previously granted to franchise grantees under Section 12 of R.A. 7082.

PLDT believes, based on the opinion of its legal counsel, that R.A. 7925 which took effect on March 16, 1995, and the grant of local franchise and business taxes exemption privileges to other franchise holders subsequent to the effectivity of R.A. 7160, implicitly restored its local franchise and business taxes exemption privilege under Section 12 of R.A. 7082, or the PLDT Franchise pursuant to Section 23 thereof or the quality of treatment clause.

To confirm this position, PLDT sought and obtained on June 2, 1998 a ruling from the Bureau of Local Government Finance, or BLGF, of the Philippine Department of Finance, which ruled that PLDT is exempt from the payment of local franchise and business taxes imposed by LGUs under R.A. 7160.

By virtue of the BLGF Ruling, PLDT stopped paying local franchise and business taxes starting with the fourth quarter of 1998 and has filed with certain LGUs claims for tax refund covering the period from the second quarter of 1995 to the third quarter of 1998. PLDT has received assessments for local franchise and business taxes from several cities and provinces following PLDT's decision to stop payment of local franchise and business taxes.

Following a decision of the Supreme Court on March 25, 2003, a judgment in the amount of Php4 million against PLDT involving the City of Davao became final and executory on April 9, 2003, pursuant to which PLDT was declared not exempt from the local franchise tax. Pursuant to the said decision, PLDT has voluntarily paid the total amount of Php15 million for the period from the fourth quarter of 1998 until December 31, 2003, which includes the Php4 million subject of the case. The said amount constitutes only the basic franchise tax due for the said period, excluding surcharges and interest which PLDT is asking the City of Davao, through the local council, to waive. PLDT believes, based on the opinion of its legal counsel, that PLDT is not liable for surcharges and interest considering that the legal issue involved was a difficult one and PLDT's non-payment of the said taxes was made in good faith. On August 2, 2005, the local Sanggunian passed a resolution denying PLDT's request for abatement of surcharges and penalties and directing the City Treasurer to update PLDT's liability and immediately collect the same. Accordingly, on August 26, 2005, the city treasurer issued an assessment to PLDT in the amount of Php12 million. In order to maintain and preserve its good standing and relationship with the City of Davao, PLDT has paid the surcharges and penalties as at December 31, 2005.

Although PLDT believes that it is not liable to pay local franchise and business taxes, PLDT has entered into compromise settlements with several LGUs, including the City of Makati, in order to maintain and preserve its good standing and relationship with these LGUs. Under these compromise settlements, which have mostly been approved by the relevant courts, PLDT has paid a total amount of Php680 million for local franchise tax covering prior periods up to the end of 2006 as at September 30, 2007.

PLDT no longer had contested assessments from LGUs for franchise taxes based on gross receipts received or collected for services within their respective territorial jurisdiction as at December 31, 2006.

PLDT likewise continues to contest the imposition of local business taxes in addition to local franchise tax by the Cities of Tuguegarao, Balanga and Caloocan in the amounts of Php1.9 million, Php0.2 million and Php6.2 million, respectively, for the years 1998 to 2003 for the City of Tuguegarao, and for the years 2005 to 2007 for the Cities of Balanga and Caloocan. PLDT is likewise contesting the imposition of a business tax on the transmission of messages by the Municipality of San Pedro in the amount of Php0.3 million for the years 2005 to 2007. In addition, PLDT is contesting the imposition of franchise tax by the Province of Cagayan based on gross receipts derived from outside its territorial jurisdiction in the amount of Php3 million for the years 1999 to 2006.

PLDT currently expects that going forward it will pay local franchise taxes on an annual basis and based on the gross receipts received or collected for services rendered within the jurisdiction of the respective taxing authority.

Smart has received and paid under protest the local franchise tax assessment issued by the City of Makati totaling approximately Php312 million, but which had been finally resolved by the Regional Trial Court (RTC) of Makati and upheld by the Court of Appeals (CA) in favor of Smart in the case entitled *Smart Communications, Inc. vs. City of Makati* (Civil Cases No. 02-249 and 02-725, August 3, 2004) dated August 3, 2004. The said RTC decision declaring Smart exempt from payment of local franchise tax and in reversing the decision of the Makati City Miscellaneous Taxes, Fees and Charge Division to assess and/or collect from Smart an amount totaling approximately Php312 million had already become final and executory.

Also, Smart received LFT assessments issued by the City of Iloilo amounting to approximately Php1 million. The RTC of Iloilo likewise ruled in favor of Smart in its decision dated January 19 2005, but the City of Iloilo filed an appeal with the Supreme Court which remains unresolved to date.

*Piltel's Bureau of Internal Revenue, or BIR, Assessment*

On December 12, 2005, Piltel filed a collective application for a compromise settlement with the BIR for the deficiency tax assessments arising from taxable years 1998, 1999 and 2001, citing reasonable doubt as to the validity of the tax assessments as a basis. The prescribed minimum percentage of the compromise settlement for such basis is 40% of the basic assessed tax.

