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. The System is an attached agency to the Department of Public Works and Highways. 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.

On March 8, 2001, due to financial difficulties, Maynilad suspended payment of concession fees. From March 2001 to July 2001, MWSS used its own funs to meet the maturing obligations of Maynilad. Thereafter, from July 2001 to 2006, MWSS had to obtain a number of loans from various banks and financial institutions to meet its maturing obligations and expenses which the (unpaid) concession fees from Maynilad were supposed to cover.

Despite continuous negotiations, several disputes between Maynilad and MWSS led the former to issue a "Notice of Early Termination of the Concession" on December 9, 2002. On January 7, 2003, MWSS arbitration proceedings were commenced and and November 7, 2003, the Appeals Panel for Major Disputes ruled that (1) there was no MWSS or Concessionaire Event of Termination under Article 10 of the CA, (2) the parties should continue to perform their obligations under the CA until the expiration thereof, (3) MWSS may draw on the USD120M Performance Bond. The Arbitration Order became final on November 22, 2003.

During the pendency of the corporate rehabilitation proceedings, and prior to the drawing on the USD120M Performance Bond, MWSS had to seek funding from other sources to meet its maturing obligations and operating expenses. As a result, on March 16, 2004, MWSS with the Republic as Guarantor, and BNP Paribas, entered into a Subscription Agreement wherein BNP Paribas agreed to subscribe to the MWSS-BNP Notes.

On April 29, 2005, Maynilad submitted to the Rehabilitation Court its 2005 Rehabilitation Plan incorporating the terms and conditions of the Debt and Capital Restructuring Agreement (DCRA) executed between Maynilad, MWSS, Benpress Holdings Corporation, the Suez Group and other lenders. One June 1, 2005, the Rehabilitation Court approved the 2005 Rehabilitation Plan, including the DCRA.

Under Clause 2.6 of the DCRA, MWSS was given the right to subscribe to 83.97% of the shares of Maynilad. On September 8, 2005, the MWSS Board of Trustees resolved to assign the MWSS Subscription Rights pursuant to Clause 24 of the DCRA. After going through the process of competitive public bidding, DMCI-MPIC Water Company, Inc. (DWCI) was awarded the MWSS Subscription Rights and the right to acquire receivables of MWSS, subject to the conditions imposed under the DCRA. On December 27, 2006, MWSS and DWCI entered into an Assignment and Assumption Agreement (AAA) to formalize the award.

In accordance with the AAA, DWCI, decided to effect the early exit of Maynilad from rehabilitation proceeding by contributing cash to the latter and enabling the latter to prepay, among others, its obligations to MWSS under the DCRA. To implement this, DWCI entered into a Prepayment and Settlement Agreement (PSA) with Maynilad, MWSS, the Suez Group and other lenders on August 9, 2007.

Thereafter, Maynilad MWSS, the Suez Group, and other creditors of Maynilad filed a Joint Omnibus Motion dated August 14, 2007. Acting on the Joint Omnibus Motion, the Rehabilitation Court issued an order dated December 19, 2007 (1) immediately approving the PSA, (2) declaring that Maynilad had successfully implemented the 2005 Rehabilitation Plan subject to the fulfillment of certain conditions, and (3) disallowing the disputed or unresolved claims of MWSS and the Suez Group. On February 6, 2008, the Rehabilitation Court issued another order confirming the December 19, 2007 Order, declaring that the conditions in its previous order have been met, and releasing Maynilad from the corporate rehabilitation proceedings.

During the 11th year of the implementation of the Concession Agreement, the Parties, MWSS and MWCI and Maynilad (under a new Sponsor, DMCI) identified and discussed the option of renewing/extending the Concession Agreement pursuant to the following government policies:

a. To increase investments in water and wastewater improvement projects, to pursue the mandate of the government to accelerate waste water projects, to comply with the Clean Water Act and the recent Supreme Court decision for the clean up and preservation of Manila Bay, and sufficient concession fees to support the implementation of new water source projects as enumerated in the Final Business Plan;

b. To mitigate the impact on tariff increases through the renewal/extension of the Concession Agreement.

On October 19, 2009, the DOF transmitted to the MWSS, the signed letter of Consent and Undertaking in behalf of the Republic the approval of extension of the

Concession Agreement of MWCI to an additional of 15 years from 7 May 2022 to 6 May 2037

On March 17, 2010, the DOF thru the MWSS, again transmitted the signed Letter of Undertaking in behalf of the Republic another approval of 15 years extension of the Concession Agreement of the Maynilad from 6 May 2022 to 6 May 2037.

The Term Extension committed the Concessionaires to increase by 100% the concession fees (Corporate Operating Budget or COB) of the MWSS Corporate Office and the Regulatory Office.

In CY 2013 Rate Rebasing was performed which served as basis for reviewing the performance as well as to determine the new business plan that the MWCI and MWSI will undertake. The exercise will also ensure that notwithstanding the changes in the economic and operating assumptions, both concessionaires will be able to recover all its expenditures (Opex, Capex and Income Taxes), plus guaranteed rate of return. As such, the exercise will serve as one of the major drivers of tariff adjustments under the Concession Agreement (CA).

Section 9.2 of the CA provides that the Standard Rates for water and sewerage services shall be adjusted each year effective January 1 of each Charging Year. In accordance with the (i) the Rate Adjustment Limit set forth in Section 9.2.1., (ii) the adjustment principles set forth in Section 9.2.2 and (iii) the procedures set forth in Sec. 9.2.3.

Rata Adjustment Limit (RAL) is defined as the percentage, either positive or negative, equal to the sum of “C” or the percentage change in the Consumer Price Index, “E” or Extraordinary Price Adjustment and “R” or the Rate Rebasing Convergence Adjustment.

As for MWCI, on March 30, 2012, the Concessionaire filed a petition for the determination of its “R: factor for the 3rd Rate Rebasing (RR), proposing an upward adjustment of 22.79% of its average basic water charge or P5.83 per cubic meter beginning January 1, 2013.

After careful study, the MWSS Board of Trustees resolved and adopted the recommendation of the RO:

- To deny Manila Water’s petition for an upward adjustment of its average basic water charge; and
- To approve and effect a negative adjustment of 29.47% of its 2012 average basic water charge of P24.57 per cu.m. to be implemented in five equal tranches of negative 5.894% per Charging year.

MWCI objected to MWSS RR determination and commence arbitration under the 1976 United National Commission on International Trade Law Arbitration Rules, in the case entitled Manila Water Company, Inc. vs MWSS and Regulatory Office which was subsequently docketed with the International Chamber of Commerce as Case No. UNC 136/CYK.

On February 27, 2015, the RO received a copy of the Partial Award in ICC Case No. UNC136/CYK. The dispositive portion reads:

a.) Corporate Income Tax (CIT) is not allowed Expenditures under the CA;

b.) The Appropriate Discount Rate should not be computed fully pre-tax; and

c.) Each Party is to bear its own legal and other costs. The cost of the arbitration including the fees and expenses of the Appeals Panel are to be borne equally by MWSS and MWCI.

On April 21, 2015, the RO received a copy of the Final Award in ICC Case No. UNC136/CYK. The dispositive portion reads:

a.) Affirm that the parties have reached agreement on the Rate Rebasing Adjustment after taking to account the Partial Award dated 26 February 2015;

b.) Order that the Rate Rebasing Adjustment for the period 2013 to 2017 be set as a negative adjustment of 11.05% of MWCI'S 2012 average basic charge of P25.07 per cu.m. or negative P2.77 per cu.m. to be implemented in 5 equal tranches of negative 2.21% per charging year, pursuant to Article 9.4.3 (ii) of the CA; and

c.) Order that each party is to bear its own legal and other costs.

