METROPOLITAN WATERWORKS AND SEWERAGE SYSTEM
NOTES TO FINANCIAL STATEMENTS
(In Thousand Pesos)

1. Corporate Information

The Metropolitan Waterworks and Sewerage System (MWSS), a government-owned and controlled corporation, was created under Republic Act No. 6234 which was approved on June 19, 1971 replacing the National Waterworks and Sewerage Authority. Its main objective is to ensure an uninterrupted and adequate supply and distribution of potable water for domestic and other purposes to its consumers at just and equitable rates. It also aims to provide sewerage and sanitation services to the public. MWSS owns and has jurisdiction over all waterworks and sewerage system of all the cities and municipalities of Metro Manila, and some municipalities of Cavite and Bulacan.

Because of the felt need for the government to adopt urgent and effective measures and to address the nationwide water crisis which adversely affected the health and well-being of the public, legislators passed into law Republic Act No. 8041, otherwise known as the National Water Crisis Act of 1995, implemented under Executive Order No. 286 dated December 6, 1995, which reorganized the MWSS. The passage of Executive Order No. 311 on March 20, 1996 encouraged the private sector's participation in the operation of the facilities of MWSS and paved the way for its privatization.

Pursuant to a process of a competitive public bidding and selection, MWSS' operations were privatized. Thus, on February 21, 1997, MWSS entered into a Concession Agreement (CA) with two private companies (Concessionaires), namely, the Manila Water Company Incorporated (MWCI) and the Maynilad Water Services Incorporated (MWSI), granting them the rights to manage, operate, repair, decommission and refurbish the Facilities in the Service Area, including the right to bill and collect for water and sewerage services supplied in the Service Area. MWCI operates on the east zone while MWSI services the west zone The two concessionaires formally took over the operations of MWSS on August 1, 1997. In addition to the performance of the service obligations, the concessionaires are required, under the CA, to pay MWSS concession fees in consideration for such right.

As a result of the privatization in 1997, MWSS is now divided into two Offices, the MWSS-Corporate Office and the MWSS- Regulatory Office.

Due to financial difficulties, the MWSI suspended payments of concession fees to MWSS beginning on March 8, 2001. As a result, disputes between MWSS and the concessionaire ensued which brought them to a process of arbitration before the Appeals Panel appointed pursuant to the CA. On November 7, 2003, the Appeals Panel issued an award declaring that there is neither a Concessionaire Event of Termination nor an MWSS event of termination and that, consequently, the CA shall continue in force and that MWSS and the concessionaire shall perform their respective obligations under the CA until the termination of the concession. The Appeals-Panel further declared that concession fees which should have been paid by the concessionaire to MWSS were due and payable to MWSS with the corresponding interest pursuant to the CA and that MWSS may draw on the performance bond in accordance with Section 6.9 (Performance Bond) of the Concession Agreement.

On November 13, 2003, MWSI filed a petition for its corporate rehabilitation with the Rehabilitation Court, submitting therewith a rehabilitation plan as required under applicable legal requirements. A stay order was then issued by the Rehabilitation Court on November 17, 2003 prohibiting the concessionaire, among other things, from making any payment of its liabilities outstanding as at the date of the filing of the petition.

After securing a favorable decision from the Supreme Court, MWSS was able to draw on the Performance Bond in the entire amount of One Hundred Twenty Million US Dollars (US$120,000,000.00) for unpaid concession fees. On September 9, 2004, the concessionaire filed with the Rehabilitation Court a revised rehabilitation plan which was recommended for approval by the court-appointed Rehabilitation Receiver. However, the terms thereof had to be further modified in order to address the concerns raised by several creditors of the concessionaire. On April 29, 2005, the concessionaire submitted its 2005 Rehabilitation Plan incorporating therein the terms of a Debt and Capital Restructuring Agreement (DCRA) executed among the concessionaire, MWSS, Benpress Holdings Corporation, the Suez Group and the Lenders (the DCRA). The Rehabilitation Court approved the 2005 Rehabilitation Plan as well as other related documents, including the DCRA, on June 1, 2005.

Under Clause 2.6 (Increase in capital) of the DCRA, as part of the implementation of the Capital Restructuring, MWSS is given the right and obligation to subscribe to 1,238,476,000 Class “A” shares (the MWSS Subscription shares) representing 83.97% of the outstanding capital stock of the concessionaire (the MWSS Subscription Right), pursuant to Clause 2 (Capital Restructuring) of the DCRA, which subscription shall be paid for by MWSS by way of conversion into equity of the MWSS receivables converted into Philippine pesos based on assumed exchange rate of P54.63 to US$1.00. Alternatively, under Clause 24 (Substitution of the MWSS) of the DCRA, MWSS is given the right, subject to the prior approval of all the lenders and the Suez Group, to assign the MWSS Subscription Right; provided, that the assignee of MWSS shall assume all the obligations and undertakings of MWSS under the DCRA in connection with, relating to or arising from, such right, including the execution of a debt conversion and subscription agreement with the concessionaire and the provision of the Financial Assistance to the concessionaire, as required under Clause 14.1 (the Financial Assistance) of the DCRA.