On January 27, 2006, Piltel received the favorable recommendation and approval from the BIR on the said application for a compromise settlement. On January 31, 2006, Piltel settled the total amount of Php114 million, which is equivalent to 40% of the basic taxes per final assessment notices received, to effect the immediate cancellation of the tax assessments. On February 24, 2006, the BIR accepted Piltel's application for compromise settlement of income tax and VAT for the years 1998 and 1999, and income taxes and VAT for the year 2001, and accordingly, issued the Certificate of Availment on the said date.

*Enhanced Voluntary Assessment Program, or EVAP, Availment*

In 2005, the BIR launched the EVAP which grants taxpayers, who availed themselves of the program and are qualified, the privilege of the last priority in BIR audit and investigation. The EVAP apply to all internal revenue taxes covering the taxable year ending December 31, 2004 and all prior years, including one-time transactions such as estate tax, donor's tax, capital gains tax, expanded withholding tax and documentary stamp tax on the transfer, sale, exchange, or disposition of assets, and shall likewise cover taxpayers enjoying preferential tax treatment. A taxpayer who has availed of the EVAP and is qualified to avail shall not be audited except upon prior authorization and approval of the Commissioner of Internal Revenue when there is strong evidence or finding of understatement in the payment of a taxpayer's correct tax liability by more than 30% as supported by a written report of the appropriate office stating in detail the facts and the law on which such finding is based: Provided, however, that any EVAP payment should be allowed as tax credit against the deficiency tax due, if any, in case the concerned taxpayer has been subjected to tax audit.

PLDT availed itself of the program and paid a total of Php6 million for VAT and income tax for taxable year 2004, and VAT and withholding tax for taxable year 2002.

Maratel availed itself of the EVAP for income tax for the taxable year 2004, SubicTel availed the program for its income tax, withholding tax and percentage tax for taxable year 2002 and ClarkTel availed of the program for its income tax for both taxable years 2003 and 2004. The total payment of Maratel, SubicTel and ClarkTel amounted to Php800,000. Smart availed of the EVAP and paid Php53 million for the following tax types and taxable years: income tax for the taxable years 2003 and 2004; VAT for the taxable year 2002; OCT for the year 2002; and the withholding taxes for the taxable years 2002, 2003 and 2004. On August 2, 2006, Smart received its Certificate of Qualification, or CQ, for the EVAP availment for income tax, VAT, OCT and withholding taxes for taxable year 2002. Piltel likewise availed of EVAP and paid Php3 million for the following tax types and taxable years: income tax for the taxable year 2003; and the expanded withholding tax for the taxable years 2003 and 2004. To date, the BIR has not issued the CQ for Piltel's EVAP availment.

PLDT received its EVAP CQ on January 22, 2007 for income tax and VAT for taxable year 2004 and on March 28, 2007 for VAT for taxable year 2002 while it received a Notice of Disqualification for EVAP on March 30, 2007 for withholding tax for taxable year 2002. SubicTel and ClarkTel received their respective EVAP CQ on September 13, 2006 and December 10, 2006, respectively, while Maratel was advised by BIR Revenue District Office No. 101, Iligan City in December 2006, that its EVAP application has been disqualified, however, Notice of Disqualification has not been issued by the BIR.

#### *Improved Voluntary Assessment Program, or IVAP, Availment*

In 2006, the BIR launched the IVAP which similarly grants taxpayers who availed themselves of the program and are qualified, the privilege of the last priority in BIR audit and investigation. The IVAP applies to all internal revenue taxes covering the taxable year ending December 31, 2005 and fiscal year ending on any day not later than June 30, 2006 and all prior years, including one-time transactions such as estate tax, donor's tax, capital gains tax, expanded withholding tax and documentary stamp tax on the transfer, sale, exchange, or disposition of assets, and shall likewise cover taxpayers enjoying preferential tax treatment. Unlike the EVAP, however, where the taxpayers only enjoy the privilege of last priority in audit, with the IVAP, taxpayers who availed themselves of the same will no longer be subject to tax audit except only in the case of fraud manifested through understatement of the correct tax liability by more than 30%.

Smart availed of the IVAP and paid Php40 million for the following tax types and taxable years: income tax for year 2005; and VAT for year 2005. To date, the BIR has not issued the CQ for Smart's IVAP availment.

Maratel availed itself of the IVAP for the taxable years 2004 and 2005 for its income, VAT, percentage and withholding taxes, while SubicTel availed itself of the program for the taxable year 2004 for its income and value added taxes only and for the taxable year 2005, for its income, VAT and withholding taxes. ClarkTel availed itself of the IVAP for the taxable years 2003, 2004, 2005 for income and withholding taxes except for income taxes for taxable years 2003 and 2004 where an EVAP CQ covering these taxable periods was already issued. The total collective IVAP payments for Maratel, SubicTel and ClarkTel amounted to Php12 million. The IVAP CQ has been issued for the IVAP availments made by Maratel last April 12, 2007 and May 9, 2007 for 2004 and 2005 respectively. In July 2007, the IVAP CQ has been issued for the IVAP availments made by Clarktel for taxable years 2003 2004 and 2005. The IVAP CQ of SubicTel is still being processed by their BIR Regional Office.