On April 30, 2015, the RO transmitted its Resolution No. 2015-0905-CA to the MWSS Board of Trustees containing the MWCI's determination of 2015 Rate Adjustment Limit as follows:

a.) To set the 2015 RAL of Manila Water at negative 2.42% to be applied on the prevailing basic charge; and

b.) To recommend the publication of the 2015 Table of Standard Rates for Manila Water pursuant to the requirement under Section 12 of the MWSS Charter that such "rates and fees shall be effective and enforceable fifteen (15) days after publication in a newspaper of general circulation.

Board Resolution No. 2015-058-RO dated May 8, 2015 resolved, approved and confirm the above recommendation. The Rate Adjustment of Manila Water will take effect June 1, 2015.

As for Maynilad, on March 30, 2012, the Concessionaire filed a petition for the determination of its "R: factor for the 4th Rebasing Period (2013-2017), proposing an upward adjustment of 24.69% of its average basic water charge or P7.41 per cubic meter beginning January 1, 2013.

On September 14, 2012, Maynilad revised their proposed rate adjustment to 34.06% of its average basic charge – or an equivalent increase of P10.31 per cu.m.

Pending the final determination of the "R", Maynilad in a letter dated November 26, 2012, sought an interim rate increase of at least 20% of P2.06 per cu.m. of the anticipated "R" based on its September 2012 Business Plan. The MWSS Board of Trustees, upon the recommendation of the RO in Resolution No. 2012-010-CA dated December 3, 2012, declined Maynilad proposed interim rate increase, but allowed the "C" factor of 3.2%.

After careful study, the MWSS Board of Trustees resolved and adopted the recommendation of the RO:

- To deny Maynilad's petition for an upward adjustment of its 2012 average basic water charge; and
- To approve and effect a negative adjustment of 4.82% of its 2012 average basic water charge of P30.28 per cu.m. to be implemented in five equal tranches of negative 0.964% per Charging year; and
- Discontinuance of the CERA.

Maynilad objected to MWSS RR determination and commence arbitration under the 1976 United National Commission on International Trade Law Arbitration Rules, in the case entitled Maynilad Water Services, Inc. vs MWSS and Regulatory Office which was subsequently docketed with the International Chamber of Commerce as Case No. UNC 141/CYK.

Maynilad argued that the RO erred in the Rate Rebasing Determination and enumerated the following grounds for its objection to and disagreement with the same:

1. Unauthorized disallowance of corporate income tax;
2. Incorrect estimate of the ADR for Future Cash Flows (FCF);
3. Unauthorized adjustments to the Opening Cash Position (OCP) set during the last Rate Rebasing;
4. Improper addition of Guaranty Deposits to Maynilad's historical and future receipts; unreasonable and improper disallowances in other expenditures in the OCP; and
5. Unreasonable and improper adjustment to other expenditures in the FCF.

On December 29, 2014, the Appeals Panel in the Maynilad dispute promulgated its Final Award as follows:

1. By majority, finds that the Maynilad is entitled to include its Corporate Income Tax (CIT) in its Future Cash Flows for each year of operation;
2. By majority, upholds Claimant's alternative Rebasing Adjustment for the 4th Rate Rebasing Period of 13.41%, which means an average basic waer charge of P30.28 per cu.m. resulting in an adjusted rate of P34.34 per cu.m for every charging year of the 4th Rate Rebasing Period;
3. Unanimously decides that each Party shall bear its own legal costs and that the costs of the arbitration shall be borne by the Parties equally;
4. Unanimously orders Respondents to reimburse to Claimant the sums of USD15,012.50, Php540,502.81 and HKD179.73, representing Respondents' share of the costs of the arbitration that were advanced by the Claimant' and
5. Dismiss all other claims.

Finding the conclusion reached by the Appeals Panel in the Maynilad Dispute as **directly in contrast** to the conclusions reached in the MWCI Dispute, the MWSS Board of Trustees after thorough deliberation of the RO and Maynilad, granted the request of Maynilad on certain terms in the implementation of the Rate Adjustment as follows:

1. Consistent with the RO Resolution No. 2012-010-CA dated December 3, 2012 and MWSS Board Resolution No. 2012-165 dated December 7, 2012, Maynilad shall receive the "C" factor of the RAL pending the final resolution of the "R";
2. Consistent with RO Resolution No. 13-008-CA dated September 6, 2013 and MWSS Board Resolution No. 2013-100-RO dated 2013-100-RO dated September 12, 2013, Maynilad shall no longer collect CERA;
3. Consistent with RO Resolution No. 2015-004-CA dated March 25, 2015 and MWSS Board Resolution No. 2015-039-RO dated March 31, 2015, Maynilad will not charge the CIT component of its alternative "R: pending a more definite ruling by a court of justice on the CIT issue; and
4. Consistent with RO Resolution No. 2014-002-CA dated December 17,02014 and MWSS Board Resolution No. 2013-129-RO dated December 12, 2014, which restored the FCDA adjustments, the proposal will bring regularity to the rate adjustment mechanism under the CA.

On May 14, 2015, MWSS Board Resolution No. 2015-060-RO resolved, approved and confirmed the resolutions of the RO as follows:

a.) To set the 2015 RAL for Maynilad at 7.52% t be applied on the prevailing basic charge;

b.) To implement the discontinuance of the charging the CERA; and

c.) To recommend the publication of the 2015 Table of Standard Rates for Maynilad pursuant to the requirement under Section 12 of the MWSS Charter that such "rates and fees shall be effective and enforceable fifteen (15) days after publication in a newspaper of general circulation."

The Rate Adjustment of Maynilad will take effect June 1, 2015.

Meanwhile, the issue on the CIT now elevated to the Supreme Court is an urgent and real issue for the SC to decide. Early resolve for the issue at hand was manifested.

SOURCES OF FUNDS

The following are the sources of funds of MWSS:

- Concession fees collected
- Rentals on leased properties
- Interest income on investments
- Loan availments from foreign and domestic financial institutions
- Collection of raw water and accounts receivable
- Other incidental revenues

STRATEGIC INITIATIVES AND WATER SECURITY LEGACY BUBBLE

Water Security Legacy (WSL) Roadmap – MWSS is driven by the Water Security Legacy Roadmap and is composed of seven legacies to help ensure a more holistic, long-term and sustainable approach to water service for Metro Manila and its outskirts. These legacies are:

a) Legacy 1 – Water Resources and Infrastructure Management, Development and Protection

b) Legacy 2 – Water Distribution Efficiency

c) Legacy 3 – Sewerage and Sanitation Compliance

d) Legacy 4 – Water Rates Reviews and Rationalization

e) Legacy 5 – Organization Excellence

f) Legacy 6 – Partnership Development

g) Legacy 7 – Communication and Knowledge Management

Strategic Initiatives – MWSS – CO hereby commits to undertaking the following key programs and/or projects identified as having a significant impact on its Performance Scorecard:

a) Strategic Initiative 1 – New Centennial Water Supply Source Project (NCWSP) - Kaliwa Dam Project (P18.72 billion)

- Fund Source : Private Proponent under PPP scheme
- involves the financing, design and construction of a raw water supply source with a capacity of 600 MLD, through the commissioning of the Kaliwa Dam, including intake facilities and other pertinent facilities

- part of the Project is a water conveyance tunnel intended to supply 2,400 MLD of raw water for Metro Manila, thereby reducing heavy dependence on the Angat Dam reservoir.