Article 3(j) of the Charter authorizes MWSS, among other things, to dispose of real and personal property, including rights and franchises, consistent with the purpose for which MWSS was created and reasonably required for the transaction of the lawful business of the same. Consistent with the privatization policies of the Republic, the MWSS Board of Trustees, in its meeting dated September 8, 2005, issued Resolution No. 2005-203 authorizing MWSS to exercise its option to assign the MWSS subscription right to a private investor. Pursuant to a process of a competitive public bidding and selection, the sponsor was awarded the right to acquire the MWSS receivables and the MWSS subscription right, subject to the sponsor’s assumption of the DCRA sponsor obligations and performance of the other sponsor obligations.

0n March 2, 2009, MWCI submitted a business plan proposing to increase the investments on wastewater and new water sources project and to ensure water supply security to support their request for extension of the Concession Agreement for an additional period of fifteen (15) years, from 2022 to 2037, subject to the written consent of the Republic of the Philippines (ROP) as required under Section 16.12 of the CA. Series of public consultations were conducted to inform and educate stakeholders of the issues to warrant the extension. On April 28, 2009, per Board Resolution 2009-072, MWSS approved the extension of the concession for the East Area Concession.

Following the extension of the CA with the MWCI was the extension of the CA with the MWSI for additional fifteen (15) years. On June 24, 2009, MWSI submitted its formal proposal for 15-year extension of its Concession anchored on the following considerations:

a. Economic benefits to consumers through the mitigation of tariff increases;

b. Ability to undertake long-term water supply and sewerage projects to ensure adequate service and comply with more aggressive regulatory and environment requirements;

c. Access to longer-term financing at competitive rates to fund more long-term CAPEX projects; and

d. Ensure the long-term viability of the Concessionaire.

On September 10, 2010, Board Resolution No. 2009-180 resolved that the Concession period of the Maynilad Water Services, Inc. be renewed/extended for an additional period of fifteen (15) years, subject to the same conditions required when the MWCI was granted their extension.

SOURCES OF FUNDS

The following are the sources of funds of MWSS:

- Concession fees collected from concessionaires
- Rentals on leased properties
- Interest income on investments
- Loan availments from foreign and domestic financial institutions
- Collection of raw water and accounts receivable (accounts prior to privatization)

KEY PROJECTS FOR CY 2009 TO CY 2010

In line with the then President Gloria Macapagal Arroyo's 10- point agenda, particularly to ensure the delivery of clean and potable water to Metro Manila, MWSS continues to implement the following projects:

A. Foreign-Assisted Projects

Angat Water Utilization and Aqueduct Improvement Project (AWUAIP) - Phase 2

In order to secure the conveyance of raw water coming from the Angat Dam, the Project, denominated as Angat Water Utilization and Aqueduct Improvement Project (AWAUAIP), was conceived.

Phase 1, which involves the construction of a 5.50 km by-pass aqueduct, was completed in January 2006 and is now operational.

Phase 2, which is on-going, involves the construction of a 9.9 kilometers aqueduct extension, the rehabilitation of existing Aqueduct No. 5 and interconnection works for the six (6) aqueducts, including the clearing of informal settlers/illegal structures along the 60-meters right of way of the aqueduct alignment.

Project Location	: San Jose Del Monte, Bulacan
Project Schedule	: March 2010 – March 2013 (3 years)
Total Project Cost	: ₱6.109 Billion (as approved by NEDA – ICC)
Total Project Cost	: ₱6.089 Billion (cost after the bidding)
Amount of Loan	: ₱5.537 billion (US$116.602 Million) Export-Import Bank of China
Contract Cost with China International Water and Electric Corporation	: ₱5.298 Billion
Project Status as of Dec. 31, 2010	: The project was awarded to China International Water and Electric Corporation.

B. <u>Locally – Funded Projects</u>

1.	100 MLD Putatan Water Treatment Plant	-	₱1.20 Billion
2.	Patubig ni PGMA	-	₱437.00 Million
3.	Modernization of two (2) Passenger-Type elevators	-	₱ 6.25M
4.	Sumag River Diversion Project	-	₱ 562M
5.	Umiray-Angat Transbasin Tunnel Rehabilitation Project Phase 2	-	₱ 454M

1) 100 MLD Putatan Water Treatment Plant

This was implemented and funded by MWSI utilizing the Laguna Lake as the source of raw water. The Project was completed in December 2010 and is now operational serving the southern part of MWSI service area.

2) Patubig ni PGMA

This Project, since its start in 2004, has benefited a total of 221,391 households equivalent to about 1.517 million population in 219 areas or an 80% accomplishment as of December 2010.

3) Sumag River Diversion Project

Detailed engineering design of this Project was already completed and this was proposed to be implemented and funded by the Concessionaires under the Common Purpose Facility (CPF) framework of the Concession Agreement.

4) Umiray-Angat Transbasin Tunnel Rehabilitation Project Phase 2

Detailed engineering design of this Project was already completed and this was proposed to be implemented and funded by the Concessionaires under the Common Purpose Facility (CPF) framework of the Concession Agreement.

2. Basis of Financial Statement Preparation

The Administrator has the inherent authority to issue Financial Statements of MWSS pursuant to Section 8 (g) of Republic Act No. 6234, the MWSS Charter.