## 24. Financial Assets and Liabilities

Our financial assets and liabilities are recognized initially at fair value. Transaction costs (debt issuance costs) are included in the initial measurement of all financial assets and liabilities except those classified as financial instruments measured at fair value through profit and loss. Subsequent to initial recognition, assets and liabilities are either valued at amortized cost using the effective interest rate method or at fair value depending on the classification.

The following table sets forth the carrying values and estimated fair values of our financial assets and liabilities recognized as at September 30, 2007 and December 31, 2006. There are no material unrecognized financial assets and liabilities as at September 30, 2007 and December 31, 2006.

	Carrying Value		Fair Value	
	September 30, 2007	December 31, 2006	September 30, 2007	December 31, 2006
	(Unaudited)	(Audited)	(Unaudited)	(Audited)
	(in million pesos)			
<b>Noncurrent Financial Assets</b>				
Investments-available-for-sale (Note 2)	142	116	142	116
Derivative financial assets (Note 2)	93	434	93	434
Investment in debt securities (Note 2)	268		269	
Total noncurrent financial assets	503	550	504	550
<b>Current Financial Assets</b>				
Cash and cash equivalents (Notes 2 and 13)	8,471	16,870	8,471	16,870
Short-term investments (Note 2)	11,522	8,327	11,522	8,327
Trade and other receivables (Notes 2, 3 and 14)	10,245	10,158	10,245	10,158
Derivative financial assets (Note 2)	80	47	80	47
Total current financial assets	30,318	35,402	30,318	35,402
<b>Total Financial Assets</b>	<b>30,821</b>	<b>35,952</b>	<b>30,822</b>	<b>35,952</b>

**Noncurrent Financial Liabilities**

Long-term debt - net of current portion* (Notes 2, 8, 17, and 22)	<b>57,273</b>	63,769	<b>61,632</b>	70,416
Obligations under capital lease* (Notes 2, 8, 17, and 22)	<b>26</b>	106	<b>26</b>	106
Preferred stock subject to mandatory redemption* (Notes 2, 17 and 22)		1,369		1,528
Derivative financial liabilities (Note 2)	<b>6,800</b>	6,872	<b>6,800</b>	6,872
Total noncurrent financial liabilities	<b>64,099</b>	72,116	<b>68,458</b>	78,922
<b>Current Financial Liabilities</b>				
Accounts payable (Note 2)	<b>12,042</b>	8,634	<b>12,042</b>	8,634
Notes payable* (Notes 2, 8, 17, and 22)	<b>487</b>	201	<b>487</b>	201
Derivative financial liabilities (Note 2)	<b>15</b>	108	<b>15</b>	108
Current portion of long-term debt* (Notes 2, 8, 17, and 22)	<b>6,965</b>	16,184	<b>7,845</b>	17,512
Obligations under capital lease* (Notes 2, 8, 17, and 22)	<b>911</b>	924	<b>911</b>	924
Preferred stock subject to mandatory redemption* (Notes 2, 17 and 22)	<b>1,114</b>		<b>1,164</b>	
Total current financial liabilities	<b>21,534</b>	26,051	<b>22,464</b>	27,379
<b>Total Financial Liabilities</b>	<b>85,633</b>	98,167	<b>90,922</b>	106,301

\* Included under *Interest-bearing Financial Liabilities* in the consolidated balance sheets.

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

Interest-bearing Financial Liabilities:

*Long-term debt*: Fair value is based on the following:

<b>Debt Type</b>	<b>Fair Value Assumptions</b>
Fixed Rate Loans:	
U.S. dollar notes/convertible debt	Quoted market price.
Other loans in all other currencies	Estimated fair value is based on the discounted value of future cash flows using the applicable CIRR and PDST rates for similar types of loans.

Variable Rate Loans	The carrying value approximates fair value because of recent and regular repricing based on market conditions.
---------------------	--

*Preferred stock subject to mandatory redemption:* The fair values were determined using a discounted cash flow model.

Derivative financial instruments:

*Foreign currency options:* The fair values were computed using an option pricing model.

*Forward foreign exchange contracts, bifurcated foreign currency forwards, foreign currency and interest rate swaps:* The fair values were computed as the present value of estimated future cash flows.

*Bifurcated equity call options:* The fair values were computed using an option pricing model.

Due to the short-term nature of the transactions, the fair value of cash and cash equivalents, short-term investments, trade and other receivables, notes payable and accounts payable approximate the carrying amounts as of the balance sheet date.