- Status: There is an on-going coordination with DPWH relative to the signing of MOA for the joint implementation of the Project; Bidding documents were already completed but still to be approved by the Joint Special Bids and Awards Committee (JSBAC) and the new MWSS Board (still to be appointed by the President); On-going coordination with the other LGUs relative to their endorsements of the Project, including with the NCIP and PAMB for the required clearance. Indicative Timeline: Date of construction – October 2017 while Target completion Date is October 2022.

b) *Strategic Initiative 2 – Bulacan Bulk Water Supply Project (BBWSP) (P16.32 billion)*

- Funding Source : Private Proponent under PPP scheme

- Aims to provide clean and affordable treated water, will be implemented in three stages, covering 24 water service providers (WSPs) serving 21 municipalities and three cities in Bulacan.

- Will involve the development of surface water source facilities and new groundwater sources; provision of water treatment facilities and lift and booster pump stations; and the installation of new conveyance/transmission lines, among others.

- Status: Detailed Engineering Design (DED) completed; Financial Close completed; Construction of Water Treatment Plant is on-going (5% physical accomplishment); Shortlisting of consultants for construction supervision was already completed (awaiting approval from the new MWSS Board, which are still to be appointed by the President). Indicative Timeline: Date of Start for Stage 1 is September 2016 while for Stage 2 is September 2017; Target Completion date for Stage 1 is March 2018 while for Stage 2 is September 2018.

c) *Strategic Initiative 3 – Angat Water Transmission Improvement Project (AWTIP) (US$133.98M)*

- Funding Source: Loan and GOP counterpart funded by Concession Fees

- Aims to improve the reliability and security of the Angat raw water transmission system through the rehabilitation of existing conveyance and appurtenances from Ipo Dam to the La Mesa Treatment Plant.

- Involves the construction of an additional tunnel, which will allow the alternate closing of older tunnels and aqueducts in the conveyance system. This will enable the conduct of necessary inspection and rehabilitation of portions of the systems without interrupting the transmission of water.

- Status: Detailed Engineering Design (DED) completed; On-going mobilization and preparatory works for construction; Procurement of consultants for the review of DED and construction management is ongoing; Issuance of Request for Proposal (RFP) documents for the six (6) shortlisted bidders is still pending due to the absence of approving authority (the MWSS Board); Latest Indicative timeline: Date of start is May 2016 and target completion date is September 2020.

d) *Strategic Initiative 4 - Angat Dam and Dykes Strengthening Project (ADDSP)*

- National Government released P553M on April 2015
- Involves the strengthening of the dam/dyke & auxiliary spillway, installation of flood forecasting and warning system on dam operation and flood protection works to ensure structural integrity of the dam and dyke and to increase dam storage capacity.
- Aims to mitigate risks as a result of the dam being on the West Valley Fault. It will include the installation of flow forecasting and warning systems beneficial to downstream towns and cities.
- Status: Instead of MWSS, the strengthening works of the dam and dyke is being implemented and funded by Angat Hydropower Corporation (AHC), the new Owner/Operator of the Angat HydroElectric Power Plant (AHEPP), pursuant to their contract obligation to undertake mandatory rehabilitation of Angat Dam. However, contract package 2 (dam instrumentation) & contract package 4 (flood protection works) of ADDSP in the total cost of P553.30 Million remains to be the responsibility of the government, thus MWSS, as allowed by the DBM and NEDA, transferred the funds directly to the agency mandated to implement contract packages 2 & 4, which are the National Power Corporation (NPC) and the Provincial Government of Bulacan (PGB), respectively. Corresponding MOAs were executed for the subject transfer of funds and its implementation. a) Strengthening works: construction works is on-going being undertaken by Hanjin, the contractor engaged by AHC. b) Dam Instrumentation: Six (6) out of seven (7) contract packages were already awarded and are now on-going. Contract Package #7 is still under bidding stage with on-going post classification. c) Flood protection works: construction works is on-going wherein 3 out of 10 contract packages were already completed.
- Indicative Timeline: Started construction in 3rd Quarter of 2016 and completion date is 2nd Quarter of 2018.

e) *Strategic Initiative 5 - Rehabilitation, Operation and Maintenance of MWSS-owned Auxiliary turbines 4 and 5 of the Angat Hydro-Electric Power Plant (AHEPP)*

- Funding Source: Private Proponent under PPP Scheme
- The Project involves the opportunity to optimize the benefit from the MWSS-owned auxiliary turbines 4 & 5 by developing the hydropower generation component, a “by-product” of water releases.
- Status: Due to the failure of the first bidding and the issue of sharing of facilities with Angat Hydropower Corporation (AHC), the new owner/operator of the Angat Hydro-electric Power Plant (AHEPP), the MWSS sought NEDA Board’s approval to negotiate directly with AHC and an exemption from the 2013 NEDA Joint Venture Guidelines; the NEDA in its letter to MWSS date 28 July 2016 responded that they cannot grant the exemption of the Project from the required competitive challenge under the 2013 JV Guidelines. In addition, NEDA informed that MWSS may seek an opinion from the OGCC on whether a negotiated JV may be pursued for the Project under the 2013 JV Guidelines; Hence, MWSS wrote OGCC on 21 Sept 2016 in compliance with NEDA’s advice/comments. The OGCC responded in its Opinion No. 165 dated 24 October 2016 that MWSS may pursue a negotiated Joint Venture under the 2013 JV Guidelines and should observe the procedure

for negotiated JV and must comply with the documentary requirements required by the 2013 JV Guidelines; Awaiting guidance from the new MWSS Board (still to be appointed by the President).

f) *Strategic Initiative 6 – Sumag Diversion Project*

- Funding Source: Concessionaire' Fund through the Common Purpose Facility (CPF)
- Aims to provide additional raw water (188 MLD) from Sumag River in Gen Nakar, Quezon which will be diverted to Umiray Tunnel to augment water supply in Angat Dam.
- The proposed project involves the construction of appurtence structures of Tyrolean Type Weir, Intake, Desilting Basis with Sluice Way, Transition Channel, Cut and Cover, Tunnel (600 linear meters with 2.70 meters diameter), Open Channel and Intrasite Access connecting to the UATP.
- Status: The construction works is still suspended upon the Order of LGU Quezon due to the incident last 13 August 2016 that resulted to the death of six (6) persons. The CPF is still to comply with the LGU requirements prior to resumption of works.; Proposed time Extension No. 2 is in process; 67.79% physical accomplishment as of 31 July 2016.

g) Rehabilitation of Umiray Facilities

- Funding Source: Concessionaire Fund' through the Common Purpose Facility (CPF)
- Rehabilitation and strengthening of existing tunnel structures/facilities to withstand future typhoons in order to ensure the continuous flow of raw water from the Umiray River to the Angat Reservoir.
- Status: The construction works is also suspended due to the incident in the Sumag Project. The CPF is still to comply with the same LGU requirements prior to resumption of works; 37.87% physical accomplishment as of 31 July 2016.