The accompanying financial statements have been prepared in conformity with generally accepted state accounting principles in the Philippines.

The financial statements of MWSS have been prepared using the historical cost basis and are presented in Philippine pesos, which is the System's functional and presentation currency. All values are rounded to the nearest thousand. The financial statements of the MWSS Corporate Office and the Regulatory Office are consolidated in this report.

3. Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year.

4. Summary of Significant Accounting Policies

Cash and cash equivalents

Cash in banks earn interest at the respective authorized government depository bank rates. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less from dates of acquisition and that are subject to an insignificant risk of changes in values. Cash equivalents are for varying periods of up to three months depending on the immediate cash requirements of the System, and earn interest at the respective investment rates. Due to the short-term nature of the transaction, the fair value of cash and cash equivalents and short-term investments approximates the amount at the time of initial recognition.

Receivables

Receivables are recognized and carried at original billed amount. Provision for doubtful accounts on water/sewer accounts receivable prior to privatization is maintained at a level considered adequate to provide for potential losses on receivables. The level of this provision or allowance is based on management's evaluation of collection experience and other factors that may affect collectability.

Property, plant and equipment

Property, plant and equipment (PPE), except those fully depreciated and those classified as administration equipment, are stated at appraised value based on the appraisal conducted in 1995 by Cuervo Appraisers, Inc., an independent appraiser hired by MWSS for that purpose, less impairment in value. Appraisal increments are recorded as appraisal capital. Additional PPE acquired after said appraisal were recorded at cost. In

2006, another appraisal was conducted by Cuervo Appraiser Inc. Appraisal increments were recorded in the books in 2007.

Depreciation of PPE commences once the properties become operational and available for use, and are calculated on a straight-line basis over the estimated useful lives of the property, plant and equipment.

Minor repairs and maintenance costs are expensed when incurred, while major repairs and/or those repairs that will prolong the useful lives of the assets are capitalized.

When property and equipment is retired or disposed of, the cost and the related accumulated depreciation, amortization and accumulated provision for impairment losses, as the case may be, are removed from the accounts and any resulting gain or loss is recognized in profit or loss.

The useful lives and the depreciation and amortization methods are reviewed periodically to ensure that they are consistent with the expected pattern of consumption of the future economic benefits embodied in the items of property, plant and equipment.

Construction in progress

Construction in progress is stated at cost. While the construction is in progress, project costs are accrued based on the contractors' accomplishment reports and billings. These represent costs incurred for technical services and capital works program contracted by the System to facilitate the implementation of the project. While the construction of the project is in progress, no provision for depreciation is recognized.

Construction in progress are transferred to the related Property, Plant and Equipment account when the construction or installation and related activities necessary to prepare the property, plant and equipment for their intended use have been completed, and the property, plant and equipment are ready for service.

Long-term foreign loans

Long-term foreign loans are recorded in peso based on the exchange rate at the time of withdrawal and are revalued at the end of each reporting date.

Impairment of financial assets

An assessment is made at each reporting date to determine whether there is any indication of impairment of assets, or whether there is any indication that an impairment loss previously recognized for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognized only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to operations in the year in which it arises.

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

A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however, not to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. In 2004, an impairment loss was recognized by MWSS for the Umiray-Angat Transbasin due to damages caused by typhoons. Since said impairment was effected in the books only in 2005, it was charged directly to Retained Earnings of that year.

Leases

A lease where the lessor retains substantially all the risk and benefits of ownership of the asset is classified as an operating lease.

Revenue recognition

All Concession fees billed/collected/received from the Concessionaires are treated as operating revenue.

Concession fees – Debt Service and Progress Billings are concession fees received from the Concessionaires that are intended for MWSS loan amortization and payments to contractors/suppliers, respectively. These are pass-on payment without any margin in favor of MWSS. Concession Fee – COB is the annual Current Operating Budget being paid by the concessionaires to MWSS for administrative expenditures subject to annual Consumer Price Index adjustment.

Foreign currency-denominated transactions

Foreign currency-denominated transactions are recorded using the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the closing exchange rate at reporting date. Foreign exchange gains and losses arising from foreign currency fluctuations are recognized in profit or loss for the period.

Subsequent events

All post year-end events up to the date the financial statements are authorized for issue that provide additional information about the System’s position at reporting date (adjusting events) are reflected in the financial statements. Any post year-end event that is material and not an adjusting event is disclosed in the notes to the financial statements.

Borrowing costs

Borrowing costs are generally expensed as incurred. Borrowing costs that are directly attributable to the acquisition, development, improvement and construction of fixed assets (including costs incurred in connection with rehabilitation works) are capitalized as part of the cost of the asset. The capitalization commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Capitalization of borrowing costs ceases when substantially all activities necessary in preparing the related assets for their intended use are complete.

Judgments and use of estimates

The preparation of the accompanying financial statements in conformity with PFRS requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The estimates and assumptions used in the accompanying financial statements are based upon management's evaluation of relevant facts and circumstances as of the date of the financial statements. Actual results could differ from such estimates.