*Financial assets and liabilities carried at amortized cost*

Unamortized debt discount, representing debt issuance costs and any difference between the fair value of consideration given or received on initial recognition, included in following financial liabilities amounted to Php5,571 million and Php6,753 million as at September 30, 2007 and December 31, 2006, respectively, see *Note 17 Interest-bearing Financial Liabilities*.

*Financial assets and liabilities carried at fair value*

The following financial assets and liabilities were carried at fair value as at September 30, 2007 and December 31, 2006.

	<b>September 30, 2007</b>	December 31, 2006
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Investments-available-for-sale	<b>142</b>	116
Derivative financial instruments	<b>(6,642)</b>	(6,499)
	<b>(6,500)</b>	(6,383)

### *Derivative Financial Instruments*

Our derivative financial instruments are accounted for as either cash flow hedges or transactions not designated as hedges. Cash flow hedges refer to those transactions that hedge our exposure to variability in cash flows attributable to a particular risk associated with a recognized asset or liability. Changes in the fair value of these instruments representing effective hedges are recognized as cumulative translation adjustments in equity until the hedged item is recognized in earnings. For transactions that are not designated as hedges, any gains or losses arising from the changes in fair value are recognized directly to income for the period.

The table below sets out the information about our derivative financial instruments as at September 30, 2007 and December 31, 2006:

	<b>September 30, 2007</b>		December 31, 2006	
	<b>(Unaudited)</b>		(Audited)	
	<b>Maturity</b>	<b>Notional</b>	<b>Mark-to-market Gains</b>	<b>Mark-to-market Gain</b>
			<b>(Losses)</b>	<b>(Loss)</b>
			Notional	
			(in millions)	
<b><i>PLDT</i></b>				
Cash flow hedges:				
Long-term currency swaps				
	2017	<b>US\$300</b>	<b>(Php3,003)</b>	US\$300
	2012	<b>250</b>	<b>(2,798)</b>	250
				(Php2,716)
				(2,475)
Long-term foreign currency options				
	2009	<b>136</b>	<b>(586)</b>	167
				(747)
Transactions not designated as hedges:				
Long-term foreign currency options				
	2009	<b>136(1)</b>	<b>84</b>	167(1)
				138



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Short-term currency options	2007			7	(6)	
Interest rate swap	2012	<b>31</b>		<b>(206)</b>	63	(423)
Forward foreign exchange contracts				202	(90)	
Bifurcated equity call options	2008	<b>1 share</b>		<b>(213)</b>	1 share	(224)
				<b>(6,722)</b>		(6,543)
<b>Smart</b>						
Transactions not designated as hedges:						
Forward foreign exchange contracts	2007	<b>US\$19</b>		<b>30</b>	US\$	
Bifurcated embedded derivatives	2007	<b>11</b>		<b>50</b>	15	44
				<b>80</b>		44
Net liabilities				<b>(Php6,642)</b>		(Php6,499)

(1) Non-hedged portion of 2009 long-term foreign currency options based on the same notional amount as the hedged portion.

	<b>September 30,</b>	December 31, 2006
	<b>2007</b>	(Audited)
	<b>(Unaudited)</b>	(Audited)
	(in million pesos)	
Presented as:		
Noncurrent assets	<b>93</b>	434
Current assets	<b>80</b>	47
Noncurrent liabilities	<b>(6,800)</b>	(6,872)
Current liabilities	<b>(15)</b>	(108)
Net liabilities	<b>(6,642)</b>	(6,499)

Cumulative translation adjustments as at September 30, 2007 and December 31, 2006 consists of:

	<b>September</b>	December 31,
	<b>30,</b>	2006
	<b>2007</b>	(Audited)
	(in million pesos)	
Cumulative translation adjustments at beginning of period	<b>(1,796)</b>	1,253

Movements of cumulative translation adjustments:		
Deferred income tax effects on cash flow hedges	<b>(633)</b>	1,088
Currency translation differences	<b>(935)</b>	(535)
Net gains (losses) on available-for-sale financial assets	<b>31</b>	(5)
Net losses on cash flow hedges removed from cumulative translation adjustments and taken to income	<b>2,570</b>	2,855
Net losses on cash flow hedges	<b>(460)</b>	(6,452)
	<b>573</b>	(3,049)
Cumulative translation adjustments at end of period	<b>(1,223)</b>	(1,796)

Analysis of loss on derivative transactions for the nine months ended September 30, 2007 and 2006 are as follows:

	<b>Nine Months Ended September 30, 2007 2006 (Unaudited) (in million pesos)</b>	
Net mark-to-market losses at end of period	<b>(6,642)</b>	(5,075)
Net mark-to-market losses at beginning of period	<b>(6,499)</b>	(3,284)
Net change	<b>(143)</b>	(1,791)
Net losses charged to cumulative translation adjustments	<b>460</b>	4,711
Settlements, accretion and conversion	<b>(524)</b>	(3,071)
Net losses on derivative transactions (Note 5)	<b>(207)</b>	(151)