h) Acquisition of 7.5 cms from NIA

- In the collective desire of both MWSS and NIA to properly manage the water supply from the Angat Reservoir, the Parties agreed to settle pending issued regarding water allocation and use of water from the Angat Reservoir which includes, NIA's claim for compensation for (i) opportunity losses due to reallocation of water supply from 2000 to 2010 as set out in NIA's letter dated June 14, 2011; and (ii) the reduction of NIA's water rights allocation from 15 cms to 7.5 cms.
- In the process, the MWSS agreed to deliver to NIA the amount of P52M Financial Assistance as and by way of final settlement of NIA's claim for compensation for NIA's Opportunity Losses.
- MWSS shall also deliver to NIA the amount of P1B (Compensation) to be sourced from MWSS' Concessionaires the same being part of 2013 Approved Business Plans of the Concessionaires, as and by way of full and final settlement of NIA's claim for Compensation for the 7.5 cs out of the 15 cms granted to MWSS as Additional allocation under NWRB Resolution and MWSS Water Permit.
- Status: MOA between MWSS and NIA was signed on 11 May 2015; Joint Petition letter of MWSS and NIA to NWRB requesting the latter to

effect the corresponding amendments to NIA and MWSS' water permits forwarded to NWRB on 12 May 2015; The Project has already been awarded and started in November 2016.

i) Strategic Initiative 5 – MWSS Reorganization

MWSS Corporate Office has an approved Reorganization based on GCG MC 2013-17.

j) Strategic Initiative 6 – Customer Satisfaction Survey

The ultimate customers of both MWSS and Concessionaires are the general public to whom it serves potable water and sewerage and sanitation services in its service area. This is a system for obtaining feedback from our direct customers. The UP-CIDS did the study in 2016 and final report is for presentation to the new Board this March 2017.

Board Resolution No. ______ dated _______ authorized the issuance of the Financial Statements of MWSS pursuant to Section 8 (g) of Republic Act No. 6234, the MWSS Charter.

2. Basis of Financial Statement Preparation

The accompanying financial statements have been prepared in accordance with applicable Philippine Accounting Standards as aligned with the International Financial Reporting Standards 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.

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3. Changes in Accounting Policies

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

Since 2005 the system is already adopting the International Financial Reporting Standards (IFRS) . These accounting standards are as follows:

- PAS 1, *Presentation of Financial Statements*, (a) provides a framework within which an entity assesses how to present fairly the effects of transactions and other events; (b) provides the base criteria for classifying liabilities as current or non-current; (c) prohibits the presentation of income from operating activities and extraordinary items in the statement of income; and (d) specifies the disclosures about key sources of estimation, uncertainty and judgments management has made in the process of applying the company's policies.

- PAS 2, *Inventories,* reduces the alternatives for measurement of inventories by disallowing the use of the last in, first out formula. Moreover, the revised accounting standards does not permit foreign exchange differences arising directly on the recent acquisition of inventories invoiced in foreign currency to be included in the cost of purchase of inventories.

- PAS 7, *Statement of Cash Flows,* provides information about the cash flows of an entity which is useful in providing users of financial statements with basis to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilize those cash flows.

- PAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, (a) removes the concept of the fundamental error and the allowed alternative to retrospective application of voluntary changes in accounting policies and retrospective restatement to correct prior period errors; (b) updates the previous hierarchy of guidance to which management refers and whose applicability it considers when selecting accounting policies in the absence of standards and interpretations that specifically apply; (c) defines materials omission or misstatements; and (d) describes how to apply the concept of materiality when applying accounting policies and correcting errors.

- PAS 10*. Events after the Balance Sheet Date,* provides a limited clarification of the accounting for dividends declared after the balance sheet date.

- PAS 16, *Property, Plant and Equipment*, (a) provides additional guidance and clarification on recognition and measurement of items of property, plant and equipment (b) requires the capitalization of the costs of asset dismantling, removal or restoration as a result of either acquiring or having used the asset for purposes other than to produce inventories during the period; and (c) requires measurement of an item of property , plant and equipment acquired in exchange for a non-monetary asset or a combination of monetary and non-monetary assets at fair value, unless the exchange transaction lacks commercial substance. Under the previous version of the standard, an entity measured such an acquired asset at fair value unless the exchanged assets were similar.

- PAS 17, *Leases,* prescribes for lessees and lessors, the appropriate accounting policies and disclosures to apply in relation to leases.

- PAS 18, Revenue, prescribes the accounting treatment of revenue arising from certain types of transaction and events. The primary issue in accounting for revenue is determining when to recognize revenue.

- PAS 19, Employee Benefits, prescribes the accounting and disclosure for employee benefits. It requires an entity to recognize: (a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and (b) an expenses when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

- PAS 21, *The Effects of Changes in Foreign Exchange Rates* eliminates the deferral/capitalization of foreign exchange differentials. The adoption of the standard resulted in the recognition of gain or loss on foreign exchange transactions.

- PAS 23 (Revised), *Borrowing Costs,* prescribes that borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asses shall form part of the cost of that asset. Other borrowing costs are recognized as an expense. The main change is the removal of the option of immediately recognizing as an expense borrowing costs that are directly attributable to the acquisition, construction or productivity of a qualifying asset. A qualifying asset is one that takes a substantial period of time to get ready for use or sale. An entity is therefore required to capitalize such borrowing costs as part of the cost of the asset. The standard does not require the capitalization of borrowing costs relating to assets measured at fair value, and inventories, even if they take a substantial period to time to get ready for use or sale. The standard applies to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after January 1, 2009.

- PAS 36, *Impairment of Asset*, establishes frequency of impairment testing for certain intangibles and provides additional guidance on the measurement of an asset's value in use.

- PAS 37, Provisions, Contingent Liabilities and Contingent Assets, ensures that appropriate recognition criteria and measurements bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the note to enable users to understand their nature timing and amount.

- PAS 38, *Intangible Assets* outlines the accounting requirements for intangible assets, which are non-monetary assets which are without physical substance and identifiable (either being separable or arising from contractual or other legal rights). Intangible assets meeting the relevant recognition criteria are initially measured at cost, subsequently measured at cost or using the revaluation model, and amortized on a systematic basis over their useful lives (unless the asset has an indefinite useful life, in which case it is not amortized). If recognition criteria of these intangible item does not meet both the definition of and the criteria for recognition as an intangible asset, PAS 38 requires the expenditure on this items to be recognized as an expenses when it is incurred.

- PAS 40, Investment Property applies to the accounting for property (land and/or buildings) held to earn rentals or for capital appreciation (or both). Investment properties are initially measured at cost and, with some exceptions. May be subsequently measured using a cost model or fair value model, with changes in the fair value under the fair value model being recognized in profit or loss.

- FRS 30, *Heritage Assets*, applies to all heritage assets that are held and maintained by an entity principally for their contribution to knowledge and culture. Heritage assets can be historical, artistic, scientific, geophysical or environmental qualities. The FRS sets our new disclosure requirements for the reporting of heritage assets, which apply whether or not they are reported in the balance sheet.

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4. Summary of Significant Accounting Policies

Cash and Cash Equivalents

Cash in bank earns interest at the respective authorized government depository bank rates. Cash equivalents are short term, high 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 period 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 investment 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) were either Retained Assets which are those assets that are retained by MWSS at the start of the Concession, Allocated Assets which are those assets assigned to the two Concessionaires, the MWSI and MWCI, and the Common Purpose Facility (CPF) assets.

Property, plant and equipment (PPE) are stated at cost.

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 are 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.

An oil painting by H.R. Ocampo "Abstract in Red and Black" and the water color painting "Rooster" by Kiukok, both declared National Artists of the Philippines are listed in the PPE. These have yet to be registered in the Philippine Registry of Cultural Property of the National Museum per IRR of RA 10066 otherwise known as The Cultural Heritage Act of 2009.

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 is 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.

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

Contingent Liabilities are not recognized in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the financial statements but are disclosed when an inflow of economic benefits is probable. Contingent assets are not recognized unless virtually certain.