PAS 1, *Presentation of Financial Statements*, which was adopted by the System effective January 1, 2005, requires disclosures about key sources of estimation, uncertainty and judgments management had in the process of applying accounting policies. Management believes the following represent a summary of these significant estimates and judgments:

Use of estimates

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

Estimating allowance for doubtful accounts

The System maintains allowances for doubtful accounts at a level considered adequate to provide for potential losses on receivables. The level of this allowance is based on management's evaluation of collection experience and other factors that may affect collectability. The amount and timing of recorded expenses for any period would, therefore, differ depending on the judgments and estimates made for the year.

Estimated useful lives of property, plant and equipment

The System estimates the useful lives of its property, plant and equipment based on the period over which the assets are expected to be available for use. The System reviews annually the estimated useful lives of property, plant and equipment based on factors that include asset utilization, internal technical evaluation, technological changes, environmental and anticipated use of the assets tempered by related industry benchmark information. It is possible that future results of operation could be materially affected by changes in the System's estimates brought about by changes in the factors mentioned.

Contingencies

The System is currently involved in various legal proceedings. The estimate of the probable costs for the resolution of various claims is established in consultation with the in-house lawyers and the Government Corporate Counsel handling the case.

5. Cash and cash equivalents

Cash and cash equivalents consist of the following:

	2010	2009
Cash	**1,717**	295,723
Cash equivalents	**4,383,059**	4,652,887
	4,384,776	4,948,610

6. Accounts receivable

This account consists of:

	2010	2009
Trade/Business		
Receivables from customers-water, sewer, including raw water accounts	**1,117,538**	1,118,014
Receivables from concessionaires	**555,040**	902,395
	1,672,578	2,020,409
Allowance for doubtful accounts	**1,117,002**	1,117,109
	555,576	903,300
Non-trade receivables		
Intra-agency receivables	**820,436**	324,949
Inter-agency receivables	**16,754**	16,567
Due from officers and employees	**66,276**	62,135
Loans receivables	**54,563**	48,987
Interest receivables	**2,014**	1,827
	960,043	454,465
	1,515,619	1,357,765

The receivables from customers-water, sewer, including raw water accounts represent receivables prior to the privatization of MWSS in 1997 and also current accounts.

The receivables from concessionaires represent concession fees for Current Operating Budget, Debt Service and Progress Billing outstanding as of balance sheet date.

Intra-agency receivables are receivables from the MWSS Regulatory Office consisting of electric bills, telephone bills and share in dividends paid to the National Government plus other accounts such as share in janitorial, security and other expenses.

Inter-agency receivables represent collectibles from other government agencies such as the Department of Public Works and Highways (DPWH), Office of the Government Corporate Counsel (OGCC), Supreme Court, Manila International Airport Authority (MIAA), Local Water Utilities Administration (LWUA) and the City of Manila for office rental, electric and water bills.

7. Other receivables

This account consists of the following:

	2010	2009
Receivables from MWSI	**5,225,891**	4,675,734
Receivables from MWCI	**160,005**	159,936
Others	**21,801**	30,214
	5,407,697	4,865,884

Details of the Receivables from MWSI and MWCI are as follows:

	2010	**2009**
MWSI		
Cost of borrowings	**3,797,066**	3,226,768
Penalty on delayed remittance of Concession fees	**1,118,315**	1,118,315
Inventory held in trust	**98,050**	98,050
Penalty for non-payment of borrowing costs	**95,247**	95,247
Guarantee deposits	**94,996**	94,996
Raw water	**-**	19,309
Mabuhay Vinyl	**4,994**	4,994
LMG Chemphil	**4,627**	4,627
Other receivables	**12,596**	13,428
	5,225,891	4,675,734
MWCI		
Guarantee deposits	**72,210**	72,210
Inventory held in trust	**43,747**	43,747
Penalty on delayed remittance of Concession fees	**13,182**	13,182
LMG Chemphil	**7,730**	7,730
La Vista	**591**	591
Other receivables	**22,545**	22,476
	160,005	159,936

Cost of borrowings include the principal, interest and finance charges such as bank conversions, documentary stamps, cable charges and penalties.

Inventory held in trust represents costs of inventories turned-over to the concessionaires upon commencement of the Concession Agreement. Under Sec.16.12 of the Concession Agreement, upon the expiration of the Concession, the Concessionaires shall transfer to MWSS the inventory having a value (adjusted for CPI) at least equal to the Inventory made available to the Concessionaire on the Commencement Date.

Guarantee deposits pertain to the deposits made by customers before the extension of any service connections as security for the payment of subsequent bills, or as a meter deposit.

8. Inventories

This account consists of the following:

	2010	2009
Construction materials	**60,430**	60,430
Office supplies and printed forms	**739**	647
Auto parts and supplies	**77**	82
IT supplies and accessories	**17**	96
	61,263	61,255

Construction materials represent materials available for use in the projects.

9. Prepayments

This account consists of the following:

	2010	2009
Advances to suppliers/contractors	**895,212**	366,745
Prepaid expenses	**29,261**	24,104
Deposits on letters of credit	**2,888**	3,224
	927,361	394,073

Advances to suppliers/contractors include the balance of the 15% mobilization costs paid to the contractors/suppliers/consultants of civil works/goods/consultancy services, subject to periodic recoupment.