## ***PLDT***

### ***Cash Flow Hedges***

#### ***Long-term Currency Swaps***

PLDT entered into long-term principal only currency swap agreements with various foreign counterparties to hedge the currency risk on its fixed rate notes maturing in 2009, 2012 and 2017. As at September 30, 2007 and December 31, 2006, these long-term currency swaps have an aggregate notional amount of US\$550 million. Under the swaps, PLDT effectively exchanges the principal of its U.S. dollar-denominated fixed rate notes into Philippine peso-denominated loan exposures at agreed swap exchange rates. The agreed swap exchange rates are reset to the lowest U.S. dollar/Philippine peso spot exchange rate during the term of the swaps, subject to a minimum exchange rate. In March and April 2004, PLDT entered into amendments to keep the lowest reset exchange rate and unwind the

downward resettable feature of US\$550 million of its long-term principal only currency swap agreements in order to lower the running hedging cost of the swaps. As at September 30, 2007 and December 31, 2006, the outstanding swap contracts have an agreed average swap exchange rate of Php50.76.

In order to manage hedge costs, these swaps included a credit-linkage feature with PLDT as the reference entity. The specified credit events include bankruptcy, failure to pay, obligation acceleration, moratorium/repudiation, and restructuring of PLDT bonds or all or substantially all of PLDT's obligations. Upon the occurrence of any of these credit events, subject to agreed threshold amounts where applicable, the obligations to both PLDT and its counterparty under the swap contracts terminate without further settlements to either party, including any mark-to-market value of the swaps. As at September 30, 2007 and December 31, 2006, US\$686 million and US\$717 million, respectively, of PLDT's long-term currency swaps/options have been structured to include credit-linkage with PLDT as the reference entity. The semi-annual fixed or floating swap cost payments that PLDT is required to make to its counterparties averaged about 4.08% and 5.18% per annum as at September 30, 2007 and December 31, 2006, respectively. As cash flow hedges, any movements in the fair value of these instruments will be taken as a cumulative translation adjustment under equity in our consolidated balance sheets.

#### *Long-term Foreign Currency Options*

To manage hedging costs, the currency swap agreement relating to the 2009 fixed rate notes with a notional amount of US\$175 million has been structured to include currency option contracts. If the Philippine peso to U.S. dollar spot exchange rate on maturity date settles beyond Php90.00 to US\$1.00, PLDT will have to purchase U.S. dollar at an exchange rate of Php52.50 to US\$1.00 plus the excess above the agreed threshold rate. On the other hand, if on maturity, the Philippine peso to U.S. dollar spot exchange rate is lower than the exchange rate of Php52.50 to US\$1.00, PLDT will have the option to purchase at the prevailing Philippine peso to U.S. dollar spot exchange rate. In July 2004, PLDT and its counterparty, agreed to re-document and re-classify the transaction into long-term currency option contracts. The net semi-annual floating hedge cost payments that PLDT is required to pay under these transactions was approximately 5.74% and 6.17% per annum as at September 30, 2007 and December 31, 2006, respectively.

The option currency contract relating to PLDT's option to purchase U.S. dollar at Php52.50 to US\$1.00 or prevailing spot exchange rate at maturity, whichever is lower, qualifies as a cash flow hedge. The option currency contract relating to the counterparty's option to purchase foreign currency from PLDT at Php90.00 to US\$1.00 is not designated as a hedge. Please refer to discussion below (under transactions not designated as hedges).

In December 2006, the currency option agreement was partially terminated, which effectively lowered the outstanding currency options notional amount to US\$167 million. Total amounts settled for the unwinding is Php40 million.

In January 2007, the currency option agreement was again partially terminated where the outstanding currency options notional amount was lowered to US\$136 million. Total amounts settled for the unwinding is Php177 million.

### *Transactions Not Designated as Hedges*

Due to the amounts of PLDT's foreign currency hedging requirements and the large interest differential between the Philippine peso and the U.S. dollar, the costs to book long-term hedges can be significant. In order to manage such hedging costs, PLDT utilizes structures that include currency option contracts, and fixed-to-floating coupon-only swaps that may not qualify for hedge accounting.

### *Long-term Foreign Currency Options*

With reference to the above-mentioned hedge on PLDT's 2009 fixed rate notes, PLDT simultaneously sold a currency option contract with the same notional amount of US\$175 million with the same maturity that gives the counterparty a right to purchase foreign currency at Php90.00 to US\$1.00. Together with the long-term currency option contract classified under cash flow hedges, PLDT has the obligation to purchase U.S. dollars at an exchange rate of Php52.50 to US\$1.00 plus the excess above the agreed threshold rate. In exchange for this condition, the overall net hedging cost for the transaction is reduced. In December 2006, the currency option agreement was partially terminated, which lowered the notional amount to US\$167 million. Since charges in fair value have already been recognized as profit and loss in prior periods, the corresponding proceeds from the partial termination of the currency option contract amounted to Php7 million.

In January 2007, the currency option agreement was again partially terminated where outstanding notional amount was lowered to US\$136 million. Proceeds from the transaction amounted to Php33 million.