5. Cash and cash equivalents

Particulars	**2016**	2015 As Restated
Cash on Hand	**426,209**	459,878
Cash in Bank – Local Currency, Current Account	**62,887,832**	330,093,514
Cash in Bank – Local Currency, Savings Account	**5,435,151**	8,088,008
Cash in Bank – Local Currency, Time Deposits	**3,266,756,620**	2,647,259,811
Cash in Bank – Foreign Currency, Savings Accounts	**54,410**	381,227
Cash in Bank – Foreign Currency, Time Deposits	**17,985,237**	16,690,582
Total Cash & Cash Equivalent	**3,353,545,459**	3,002,973,020

a. Cash on Hand - This consist of the amount of collection with the Cash Collecting Officers, amount of cash advances granted to designated Regular/Special Disbursing Officers for payment of authorized official expenditures subject to liquidation and cash granted to Petty Cash Custodians for payment of authorized petty and miscellaneous expenses which cannot be conveniently paid thru check.

b. Cash in Bank - Local Currency, Current Account - This consist of cash in local currency deposited in current account with the Land Bank of the Philippines (LBP) and Philippine National Bank (PNB) which earn interest at respective bank deposit rates.

c. Cash in Bank - Local Currency, Savings Account - This consist of cash in local currency deposited in savings account with the Development Bank of the Philippines (DBP), LBP and PNB which earn interest at respective bank deposit rates.

d. Cash in Bank – Local Currency, Time Deposits - This consist of placements in local currency time deposits with DBP and LBP are made for varying period.

e. Cash in Bank – Foreign Currency, Savings Account - This represents balances of cash in foreign currency, deposited in savings account with the Bureau of Treasury and LBP.

f. Cash in Bank – Foreign Currency, Time Deposit - This consist of placements in foreign currency time deposit with LBP.

6. Accounts receivables, net

This account consists of:

	2016	2015 As Restated
Trade/business		
Receivables from customers-water, sewer, including raw water accounts	**1,125,313,278**	1,123,527,307
Receivables from concessionaires	**424,699,591**	502,509,315
	1,550,012,869	1,626,036,622
Allowance for doubtful accounts	**(1,117,001,777)**	(1,117,001,777)
	433,011,092	509,034,845
Non-trade receivables		
Intra-agency receivables	**961,524**	142,555,779
Inter-agency receivables	**14,051,876**	15,820,373
Due from officers and employees	**33,916,125**	36,625,670
Loans receivables	**48,921,201**	49,933,867
Interest receivables	**5,548,708**	3,943,304
	103,399,434	248,878,993
Unreconciled Balances	**21,625,745**	21,625,745
	558,036,271	779,539,583

The *Receivables from customers-water, sewer, including raw water* accounts represent the balance of accounts receivables prior to the privatization of MWSS in the amount of P1.117B, the collection of which is highly improbable. Thus, Management set-up the provision for bad debts account for the same amount. Meanwhile, Management is presently considering the process of writing-off the account in accordance with the required procedures , such as the congressional approval.

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

Intra-agency receivables are receivables from the MWSS Regulatory Office consisting of electric bills and share in trainings and seminar 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. Some of these accounts are classified as dormant. The Management created a task force to work out on all inactive and dormant accounts to be written –off in the books of account.

7. Other receivables

This account consists of the following:

	2016	2015 As Restated
Receivables from MWSI	**5,443,545,619**	5,470,092,547
Receivables from MWCI	**165,653,986**	190,913,381
Others	**13,434,561**	13,886,192
Unreconciled Balances	**1,108,354**	1,108,354
	5,623,742,520	5,676,000,474

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

	2016	2015 As Restated
MWSI		
Cost of borrowings	**3,952,833,428**	3,952,833,428
Penalty on delayed remittance of Concession fees	**1,118,315,274**	1,118,315,274
Inventory held in trust	**158,479,798**	158,479,798
Penalty for non-payment of borrowing costs	**95,246,566**	95,246,566
Guarantee deposits	**94,996,518**	94,996,518
Mabuhay Vinyl	**4,993,546**	4,993,546
LMG Chemphil	**4,627,025**	4,627,025
Other receivables	**14,053,464**	40,600,392
	5,443,545,619	5,470,092,547
MWCI		
Guarantee deposits	**65,583,130**	65,583,130
Inventory held in trust	**82,438,411**	82,438,411
LMG Chemphil	**7,730,290**	7,730,290
La Vista	**591,347**	591,347
Other receivables	**9,310,808**	34,570,203
	165,653,986	190,913,381

Cost of borrowings include the principal, interest and finance charges such as bank conversions, documentary stamps, cable charges and penalties. 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 the loan with LBP/DBP Bonds Facility.

Penalty on delayed remittance of Concession fee is disputed by MWSI. On December 19, 2007, the Rehabilitation Court issued an order, Special Proceeding No. Q-03-071 disallowing the penalty and the Order was confirmed on February 6, 2008. MWSS has requested the Commission on Audit in a letter dated February 13, 2012 requesting approval for the dropping out of the subject account from the books based on the order of the rehabilitation court.

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 are customer deposit prior to the privatization of MWSS. The amounts were withheld by the two concessionaires from the collection of accounts receivable from water and sewer services of MWSS on the onset of the privatization where the two concessionaires were authorized to collect. Management and the two concessionaires went into reconciliation to arrive at the amount of guarantee deposit to be refunded to MWSS, where MWCI refunded the amount of P6.6M in 2011. The said amount is being contested by MWSS. The amount to be refunded by MWSI was also established, however to date, MWSI has not remitted the due amount from them.

The decrease in Other Receivables for both MWCI and MWSI was due to the disbursement of National Irrigation Administration's (NIA) compensation billing for opportunity losses charged to both concessionaires.

8. Prepayments

This account consists of the following:

	2016	2015 As Restated
Advances to suppliers/contractors	**778,929,154**	284,369,896
Prepaid Expenses	**20,140,192**	16,271,375
Unreconciled balances	**96,513,124**	96,513,125
	895,582,470	397,154,396

Advances to suppliers/contractors include the balance of the 15 percent mobilization costs paid to the contractors/suppliers/consultants of civil works/goods/consultancy services, subject to periodic recoupment during the billing period and project implementation.