10. Property, plant and equipment

The details of property, plant and equipment (PPE) are as follows:

	Building, Plant Equipment and Transmission Lines	Office Furniture And Other Equipment	Trans-portation Equipment	Land & Land Improve-ments	TOTAL
Cost					
January 1, 2010	61,138,831	1,247,950	592,124	12,779,936	75,758,841
Additions	81	3,704		297	4,082
Adjustments	9,230				9,230
Transfers/capitalization	314,150	1,290	27,405		342,845
December 31, 2010	61,462,292	1,252,944	619,529	12,780,233	76,114,998
Acc. Depreciation					
January 1, 2010	(33,066,701)	(807,772)	(330,192)	-	(34,204,665)
Depreciation expense	(1,465,196)	(85,791)	(46,080)		(1,597,067)
Adjustments	(133,882)	(12,939)	(29,628)		(176,449)
December 31, 2010	(34,665,779)	(906,502)	(405,900)	-	(35,978,181)
Carrying Amount December 31, 2010	**26,796,513**	**346,442**	**213,629**	**12,780,233**	**40,136,817**
Cost					
January 1, 2009	60,983,508	1,244,442	596,498	12,772,610	75,597,058
Additions		2,202			2,202
Adjustments	(228)	228	(5,685)	7,326	1,641
Transfers/Capitalization	155,551	1,078	1,311		157,940
December 31, 2009	61,138,831	1,247,950	592,124	12,779,936	75,758,841
Acc. Depreciation				-	
January 1, 2009	(31,556,894)	(709,711)	(281,044)		(32,547,649)
Depreciation expense	(1,479,830)	(96,435)	(54,520)		(1,630,785)
Adjustments	(29,977)	(1,626)	5,372		(26,231)
December 31, 2009	(33,066,701)	(807,772)	(330,192)	-	(34,204,665)
Carrying Amount December 31, 2009	28,072,130	440,178	261,932	12,779,936	41,554,176

11. Construction in progress

The movements in this account follow:

	2010	2009
Balance, beginning	**1,237,083**	1,381,793
Additions/New Project	**302,555**	13,467
Transfers/capitalization	**(342,845)**	(157,941)
Reclassification/Adjustments	**(186,288)**	(236)
Balance, end	**1,010,505**	1,237,083

12. Investments

This account consists of the following:

	2010	2009
Stocks and bonds		
NAPOCOR bonds	**457,852**	452,240
Home Guaranty Corp. bonds	**19,008**	19,008
MERALCO stocks	**2,152**	2,152
PLDT investment plan	**373**	373
	479,385	473,773
Miscellaneous		
Special reserve fund	**299,371**	284,975
Sinking fund	**29,510**	29,510
	328,881	314,485
	808,266	788,258

The NAPOCOR bonds are long-term, tax-exempt investments which will mature in December 2011 and which earn a 4% interest rate per annum.

The special reserve fund with the Bureau of Treasury, which is intended as guarantee for the financial obligations of MWSS during the concession period, was established in pursuance to Article 2.1 of the Memorandum of Agreement (MOA) between the Department of Finance (DOF) and MWSS. The original amount is P 100 million. The increase is mainly due to interest income.

13. Other assets

This account consists of the following:

	2010	2009
Unserviceable assets	**231,850**	242,797
Research and development	**157,267**	152,801
MWSS Share in Angat Dam construction	**54,897**	63,019
Car assistance plan	**-**	13,496

Garnished accounts	**11,461**	11,461
Guarantee deposits	**10,728**	10,728
Dormant accounts	**938,417**	937,566
	1,404,620	1,431,868
Allowance for dormant accounts	**(519,000)**	(519,000)
	885,620	912,868

Unserviceable assets are the costs of construction materials and supplies that can no longer be used in projects due to obsolescence or assets which are no longer operational. Management is working out on its disposal.

Dormant accounts are accounts prior to the privatization in 1997. These include balances of accounts carried over since the time of the old National Waterworks and Sewerage Administration (NAWASA).

14. Payable accounts

This account consists of:

	2010	2009
Accounts payable	**664,414**	642,903
Interest payable	**302,175**	322,159
Due to officers and employees	**120,720**	80,042
	1,087,309	1,045,104

Accounts payable includes accrued maintenance and other operating expenses and local counterpart of loans payable.

Due to officers and employees refers to unclaimed gratuity, COLA and accrued personal services.

15. Inter-agency payable

This account consists of payables to the:

	2010	2009
Bureau of Treasury	**235,091**	236,702
BIR	**1,716**	2,336
GSIS	**1,508**	1,756
Pag-IBIG	**305**	435
Other GOCCs	**507**	402
	239,127	241,631

Payable to the Bureau of Treasury pertains to the guarantee fee on existing loans.

16. Intra-agency payable

This account represents the share of the MWSS-Regulatory Office in the concession fee received from the concessionaires for their current operating budget as provided in the CA.

17. Other liability accounts

This account includes 10% retention from contractors' claims, unreturned borrowed materials, cost of flushing, attorneys' fees, guaranty deposits, depository liabilities, liabilities with existing law suits and money claims such as cost of living allowance, contract collectors early retirement pay and retirement claims of former MWSS-CO employees under RA 1616 pursuant to Supreme Court Decision GR No. 164542 dated December 18, 2007, which are released to MWSS on March 12, 2008.