### *Short-term Foreign Currency Options*

PLDT entered into short-term U.S. dollar currency option contracts to hedge our other short-term foreign currency obligations. There were no outstanding currency option contracts as at September 30, 2007. As at December 31, 2006, outstanding U.S. dollar currency option contracts amounted to US\$7 million with an average rating of US\$50.40.

### *Interest Rate Swap*

A portion of PLDT's currency swap agreements to hedge its 2017 fixed rate notes carry fixed rate swap cost payments. To effectively lower the running cost of such swap agreements, PLDT, in April 2003, entered into an agreement to swap the coupon on US\$125 million of its 2012 fixed rate notes into a floating rate Japanese yen amount. Under this

agreement, PLDT is entitled to receive a fixed coupon rate of 11.375%, provided the Japanese yen to U.S. dollar exchange rate stays above JP¥99.90 to US\$1.00. Below this level, a reduced fixed coupon rate of 3% will be due to PLDT. In order to mitigate the risk of the Japanese yen strengthening below the agreed threshold, PLDT, in December 2003, entered into an overlay swap transaction to effectively lower the portion of the coupon indexed to the U.S. dollar to Japanese yen rate to 3% such that the fixed coupon rate due to PLDT when the Japanese yen strengthens below the agreed threshold will be 8.375%. Both swap agreements include a credit-linkage feature with PLDT as the reference entity.

In March 2006, the interest rate and overlay swap agreements were partially terminated to effectively lower the outstanding interest rate swap notional amount to US\$62.5 million. Since changes in fair values have already been recognized as profit and loss in prior periods, the corresponding liability settled by PLDT amounted to Php804 million.

In April 2007, the interest and overlay swap agreements were again partially terminated where outstanding notional amount was lowered to US\$31 million. Total amounts settled for the unwinding is Php276 million.

#### *Forward Foreign Exchange Contracts*

PLDT entered into short-term U.S. dollar forward foreign exchange contracts to hedge short-term foreign currency obligations. There were no outstanding forward foreign exchange contracts as at September 30, 2007. As at December 31, 2006, outstanding forward foreign exchange contracts amounted to US\$202 million with an average exchange rate of Php49.50.

#### *Bifurcated Equity Call Options*

Pursuant to Piltel's debt restructuring plan, PLDT issued its Series VI and VII Convertible Preferred Stock, see *Note 17 Interest-bearing Financial Liabilities*. Each share of Series VI and VII Convertible Preferred Stock is convertible at any time at the option of the holder into one share of PLDT's common stock. On the date immediately following the seventh anniversary of the issue date of the Series VI Convertible Preferred Stock and on the eighth anniversary of the issue date of the Series VII Convertible Preferred Stock, the remaining outstanding shares under these series will be mandatorily converted into shares of PLDT common stock. For 30 days thereafter, the holders of these mandatorily converted shares of common stock have the option to sell such shares of common stock back to PLDT for US\$36.132 per share and JPY4,071.89 per share for Series VI and VII, respectively. On August 18, 2006, all 3,842,000 shares of Series VII shares were converted to PLDT common stock. As at September 30, 2007 and December 31, 2006, the negative fair market value of these embedded call options amounted to Php213 million and Php224 million, respectively.

***Smart***

Smart entered into short-term offshore deliverable and non-deliverable forward contracts in July and August 2007 for a total amount of US\$19 million to hedge 38% of the total expected loan proceeds from the undrawn facility of US\$50 million.

Smart's other embedded derivatives were bifurcated from service and purchase contracts. As at September 30, 2007 and December 31, 2006, outstanding contracts included service contract with foreign equipment suppliers and various suppliers covering handset importations denominated in U.S. dollars, which is not the functional currency of a substantial party to the contract or the routine currency of the transaction.

**Financial Risk Management Objectives and Policies**

The main purpose of our financial instruments is to fund our operations. We also enter into derivative transactions, the purpose of which is to manage the currency risks and interest rate risks arising from our operations and our sources of financing. It is, and has been throughout the year under review, our policy that no trading in financial instruments shall be undertaken.

The main risks arising from our financial instruments are liquidity risk, foreign exchange risk, interest rate risk and credit risk. Our Board reviews and approves policies for managing each of these risks. These risks are summarized below. We also monitor the market price risk arising from all financial instruments. Our accounting policies in relation to derivatives are set out in *Note 2 Summary of Significant Accounting Policies and Practices*.

***Liquidity Risk***

We seek to manage our liquidity profile to be able to finance our capital expenditures and service our maturing debts. To cover our financing requirements, we currently intend to use internally generated funds and proceeds from debt and equity issues and sales of certain assets.

As part of our liquidity risk management program, we regularly evaluate our projected and actual cash flow information and continuously assess conditions in the financial markets for opportunities to pursue fund-raising initiatives. These initiatives may include bank loans, export credit agency-guaranteed facilities, and debt capital and equity market issues.