9. Property, plant and equipment, net

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

	Building, Plat Equipment and Transmission Lines	Office Furniture and Other Equipment	Transportation Equipment	Land & land Improvements	TOTAL
Cost					
January 1, 2016	**67,530,445,445**	**1,183,809,902**	**582,780,005**	**27,920,312,354**	**97,217,347,706**
Additions	**9,725,655**	**7,064,274**	**-**	**-**	**16,789,929**
Reclass/Transfers	**(73,430,208)**	**(9,687,946)**	**-**	**73,430,208**	**(9,687,946)**
Adjustments		**(8,860,065)**	**-**	**(8,020,715,102)**	**(8,029,575,167)**
Disposal			**(2,732,711)**		**(2,732,711)**
December 31, 2016	**67,466,740,892**	**1,172,326,165**	**580,047,294**	**19,973,027,460**	**89,192,141,811**
Acc. Depreciation					
January 1, 2016	**41,421,853,917**	**1,034,965,553**	**459,053,374**	**-**	**42,915,872,844**
Depreciation Expense	**1,098,640,516**	**3,479,880**	**16,609,676**	**-**	**1,118,730,072**
Adjustments		**(7,974,058)**			**(7,974,058)**
Reclassification/Transfers	**(65,729,533)**	**(8,719,151)**			**(74,448,684)**
Disposal			**(2,459,440)**		**(2,459,440)**
December 31, 2016	**42,454,764,900**	**1,021,752,224**	**473,203,610**	**-**	**43,949,720,734**
Carrying Amount December 31, 2016	**25,011,975,992**	**150,573,941**	**106,843,684**	**19,973,027,460**	**45,242,421,077**
Cost					
January 1, 2015	67,504,541,051	806,054,543	516,976,772	19,226,484,650	88,054,057,016
Additions		1,667,310	600,000	794,230	3,061,540
Adjustments	2,212,502	25,295,124	18,273,683	682,637,772	728,419,081
Transfers/Capitalization		(1,854,801)	(1,735,694)	8,020,715,102	8,017,124,607
	67,506,753,553	831,162,176	534,114,761	27,930,631,754	96,802,662,244
Add: Unreconciled balances	23,691,892	352,647,726	48,665,244	(10,319,400)	414,685,462
	67,530,445,445	1,183,809,902	582,780,005	27,920,312,354	97,217,347,706
Accum. Depreciation					
January 1, 2015	40,211,604,417	689,209,472	377,405,218		41,278,219,107
Additions	1,186,714,295	4,650,153	23,143,050		1,214,507,498
Adjustments	2,212,502	22,823,232	15,476,958		40,512,692
	41,400,531,214	716,682,857	416,025,226		42,533,239,297
Add: Unreconciled balances	21,322,703	318,282,696	43,028,148		382,633,547
	41,421,853,917	1,034,965,553	459,053,374		42,915,872,844
Carrying Amount December 31, 2015	**26,108,591,528**	**148,844,349**	**123,726,631**	**27,920,312,354**	**54,301,474,862**

10. Construction in-progress

The movements in this account follow:

	2016	2015 As Restated
Balance, beginning	**160,218,665**	157,496,267
Additions/New Project	**63,477,629**	3,681,544
Transfers/capitalization/Reclassification	**(3,681,544)**	(959,146)
Unreconciled balances	**457,018,739**	457,018,739
Balance, end	**677,033,489**	617,237,404

The increase in *Construction in Progress* was due to the implementation of Angat Water Transmission Improvement Project (AWTIP) that involves the design and construction of new tunnel (Tunnel No. 4) along MWSS' existing tunnel No. 1 from Ipo to bigte in Norzagaray, Bulacan. The decrease in reclassification was due to variation order of Sewerage Treatment Plant – 01 (STP-01) recorded as Construction in Progress in CY 2015 instead of Trust Liabilities.

11. Investments

This account consists of the following:

	2016	2015
Held to maturity/Special reserve fund	**399,353,478**	379,538,835
Stocks and bonds		
MERALCO stocks	**2,151,518**	2,151,518
PLDT investment plan	**372,650**	372,650
	2,524,168	2,524,168
	401,877,646	382,063,003

Held to maturity/special reserve funds are investments in Fixed Rate Treasury Bonds with varying yield to maturity/interest rates and coupon rates, which will mature from CY 2016 to 2037 with settlement amount ranging from P100,000 to P29,430,649.50.

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.

12. Other assets, net

This account consists of the following:

	2016	2015 As Restated
Unserviceable assets	**716,699,364**	715,156,452
Research and development	**6,212,055**	6,212,055
MWSS Share in Angat Dam construction	**6,161,066**	14,283,669
Garnished accounts	**10,613,512**	10,613,512
Guarantee deposits	10,728,425	10,728,425
Dormant accounts	**688,359,479**	688,359,479
Unreconciled balances	**(19,575,783)**	(19,575,783)
	1,419,198,118	1,425,777,809

Unserviceable assets are the costs of land, construction materials and supplies that can no longer be used in projects due to obsolescence or assets which are no longer operational. The decrease in MWSS Share in Angat Dam construction schedule was due to amortization for the year which will fully be amortized in September 2017.

13. Payable accounts

This account consists of:

	2016	2015 As Restated
Accounts payable	**39,992,334**	50,546,098
Interest payable	**183,185,438**	111,479,076
Dividends Payable	**212,089,381**	362,089,381
Due to officers and employees	**14,333,812**	5,913,933
Unreconciled balances	**533,802,867**	533,802,867
	983,403,832	1,063,831,355

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

Due to officers and employees refer to accrued personal services to be paid the following year.

Dividends payable is the balance of amount due for CY 2015 which is equivalent to 50% of annual net income in accordance with RA 7656.

14. Inter-agency payables

This account consists of payables to the:

	2016	2015 As Restated
Bureau of Treasury	**146,720,492**	125,315,531
Bureau of Internal Revenue	**1,882,111**	4,237,128
GSIS	**1,129,469**	1,212,790
Pag-IBIG	**92,285**	85,044
Other GOCCs	**74,446**	77,254
	149,898,803	130,927,747

Payable to the Bureau of Treasury pertains to the guarantee fee on existing loans. Other GOCCs include Philhealth and National Home Mortgage and Financing Corporation.

15. Intra-agency payable

This account represents electricity and share in training and seminar expenses of the MWSS-Regulatory Office payable to the Corporate Office.

16. Other liability accounts

This account consists of the following:	**2016**	2015 As Restated
Guaranty Deposits Payable	**99,252**	98,252
Performance/Bidders/Bail Bonds Payable	**1,781,213**	2,513,813
Trust Liabilities	**101,310,718**	595,203,422
Other Liability Accounts	**97,642,045**	108,056,830
Unreconciled balances	**328,112,668**	328,113,668
	528,945,896	1,033,985,985

This account includes 10% retention from contractors' claims, unreturned borrowed materials, cost of flushing, attorneys' fees, guaranty deposits and depository liabilities. It also includes liabilities with existing law suits and money claims.

The decrease in trust liabilities is attributed to the disbursement of funds to finance the Angat Dam and Dyke Strengthening Project for the Provincial Government of Bulacan.

17. Long-term liabilities/current portion

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

Source	Maturity Date	Currency	Annual Interest Rate	2016	2015
Domestic					
DBP/LBP	12/31/18	P	4.50%	**401,785,714**	723,214,286
SPIAL	05-15-26	$	9.65%	**185,565,825**	188,124,748
ADB 1746-PHI	02-01-22	P	floating	**136,433,133**	189,009,164
NHA		P	floating	**98,795,399**	98,795,399
IBRD 1272/1282	07-15-20	$	8.50%	**71,941,292**	68,118,422
				894,521,363	1,267,262,019
Foreign					
ADB 1379-PHI	07-15-20	$	floating	**1,617,377,198**	1,829,634,132
JBIC (OECF)	02-20-20	Y	2.70%	**1,462,778,618**	1,348,880,777
IBRD 4019-PH	07-01-16	$	floating		81,990,555
China Eximbank AWUAIP II	01-21-30	$	libor rate	**5,170,452,082**	5,258,345,281
ADB 1150-PHI	10-15-16	$	floating		48,095,927
French Protocol	12-31-18	FF	3%-6.8%	**5,623,081**	18,604,537
IBRD 4227 PHI	09-15-17	$	Floating	**9,323,165**	17,227,724
ADB 3377-PHI	03-15-41	$	libor rate	**505,438,747**	-
				8,770,992,891	8,602,778,933
Total				**9,665,514,254**	9,870,040,952

Current Portion -			
Asian Development bank (ADB)			
1379	347,216,535		
1746	10,820,774	**358,037,309**	314,038,426
Int'l. Bank for Reconstruction & Development (IBRD)			
4227		**9,323,165**	164,604,623
French Protocol		**3,196,304**	16,233,115
Special Project Implementation Assistance Loan (SPIAL)		**13,116,660**	12,419,657
China Eximbank Loan		**382,996,451**	
		766,669,889	507,295,821
Non-Current Portion		**8,898,844,365**	9,362,745,131

On February 10, 2011, the MWSS Board of Trustees unanimously passed Board Resolution no. 2011-017 approving the *P2.250 Billion floating rate Bond Issuance under the DBP-LBP Club deal Arrangement.* The bond issuance was guaranteed by the National Government. The proceeds were used to partly finance the MWSS' maturing 7-year USD 150M 9.25% Fixed rate Bond with the BNP Paribas which matured last March 14, 2011. The bond was drawn in full on March 30, 2011 and payable in seven (7) years with pre-termination option. Interest rate was based on the higher of the BSP Reverse Repurchase (RRP) Facility or BSP Overnight Borrowing Rate.