18. Long-term liabilities

This account consists of domestic and foreign borrowing, as follows:

Source	**Maturity Date**	**Currency**	**Annual Interest Rate**	**2010**	2009
Domestic					
SPIAL	05-15-26	$	9.65%	**386,057**	426,104
ADB 1746-PHI	02-01-22	P	floating	**193,840**	204,754
PNB Loan	11-19-10	P	2.15%	**-**	200,000
NHA		P	floating	**98,795**	98,795
IBRD 1272/1282	07-15-20	$	8.50%	**63,380**	66,949
				742,072	996,602
Foreign					
BNP Paribas	11-26-11	$	floating	**6,582,750**	6,953,400
ADB 1379-PHI	07-15-20	$	floating	**2,747,455**	3,065,349
ADB 986-PHI	10-01-14	$	floating	**2,474,678**	2,783,212
JBIC (OECF)	02-20-20	Y	2.70%	**1,849,205**	1,740,813
IBRD 4019-PH	07-01-16	$	floating	**718,597**	870,544
China Eximbank					
AWUAIP II	01-21-30	$	libor rate	**529,899**	-
ADB 947-PHI	12-15-12	$	floating	**350,484**	472,135
ADB 1150-PHI	10-15-16	$	floating	**313,946**	330,054
French Protocol	12-31-18	FF	3%-6.8%	**133,249**	186,010
IBRD 4227 PHI	09-15-17	$	floating	**49,109**	58,996
ADB 2012-PHI	08-15-13	$	libor rate	**27,710**	37,275
				15,777,082	16,497,788
Total				**16,519,154**	17,494,390

Current Portion -		
Asian Development bank (ADB)	**916,981**	801,904
Int'l. Bank for Reconstruction & Development (IBRD)	**114,548**	117,383
French Protocol	**23,565**	27,070
Special Project Implementation Assistance Loan (SPIAL)	**11,556**	12,206
	1,066,650	958,563
Non-Current Portion	**15,452,504**	16,535,827

The *Special Project Implementation Assistance Loan* (SPIAL) is a portion of the National Government's multi-currency loans from the ADB under Loan Nos. 779 & 780. This was relent to MWSS to partly finance the following projects: Manila Water Supply Rehabilitation Project I (MWSRP I), Manila Water Supply Project II (MWSP II), and Metro Manila Sewerage Project (MMSP).

ADB Loan No. 1746 PHI is a sub-loan agreement entered into by and between the Department of Finance and the MWSS on October 13, 2003 for the implementation of the Pasig River Environmental Management and Rehabilitation Sector, a sanitation component of the loan.

NHA Loan was transferred by NHA to MWSS before the privatization that financed the transfer of water and sewer systems of Tondo Foreshore, Dagat-Dagatan and Kapitbahayan. The validity of the account is still subject to confirmation and subsequent preparation of MOA between MWSS, NHA and the two concessionaires.

IBRD Loan No. 1272/1282- Manila Urban Development Project – are likewise a national government loan relent to MWSS on October 1, 1976. Per subsidiary loan agreement dated October 1, 1976, MWSS shall repay the principal of the subsidiary loan to start on November 15, 1981.

The BNP Paribas Loan was obtained on March 26, 2004 to finance/refinance the system's maturing obligations brought about by non-payment of MWSI in its obligation and arbitration related expenses for the year 2004. Part of it was used to finance BNAQ I Project. It is a seven (7) year fixed rate note amounting to US $150Million, which will mature in 2011.

ADB Loan No. 1379 PHI was obtained on November 27, 1995. The primary objectives of the project were to divert an average annual flow of about 15.7 cubic meters per second from the Umiray river basin to the Angat reservoir and to augment the treated water supply capacity of MWSS by about nine cubic meters per second by 1999. The secondary objective of the project was to reduce Non Revenue Water (NRW) by providing support for leak detection and repair activities. It is a 20-year loan with a grace period of 5 years which will mature on July 15, 2020.

ADB Loan No. 986 PHI– Angat Water Supply Optimization Project was obtained on December 18, 1989. The objectives of the project were to maximize the capacity of the main water supply source of the MWSS and to meet projected water demand in the project area through construction of additional supply, treatment and distribution facilities. It is a 20 year loan with a grace period of 5 years which will mature in October 1, 2014.

JBIC Loan PH 110 – contracted by Japan and the national government of the Republic of the Philippines in 1990 intended for Angat Water Supply Optimization Project. The proceeds of the loan were treated by MWSS as government equity for drawdown incurred before privatization and as loan after privatization.

IBRD Loan No. 4019 PH - Manila Second Sewerage Project - was obtained on June 19, 1996. The objectives of the project were to assist the Borrower to a) reduce the pollution of Metro Manila waterways and Manila Bay; b) reduce the health hazards associated with human exposure to sewerage in Metro Manila; c) establish a gradual low-cost improvement of sewerage services in Metro Manila by expanding the Borrower's septage management program. It is a 15-year loan with a grace period of 5 years which will mature on July 1, 2016.