**Foreign Exchange Risk**

The following table shows our consolidated foreign currency-denominated monetary assets and liabilities and their peso equivalents as at September 30, 2007 and December 31, 2006:

	<b>September 30, 2007</b>		December 31, 2006	
	<b>(Unaudited)</b>		(Audited)	
	<b>U.S. Dollar</b>	<b>Php Equivalent(1)</b>	U.S. Dollar	Php Equivalent(2)
	(in millions)			
<b>Noncurrent Financial Assets</b>				
Derivative financial assets	US\$2	Php93	US\$9	Php434
<b>Current Financial Assets</b>				
Cash and cash equivalents	80	3,582	155	7,578
Short-term investments	49	2,195	92	4,521
Trade and other receivables	255	11,482	277	13,589
Derivative financial assets	2	80	1	47
Total current financial assets	386	17,339	525	25,735
<b>Total Financial Assets</b>	<b>US\$388</b>	<b>Php17,432</b>	<b>US\$534</b>	<b>Php26,169</b>
<b>Noncurrent Financial Liabilities</b>				
Interest-bearing financial liabilities - net of current portion	US\$1,121	Php50,431	US\$1,239	Php60,756
Derivative financial liabilities	151	6,800	140	6,872
Total noncurrent financial liabilities	1,272	57,231	1,379	67,628
<b>Current Financial Liabilities</b>				
Accounts payable	US\$183	Php8,224	US\$268	Php13,115
Accrued expenses and other current liabilities	80	3,578	74	3,605
Derivative financial liabilities		15	2	108
Current portion of interest-bearing financial liabilities	177	7,978	328	16,104
Total current financial liabilities	440	19,795	672	32,932
<b>Total Financial Liabilities</b>	<b>US\$1,712</b>	<b>Php77,026</b>	<b>US\$2,051</b>	<b>Php100,560</b>

(1) The exchange rate used was Php44.974 to US\$1.00.

(2) The exchange rate used was Php49.045 to US\$1.00.

In translating the foreign currency-denominated monetary assets and liabilities into peso amounts, the exchange rates used were Php44.974 to US\$1.00 and Php49.045 to US\$1.00, the Philippine peso-U.S. dollar exchange rates as at September 30, 2007 and December 31, 2006, respectively.

As at November 5, 2007, the peso-dollar exchange rate was Php43.749 to US\$1.00. Using this exchange rate, our consolidated net foreign currency-denominated liabilities as at September 30, 2007 would have decreased by Php1,622 million.

The revaluation of our foreign-currency denominated assets and liabilities as a result of the appreciation or depreciation of the Philippine peso is recognized as foreign exchange gains or losses as at the balance sheet date. The extent of foreign exchange gains or losses is largely dependent on the amount of foreign currency debt and hedges we carry. While a certain percentage of our revenues are either linked to or denominated in U.S. dollars, most of our indebtedness and related interest expense, a substantial portion of our capital expenditures and a portion of our operating expenses are denominated in foreign currencies, mostly in U.S. dollars. As such, a strengthening or weakening of the Philippine peso against the U.S. dollar will decrease or increase in Philippine peso terms both the principal amount of our unhedged foreign currency-denominated debts and the related interest expense our foreign currency-denominated capital expenditures and operating expenses as well as our U.S. dollar linked and U.S. dollar denominated revenues. In addition, many of our financial ratios and other financial tests are affected by the movements in the Philippine peso to U.S. dollar exchange rate.

To manage our foreign exchange risks, stabilize cash flows, and improve investment and cash flow planning, we enter into forward foreign exchange contracts, currency swap contracts, currency option contracts and other hedging products aimed at reducing and/or managing the adverse impact of changes in foreign exchange rates on our operating results and cash flows. However, these hedges do not cover all of our exposure to foreign exchange risks. Specifically, we use forward foreign exchange contracts, currency swap contracts, foreign currency option contracts to manage the foreign exchange risks associated with our foreign currency-denominated loans. In order to manage hedge costs of these contracts, we utilize structures that include credit-linkage with PLDT as the reference entity, a combination of foreign currency option contracts, and fixed to floating coupon only swap agreements. We accounted for these instruments as either cash flow hedges, wherein changes in the fair value are recognized as cumulative translation adjustments in equity until when the hedged transaction affects the consolidated statement of income or when the hedging instrument expires, or transactions not designated as hedges, wherein changes in the fair value are recognized directly as income or expense for the period.

As at September 30, 2007, approximately 89% of our total consolidated debts was denominated in U.S. dollars. Consolidated foreign currency-denominated debt was reduced to Php56,472 million from Php81,850 million as at September 30, 2006. PLDT's outstanding long-term principal only currency swap contracts and foreign currency option contracts amounted to US\$550 million and US\$136 million, respectively, as at September 30, 2007. Consequently, the unhedged portion of consolidated debts amounts is approximately 45% or 38%, net of our U.S. dollar cash balances as at September 30, 2007.