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.

International Bank for Reconstruction and Development (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 that started on November 15, 1981.

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 twenty (20) year loan with a grace period of five (5) years which will mature on July 15, 2020.

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.

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; and c) establish a gradual low-cost improvement of sewerage services in Metro Manila by expanding the Borrower's septage management program.

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 9.9 km 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 fifteen (15) years on a semi-annual basis starting January 21, 2015 and will mature on 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.

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 ten (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 3377-PHI is a negotiated loan agreement between MWSS and Asian Development Bank for the Angat Water Transmission Improvement Project in the amount of US$123.30 million on 27 May 2016. This loan is guaranteed by the National Government and payable semi-annually in 25 years inclusive of 6.5 years grace period. MWSS shall pay 0.25% Guarantee Fee per annum on the outstanding obligation pursuant to DC 1-2016 to the National Government. The expected closing date is 30 June 2022.

18. Deferred credits

This account consists of:

	2016	2015 As Restated
Deferred credits to income - COB	**505,114,350**	**516,153,382**
Deferred credits to Income – Penalty/Interest. on delayed payment of Concession Fee & borrowing costs	**1,267,268,877**	1,213,561,850
Others	**45,963,609**	97,215,051
Unreconciled balances	**22,632,720**	22,632,720
	1,840,979,556	1,849,563,003

Deferred credits to income- COB account represents annual income concession fee – corporate operating budget received in advance from concessionaires pursuant to the concession agreement. Said account is amortized fully within the year to the appropriate income account.

Deferred credits to Income – Penalty/Interest on delayed payment of Concession Fee is the penalty previously charged to MWSI computed based on 364 T-bills rate. The amount was disallowed by the Rehabilitation Court in Court Order approving the Prepayment and Settlement Agreement (PSA) dated 19 December 2007 and Court Order confirming the termination of the corporate rehabilitation proceedings on account of successful implementations of the 2005 Revised Rehab Plan dated 6 February 2008.

The Other Deferred Credits included the following:

Disposal/Public Auction	Sale from disposal of Assets which needs to be reconciled with the various subsidiary accounts for identification of assets, its depreciation and gain or loss on sale of assets.	31,124,028
Cost of Lot Housing	Collection from employees for Cost of Lot payment (MWSS Housing).	13,019,097
Miscellaneous - Others	Pasig River Environmental Mgt. & Rehab Sector Dev. Program (PREMSDP)	1,752,679
Miscellaneous – Cash Bond and Others	Cash deposits intended to cover up expenses in cases of breakage, damage to property and cleanliness of renting MWSS facilities which are refundable.	42,100
Amount withheld for liquidated damages	Amount withheld from contractors under dispute	25,705
Total		**45,963,609**

19. Capital Stock

MWSS has an authorized capital stock of P8 billion corresponding to 80 million shares at P100 par value, of which P6,095,486,784 were issued and outstanding equivalent to 60,954,867.84 shares.

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. Appraisal Capital Stock

The Appraisal Capital Stock is used to record changes in the carrying amount of items of PPE as a result of revaluation. The Revaluation Surplus account has an ending balance of P36.383 billion as shown below:

	2016	2015
Land	**12,205,095,285**	20,160,080,854
Structures and Improvements	**292,485,820**	292,485,820
Collecting and Impounding Reservoirs	**1,111,404,830**	1,111,404,830
Supply Mains	**3,097,555,968**	3,097,555,968
Distribution Reservoirs and Booster Station	**2,432,331,004**	2,432,331,004
Building and Improvements	**485,838,406**	485,838,406
Wells and Facilities	**76,762,346**	76,762,346
Water Treatment Equipment	**103,483,461**	103,483,461
Sewer Treatment Equipment	**4,192,576**	4,192,576
Water Treatment Plant	**126,236,850**	126,236,850
Transmission and Distribution Mains	**7,730,461,901**	7,730,461,901
Water Meters	**98,315,762**	98,315,762
Transmission and Discharge Mains	**482,090,989**	482,090,989
Public Faucets/Sanitary Facilities	**15,954,953**	15,954,953
Sewer Treatment Plant and Pumping Stations	**82,942,888**	82,942,888
Hydrants	**9,799,181**	9,799,181
Manholes and Accessories	**13,968,231**	13,968,231
House Water Connection	**8,177,985**	8,177,985
House Sewer Connection	**38,709,103**	8,177,985
Electrical Installation and Lighting System	**12,096,251**	12,096,251
	28,427,903,790	**36,382,889,359**

The decrease amounting to 7.954 million represents adjustments and appraisal made in the Land account as discussed in Note 9.

22. Revenue

This account consists of:

	2016	2015 As Restated
Concession Income	**993,105,901**	1,194,999,130
Concession Fee		
Debt Service	**1,554,341,919**	1,114,696,519
Progress Billing	**53,035,195**	-
Business Income		
Raw Water	**74,428,065**	54,023,666
Rental of Leased Properties	**95,679,346**	257,695,887
Interest on Investments and Deposits	**67,432,385**	50,047,957
Miscellaneous Income	**215,391**	3,039,977
Other Fines and Penalties	**3,230**	8,956
Gains/Loss on Foreign Exchange	**(510,677,154)**	(504,030,291)
Gain/Loss on Disposed Assets	**22,365**	247,784
Total	**2,327,586,643**	2,170,729,585

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 Income – is the annual Current Operating Budget being paid by the concessionaires to MWSS for administrative expenditures subject to annual Consumer Price Index adjustment.

Business Income – is income resulting from operation, including interest earned from deposits.

Raw Water – is business income from sale of raw water on service areas not covered by the service areas of the MWSI.

Gain or Loss on Foreign Exchange is paper gain/loss as a result of appreciation or devaluation of pesos on loan payments.

Gain/Loss on Disposed Assets – is the difference between book value and income from sale from disposal.