China Eximbank - Angat Water Utilization and Aqueduct Improvement Project Phase II (AWUAIP-II) is being financed through a loan from the Export-Import Bank of China on May 7, 2010 in the amount of US$116,602,000. The Angat Water Utilization and Aqueduct Improvement Project Phase 2 is an offshoot of the Angat Water Utilization and Aqueduct Improvement Project (AWUAIP). To be implemented by the MWSS, the AWUAIP is targeted to maintain and optimize the water conveyance from Angat Dam to the Water Treatment Plants via the Ipo Dam-Bicti-La Mesa Portal system. The project involves the rehabilitation of AQ-5, which supplies half of the raw water for Metro Manila, as well as the construction of AQ-6 in order to recover around 394 million liters of raw water lost to leakages. AWUAIP Phase 2 on the other hand involves the construction of the remaining 9.9km section of AQ-6, and the rehabilitation of AQ-5. The AQ-6 extension aims to completely recover the lost water due to leakages in AQ-5. Repayment period is 25 years on a semi annual basis starting January 21, 2015 and will mature in January 21, 2030.

ADB Loan No. 1150 PHI – Manila South Water Distribution Project – was obtained on January 23, 1992. The primary objective of the project was to improve the water supply services of MWSS in the project area. The secondary objective was to reduce the use of ground water, to prevent saline intrusion and land subsidence, as the main source of water for the remaining population not served by MWSS in the project area. It is a 20-year loan with a grace period of 5 years which will mature on October 15, 2016.

The French Protocol is a French Treasury Credit Facility from the French Republic intended to finance the implementation of the Rizal Province Water Supply Improvement Project (RPWSIP) payable within a period of 10 years that started December 2002.

IBRD 4227 PHI was part of the Water Districts Development Project funded by a loan from the World Bank-IBRD. MWSS entered into a subsidiary loan agreement with the Republic of the Philippines through the Department of Finance for a $2.3 Million from said IBRD loan. Repayment period is 15 years on a semi-annual basis starting March 15, 2003 and ending on September 15, 2017 per Schedule 3 of the Loan Agreement between the Republic of the Philippines and the International Bank for Reconstruction and Development dated May 15, 1999.

ADB Loan No. 2012 PHI – MWSS New Water Source – was obtained November 24, 2003. The objective of the project was to provide the Borrower with consulting services to a) prepare and design projects for the development of new water sources for Metro Manila and b) improve the Borrower's capacity for financial management, accounting, and fiscal control. It was a 7-year loan with a grace period of 4 years which will mature on August 15, 2013.

19. Deferred credits

This account consists of:

	2010	2009
Deferred credits to income	**1,643,280**	1,450,851
Others	**709,293**	120,403
	2,352,573	1,571,254

Deferred credits to income account represents a) annual income concession fee – corporate operating budget received in advance from concessionaires usually at the early part of the year and amortized equally over a period of twelve months to the appropriate income account, and, b) penalty for non-payment/deferment of Debt services of MWSI computed based on 364 T-bills rate which is still being disputed by the MWSI.

20. Donated Capital

This account represents the costs of waterworks facilities turned-over by private subdivisions by way of a Deed of Donation. It also includes the grant from the Japan International Cooperation Agency (JICA) for the rehabilitation of Balara Water Treatment Plant.

21. Prior-period adjustments

Details of this account are as follows:

	2010	2009
Closing of payables	**23,790**	
Collection of deferred income	**19,309**	
Capitalization of assets	**16,179**	(34,190)
Adjustment of receivables/payables	**12,954**	
Adjustment of concession fee	**3,198**	2,746
Payment of prior years' rental	**1,911**	833
Closing of dormant account	**997**	-
Collection of prior years' water accounts	**107**	20,842
Reversal of accruals	**(1,223)**	22,026
Payment of prior years' expenses	**(12,710)**	(3,816)
Adjustment on loans payable	**(44,704)**	(36,062)

Adjustment of Construction in Progress	**(162,850)**	
Dividend paid to the Bureau of Treasury	**(195,882)**	
Adjustment of Depreciation	**(208,668)**	(30,349)
Income/expense adjustments	**(221,022)**	(64,757)
	(768,614)	**(122,728)**

22. Personal services

This account is comprised of the following:

	2010	2009
Salaries and wages – regular	**61,064**	48,350
Salaries and wages – contractual	**3,194**	1,832
Additional compensation	**3,036**	3,557
PERA	**2,117**	1,186
Representation allowance	**13,124**	10,191
Transportation allowance	**2,156**	1,364
Clothing allowance	**796**	816
Subsistence, laundry & quarter allowance	**14,553**	12,103
Productivity incentive allowance	**19,533**	20,704
Year end bonus	**9,535**	8,219
Other bonuses and allowances	**41,827**	40,121
Longevity pay	**10,169**	5,596
Cash gift/13th month pay	**4,871**	4,079
Hazard pay	**1,946**	1,818
Honoraria	**6,601**	475
Life and retirement insurance contributions	**7,844**	6,208
PHILHEALTH contributions	**704**	643
ECC contributions	**268**	249
Pag-IBIG contributions	**268**	248
Terminal leave benefits	**1,157**	992
Provident fund benefits	**7,088**	3,381
Other personnel benefits	**36,614**	39,401
	248,465	211,533

The significant increase in Honoraria was due to change in the classification of the Honoraria of the Board of Trustees of MWSS from MOOE in CY 2009 to Personal Services in CY 2010.