For the nine months ended September 30, 2007, approximately 38% of our consolidated revenues are either denominated in U.S. dollars or are linked to the U.S. dollars. In this respect, the recent appreciation of the peso against the U.S. dollar reduced our revenues, and consequently, our cash flow from operations in peso terms.



The Philippine peso had appreciated by 8% against the U.S. dollar to Php44.974 to US\$1.00 as at September 30, 2007, from Php49.045 to US\$1.00 as at December 31, 2006. Likewise, as at September 30, 2006, the peso had appreciated by 5% to Php50.249 to US\$1.00 from Php53.062 to US\$1.00 as at December 31, 2005. As a result of the foreign exchange movements as well as the amount of our outstanding foreign currency debts and hedges, we recognized foreign exchange gains of Php1,662 million and Php1,601 million in the first nine months of 2007 and 2006, respectively.

**Interest Rate Risk**

On a limited basis, we enter into interest rate swap agreements in order to manage our exposure to interest rate fluctuations. We make use of hedging instruments and structures solely for reducing or managing financial risks associated with our liabilities and not for trading or speculative purposes.

The following tables set out the carrying amount, by maturity, of our financial instruments that are exposed to interest rate risk:

**Nine Months Ended September 30, 2007 (Unaudited)**

	Below 1 year	1-2 years	2	3 years	3-5 years	Over 5 years	In U.S. Dollar	Discount/ Debt		Carrying Value U.S. Dollar	Fair Value In Php
								In Php	Issuance Cost In Php (in millions)		
<b>Liabilities:</b>											
Long-term Debt											
<i>Fixed Rate</i>											
US\$ Notes (in millions)		136			250	300	686	30,847	437	30,410	34,510
Interest rate		10.500%			11.375%	8.350%					
US\$ Fixed Loans (in millions)	57	48		34	8	280	427	19,213	4,480	14,735	15,931
Interest rate	4.49% to 8.9%	4.49% to 6.66%		4.49% to 6%	4.700%	2.250%					
					85	35	120	5,420	12	5,408	5,302

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Philippine Peso (in millions)								
Interest rate	7.09%	6.500%	6.500%	5.625% to 6.125% to 6.50%	6.50%			
<i>Variable Rate</i>								
U.S. Dollar (in millions)	88	85	64	16		253 11,366	38	11,328 11,366
Interest rate	GOVCO s	0.05% to	0.05% to	0.65% to				
	Cost +	2.75% over	2.75% over	2.50% over				
	0.20%;	US\$ LIBOR	US\$ LIBOR	US\$ LIBOR				
	0.05%							
	to							
	2.75%							
	over							
	US\$							
	LIBOR							
Philippine Peso (in millions)	12	12						
Interest rate	MART1	MART1 +	MART1 +	MART1 +		53 2,368	9	2,359 2,368
	+	0.75% to	0.75% to	0.75%				
	0.75%	5.70%	5.70%					
	to							
	5.70%							
						<b>1,539 69,214</b>	<b>4,976</b>	<b>64,258 69,477</b>
<i>Interest rate swap (fixed to floating)</i>								
U.S. Dollar (US\$63 million)						5 206		206
Japanese Yen (JPY7,519 million)								5 206
Fixed Rate on	1.375%	11.375%	11.375%	11.375%	11.375%			
US\$ notional								
Variable Rate	8.11%	8.11% over	8.11% over	8.11% over	8.11%			
on JPY	over	LIBOR	LIBOR	LIBOR	over			
notional	LIBOR				LIBOR			

Year Ended December 31, 2006 (Audited)

Over 5 Discount/  
Debt



1,752,859,906      5,953      ~~79,973~~ 87,928

*Interest rate  
swap (fixed to  
floating)*

U.S. Dollar (US\$63 million)						9    423		423
Japanese Yen (JPY7,519 million)								9    423
Fixed Rate on	11.375%	11.375%	11.375%	11.375%	11.375%			
US\$ notional								
Variable Rate	8.11%	8.11% over	8.11% over	8.11% over	8.11% over			
on JPY	over	LIBOR	LIBOR	LIBOR	LIBOR			
notional	LIBOR							

Fixed rate financial instruments are subject to fair value interest rate risk while floating rate financial instruments are subject to cash flow interest rate risk.

Repricing of floating rate financial instruments is mostly done on intervals of three months or six months. Interest on fixed rate financial instruments is fixed until maturity of instrument. Financial instruments that are not subject to interest rate risk were not included in the above tables.

***Credit Risk***

We trade only with recognized and creditworthy third parties. It is our policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an on-going basis to reduce our exposure to bad debts.

With respect to credit risk arising from our financial assets, which comprise cash and cash equivalents, trade and other receivables, notes receivable and certain derivative financial instruments, our exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these financial instruments.

We have no significant concentrations of credit risk.

**25. Reclassification of Accounts**

Certain accounts in December 31, 2006 audited consolidated financial statements were reclassified to conform with the September 30, 2007 unaudited consolidated financial statements presentation.