23. Personal services

This account is comprised of the following:

	2016	2015 As Restated
Salaries and wages – regular	**64,146,472**	68,399,943
Productivity incentive allowance	**8,306,087**	13,430,789
Other personnel benefits	**6,548,714**	9,222,271
Life and retirement insurance contributions	**7,700,027**	8,261,880
Cash gift/13th month pay	**4,228,429**	6,511,177
PERA	**3,814,200**	4,010,407
Honoraria	**2,052,000**	3,495,512
Representation allowance	**2,730,721**	2,815,044
Transportation allowance	**2,590,878**	2,682,307
Other bonuses and allowances	**5,446,193**	1,871,292
Clothing allowance	**820,000**	860,000
PHILHEALTH contributions	**654,125**	693,713
Loyalty	**3,101,659**	656,500
Terminal leave benefits	**2,157,946**	968,844
Hazard pay	**214,010**	436,943
ECC contributions	**191,200**	201,450
Pag-IBIG contributions	**191,200**	201,100
Subsistence, laundry & quarter allowance	**2,846,454**	74,243
Year End bonus	**1,970,707**	-
Overtime and night pay	**21,129**	-
	119,732,151	124,793,415

24. Maintenance and other operating expenses

This account consists of the following:

	2016	2015 As Restated
Taxes, duties and licenses	**28,339,649**	85,113,492
Security services	**27,010,399**	25,411,872
Other maintenance and operating expenses	**3,990,797**	10,079,426
Consultancy expenses	**1,231,429**	11,692,938
Auditing services	**6,149,103**	11,163,866
Janitorial services	**4,288,528**	4,068,812
Other professional services	**4,500,543**	3,846,876
Electricity expenses	**3,934,245**	3,663,992
Advertising expenses	**738,203**	2,895,150
Insurance expense	**2,763,099**	2,759,350
Training expenses	**3,133,933**	2,538,826
Office supplies expenses	**1,726,770**	2,280,825
Communication expense	**2,303,790**	2,238,400

Legal Services	**-**	1,919,836
Extraordinary and miscellaneous expenses	**1,438,330**	1,890,723
Gasoline, oil and lubricants	**1,518,285**	1,546,375
Representation expenses	**2,423,221**	1,533,083
Repairs and maintenance	**1,192,183**	730,219
Other supplies expenses	**954,576**	970,454
Printing and binding expenses	**485,632**	621,741
Drugs and medicines expenses	**405,225**	633,956
Rent Expense	**735,570**	514,079
Travelling expenses	**586,124**	274,027
Subscription expenses	**1,445,555**	140,966
Water expenses	**25,424**	107,015
Fidelity bond premiums	**54,802**	53,491
Postage and deliveries	**52,343**	46,515
Membership dues and contributions to organizati	**44,136**	46,006
Environment/Sanitary Services	**-**	12,000
	101,471,894	178,794,311

25. Income Tax Expense

Section 18 of the MWSS Charter (R.A. 6234) provides that "All articles imported by the Metropolitan Waterworks and Sewerage System xxx, shall be exempt from the imposition of import duties and other taxes.

BIR Ruling No. DA-088-2001 dated May 16, 2001 ruled that the concession fees paid by the Concessionaires to MWSS, if at all they are in the nature of income, shall be excluded from the gross income subject to tax.

Categorically, MWSS is taxable with respect to its other income other than concession fees received from the concessionaires.

The account Taxes, Duties and Licenses is used to recognize the amount of taxes, duties and licenses and other fees due to regulatory agencies except income tax. This also includes taxes on interest income on savings deposits, time deposits and government securities of the bond sinking fund/other funds. (*COA Circular 2001-008 and the New Government Accounting Manual*)

26. Financial expenses

This account consists of:

	2016	2015 As Restated
Interest expenses	**397,284,771**	314,721,17
Other financial charges	**96,140,933**	52,846,442
Bank charges	**9,359,186**	132,662
	502,784,890	367,700,281

27. Contingent Liabilities

MWSS is contingently liable for lawsuits or claims filed by third parties which are either pending in the courts or under negotiations. These cases involve, among others, lease of properties, collection of sum of money, water use conflict issues, payments of claims, protest on real property taxes and tax consequences resulting from revaluation/appraisal of its Property, Plant and Equipment.

a. BIR Tax Assessment

MWSS also received Assessment/Demand Letter requiring the agency to settle tax deficiency for CY 2010 amounting to P30,772,011.57. MWSS is currently exhausting all available legal remedies with the BIR on the subject tax assessments.

b. 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 P30M. 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.

c. Other significant legal cases are as follows:

- MWSS vs. Maynilad Water Services Civil Case R-QZN-15-06702-CV
- Neri Colmenares and Carlos Zarate of Mayan Muna partylist vs Cesar Purisima, MWSS, et.al GR. 219352
- Lina Francia F. Badeo vs. MWSS for reinstatement with back wages and others
- Lease of MWSS property along Katipunan Ave by SM Prime Holdings
- Water for all Refund Movement vs. MWSS GR. 207444/208207/210147
- Gabriel Advincula vs. MWSS; GR. 179217, Re: Severance Pay
- Alexander Lopez, et.al vs. MWSS, GR 198693, Re: Contract Collectors Claim
- CSC vs MWSS; indirect Contempt on Alexander Lopez, et.al, Separation Pay and Terminal Leave of Contract Collectors
- Various cases regarding Unlawful Detainer on Land Properties of MWSS

d. MWSS Appraisal Capital Stock (Revaluation Surplus) will result in tax consequences once the actual amount of revaluation surplus is determined through the conduct of appraisal of its Property, Plant and Equipment.

28. 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:

1. Income Tax

   For the Year 2016 MWSS incurred P10,798,509 corporate income tax payable.

2. VAT Output Tax

   MWSS is a VAT registered company with VAT Output Tax declaration of Php11,941,161.54 for the year based on the amount reflected in the Income/Receivables Account of Php99,509,679.69.

3. VAT Input Tax

   The amount of VAT Input taxes claims are broken down as follows:

Particulars	Amount
Beginning of the year	291,016
Current year's purchases	3,644,709
Total	3,935,725
Claim for Tax credits and other adjustments	2,008,652
Input VAT for 2017 (January)	283,605

4. Other Taxes and Licenses

Particulars	Amount
Local	
Other Taxes and Licenses	15,221,512
BIR Registration Fee	500
BIR Assessment Fee - 2010	13,117,637
Total	28,339,649

5. The amount of withholding taxes categorized into:

Particulars	Amount
i. Tax on Compensation and Benefits	11,619,815
ii. Creditable Withholding Tax/es	17,607,039
iii. Final Withholding Tax/es	881,415
iv. Expanded Withholding Tax/es.	7,120,684

26. Unreconciled Asset and Liability Account Balances

The summary of the unreconciled balances in the Asset and Liability accounts is as follows:

Particulars	2016	2015
Asset Accounts		
Accounts Receivable	**21,625,745**	21,625,745
Other Receivables	**1,108,354**	1,108,354
Prepayments	**96,513,124**	96,513,125
Property, Plant and Equipments	**22,162,726**	32,052,328
Construction in Progress	**457,018,739**	457,018,739
Other Assets	**(19,575,783)**	(19,575,783)
Total Unreconciled Assets	**578,852,905**	588,742,508
Liability Accounts		
Payable Accounts	**533,802,867**	533,802,867
Other Liability Account	**328,112,668**	328,113,668
Deferred Credits	**22,632,719**	22,632,720
Total Unreconciled Liabilities	**884,548,254**	884,549,255
Net Unreconciled Balances	**305,695,349**	295,806,747

27. In compliance with PAS 8 (Accounting Polices, Changes in Accounting Estimates and Errors, the Retained Earnings as of January 1, 2016 has been restated as follows:

Balance, January 1, 2016 (Unrestated)	**1,278,854,597**
Adjustments:	
Reclassification of Land Revaluation Cost	8,020,715,102
Understatement of Concession Fee - DS	84,338,552
Prior Years/Adjustments/Allocated Errors	32,202,758
Adjustment of Depreciation	(57,620)
Payment of Money Claims – AA, COLA, RA 1616	(722,223)
Adjustment of PPE	(1,854,801)
Income/Expense Adjustments	(31,677,850)
Adjustment of Guarantee Fee payable to NG	(37,966,918)
Borrowing Cost that should not be Capitalized	(248,784,911)
Total	**7,816,192,089**
Retained Earnings, January 1, 2016 (As Restated)	**9,095,046,686**