23. Maintenance and other Operating Expenses

This account consists of the following:

	2010	2009
Extraordinary and miscellaneous expenses	**35,173**	15,737
Consultancy expenses	**28,681**	5,190
Security services	**22,326**	23,165
Survey expenses	**17,058**	-
Electricity expenses	**16,411**	14,904
Taxes, duties and licenses	**14,833**	19,041
Scholarship expenses	**10,982**	-
Training expenses	**10,919**	5,786
Insurance expenses	**6,486**	5,869
Other professional services	**5,944**	4,855
Drugs and medicines expenses	**5,055**	2,058
Auditing services	**5,038**	3,054
Janitorial services	**3,438**	3,821
Communication expense	**3,348**	3,637
Gasoline, oil and lubricants	**3,056**	2,695
Office supplies expense	**2,446**	2,011
Representation expenses	**1,403**	1,439
Repairs and maintenance	**1,347**	1,892
Rent expense	**805**	519
Advertising expenses	**723**	1,034
Other supplies expenses	**653**	742
Travelling expenses	**502**	511
Subscription expenses	**206**	90
Water expenses	**177**	106
Environmental/sanitary services	**158**	1,011
Fidelity bond premiums	**92**	106
Membership dues and contributions to org.	**34**	33
Donations	**23**	544
Printing and binding expenses	**6**	86
Postage and deliveries	**3**	1
Confidential expenses	**-**	900
Other maintenance and operating expenses	**30,936**	168,501
	228,262	289,338

24. Financial expenses

This account consists of:

	2010	2009
Interest expenses	**271,458**	358,469
Other financial charges	**50,708**	109,418
Documentary stamp expenses	**217**	226
Bank charges	**193**	772
	322,576	468,885

25. Subsequent events

The USD 150M BNP Paribas, 9.25% fixed Rate Guaranteed Notes, had matured on March 14, 2011. Amount due for payment on said date was USD 156.93M, which comprised principal of USD 150M and final semi annual interest of USD6.93M.

The MWSS, in order to fully pay the said amount, had availed loans with the Development Bank of the Philippines and the Land Bank of the Philippines under a club deal arrangement in the amount of the dollar equivalent of ₱2.25 Billion. The MWSS Board approved said availment of new domestic borrowings in Board Resolution No. 2010-084 dated 02 June 2010. The new loan is estimated to be paid within 7 years with pre-termination clause during the period.

Meanwhile, MWSS is still pursuing the disputed claims on cost of borrowings from Maynilad Water Co., Inc. relative to the BNP Paribas loan. Should MWSS be able to collect additional cost of borrowings, the said amount will be used to pay this new loan.

26. Contingent Liabilities

The System has pending court litigations concerning project contracts and land disputes totaling P29.71 million prior to its privatization in 1997. The MWSS has also disputed the real estate taxes charged by the local government of Quezon City in the amount of P264 Million. In 2010, the Quezon City government auctioned some of the properties located in the area. To prevent the inclusion of MWSS property in the auction held in December 2010, the System deposited ₱30 Million. The legal issues on the matter are elevated before the Supreme Court and subsequently a temporary restraining order (TRO) was issued on January 21, 2011 enjoining Quezon City government from proceeding with the levy of the subject properties until further orders from the court.

27. Report on the Supplementary Information Required Under Revenue Regulation No. 15-2010

In compliance with the above regulation, MWSS' taxes and withholding taxes paid and accrued during the year are categorized as follows:

Corporate income taxes:	CO	RO	TOTAL
Paid in 2010	-	-	-
To be paid in 2011	-	-	-
Total	-	-	-
Add: Taxes paid in 2010:			
On compensation	1,370,676.46	2,315,416.82	3,686,093.28
Final Withholding Tax (FWT) on Loans -			
BIR Form 2306	62,521,443.75		62,521,443.75
Real Property Taxes	1,922,732.19		1,922,732.19
Others:			
Input VAT	4,031,803.24		4,031,803.24
FWT on Government Transactions	848,861.40		848,861.40
FWT on Private & Government			
Transactions	3,442,231.97		3,442,231.97
ITW on Suppliers & Contractors	3,706,603.09	1,406,472.40	5,113,075.49
Output Vat	8,625,702.74		8,625,702.74
Total	86,470,054.84	3,721,889.22	90,191,944.06
Add: Taxes Withheld (To be paid in 2011)			
On Compensation - Per diem/salaries/OT	216,480.12	424,795.90	641,276.02
Input VAT	238,686.85		238,686.85
FWT on Government Transactions	16,728.44		16,728.44
ITW on Suppliers & Contractors	287,606.93	226,459.16	514,066.09
Output VAT	610,889.86		610,889.86
Total	1,370,392.20	651,255.06	2,021,647.26
Total taxes paid and accrued	**87,840,447.04**	**4,373,144.28**	**92,213,591.32**