REPUBLIC OF THE PHILIPPINES
OFFICE OF THE PRESIDENT

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-A

ANNUAL REPORT PURSUANT TO SECTION 17 OF THE SECURITIES REGULATION CODE AND SECTION 141 OF THE CORPORATION CODE OF THE PHILIPPINES

1. For the fiscal year ended December 31, 2005

2. SEC Identification Number 31171 3. BIR Tax Identification No. 000-168-801

4. Exact name of registrant as specified in its charter PETRON CORPORATION

5. Philippines
Province, Country or other jurisdiction of incorporation or organization
6. (SEC Use Only) Industry Classification Code:

7. 358 Senator Gil Puyat Avenue, Makati City
Address of principal office
1200
Postal Code

8. (0632) 886-3888
Registrant's telephone number, including area code

9. N/A
(Former name, former address, and former fiscal year, if changed since last report.)

10. Securities registered pursuant to Sections 8 and 12 of the SRC or Sections 4 and 8 of the RSA

Title of Each Class	Number of Shares of Common Stock Outstanding and Amount of Debt Outstanding
Common Stock	9,375,104,497 Shares

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

Yes [X] No [ ]

If yes, state the name of such stock exchange and the classes of securities listed therein:

Philippine Stock Exchange	Common Stocks

12. Check whether the registrant:

(a) has filed all reports required to be filed by Section 17 of the SRC and SRC Rule 17 thereunder or Section 11 of the RSA and RSA Rule 11(a)-1 thereunder and Sections 26 and 141 of The Corporation Code of the Philippines during the preceding 12 months (or for such shorter period that the registrant was required to file such reports);

Yes [X] No [ ]

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

Yes [ ] No [X]

13. The aggregate market value of the voting stock held by non-affiliates of the Registrant is P42.19 billion based on the PSE price of P4.50 as of December 29, 2005.

DOCUMENTS INCORPORATED BY REFERENCE

N o n e

PART I - BUSINESS

(A) Description of Business

(1) Business Development

Petron

Incorporated in the Philippines in 1966 as Esso Philippines, Inc., Petron Corporation is the largest refiner and marketer of petroleum products in the Philippines. The company was renamed Petrophil Corporation in 1973 when the Philippine National Oil Company (PNOC) acquired Esso. In 1985, Petrophil Corporation and Bataan Refinery Corporation (formerly the Standard Vacuum Refining Corporation) were merged with Petrophil as the surviving Corporation. Petrophil later changed its corporate name to Petron Corporation.

On March 4, 1994, PNOC sold 40% of its shares in Petron to Aramco Overseas Company B.V., a wholly owned subsidiary of Saudi Arabian Oil Company (SAUDI ARAMCO). On September 7, 1994, 20% of Petron's shares were listed with the Philippine Stock Exchange in the biggest Initial Public Offering (IPO) in the Philippines.

Subsidiaries

At present, Petron has six subsidiaries, namely:

- New Ventures Realty Corporation (NVRC) is a realty firm established on August 24, 1995. The company was then equally owned by Petron and the Retirement Fund. However, in June 2003, Petron increased its share to 79.95%. It is authorized to acquire and develop land but it does not engage in the subdivision business. Land suitable for use as service station sites, bulk plants or sales offices are purchased by NVRC. These properties are leased to Petron for use in the latter's operation. A wholly owned subsidiary of NVRC, Las Lucas Development Corporation was acquired in July 2003.

- Petrogen Insurance Corporation or Petrogen is a wholly owned subsidiary of Petron Corporation incorporated on August 23, 1996. It serves the insurance requirements of Petron and its allied business partners such as contractors, suppliers and dealers. Licensed by the Insurance Commission in November 1996, Petrogen has the authority to issue policies on fire, marine, casualty and bonds. Insurance provided excludes life insurance. In 2001, it was granted authority to cover insurance for accidental death and dismemberment, travel and directors' and officers' liability.

- Overseas Insurance Corporation or Ovincor was incorporated on November 16, 1995 under the laws of Bermuda for the purpose of expediting the reinsurance of Petron's insurable interests as covered by Petrogen Insurance Corporation. Reinsurance includes the insurance cover for the Refinery, the bulk plants and service station properties, petroleum and cargo insurance and performance bonds for Petron contractors and haulers as well.

- Petron Foundation, Inc. (PFI) was incorporated on July 25, 1996. PFI was created to function and operate as a charitable and research foundation; to handle social, environmental, and music and arts development projects of Petron; to institutionalize and intensify Petron's active involvement in corporate and social responsibility projects; to support scholarship programs for financially-handicapped but deserving students; and to participate in other social projects supported by Petron.

- Petron Freeport Corporation (formerly Petron Treats Subic, Inc) was incorporated on November 6, 2003. It is a Petron subsidiary empowered to, among others, sell on wholesale or retail fuels such as gasoline, kerosene, diesel, LPG, lubricants and greases as well as operate retail outlets, restaurants, convenience stores and the like. The company has its principal office at the Subic Bay Metropolitan Area (SBMA), and operates Petron's "mega station" at the SBMA.
- Petron Marketing Corporation (PMC) was incorporated on January 27, 2004 with the same business purpose as the Petron Freeport Corporation. The Retail Trade Liberalization Act paved the way for Petron to form a direct-retailing subsidiary. The new subsidiary operates company-owned, company-operated (COCO) service stations. It offers a complete range of fuel products. The COCO stations play a major part in launching market initiatives to strengthen the Petron brand and gives Petron the opportunity to quickly introduce innovations beyond the present services that are available in Petron stations.

The subsidiaries have no plans of engaging in other line of products or services than that provided to Petron.

Petron Corporation and any of its subsidiaries have not been the subject of any bankruptcy, receivership or similar proceedings.

Operating Highlights

Marketing

In 2005 Petron Corporation dominated the industry with a market share of 38.3%, higher by 0.6% points than its 37.7% share of the market in 2004. It sustained market leadership in the retail and industrial trades, increasing market share to 34.0% and 43.5% respectively. In the lubes business, there was an improvement in its market share from 24.5% in 2004 to 27.2% in 2005. And while the new players collectively cornered 44% of the LPG market, Gasul improved market share by 1% point to 27.6% in 2005, and remains the single biggest player in the industry.

Petron now has 1,242 service stations including two new company owned-company operated stations (COCO), bringing the company's outlet share to 30%. The point-of-sale (POS) system was installed in 31 service stations. The system is expected to help provide customers with consistent and efficient customer service, standardized prices and promotions, and build a database of information that can be used for market sales analysis. A tri-media campaign to introduce Xtra Unleaded was likewise launched.

Petron was also able to acquire several industrial accounts from competition, especially in the aviation industry. The company set-up more than 50 branch stores thru its Gasul dealers. It established three Treats convenience stores, five company-operated quick-serve-restaurants, two lube sales centers, four lube distributorships and a lube center.

Petron made its first lubes export in 2005. The number of fleet card and BPI Mastercard holders and the number of vehicles running on Xtend Autogas likewise increased. In addition, it implemented the Demand Planner as part of its commitment to strengthen its supply chain through more efficient forecasting of sales demand.

Refinery

In 2005, the Refinery commenced operation of the 22 MBSD Gas Oil Hydrotreater (GOHT-3) and the 10 MBSD LVN Isomerization Unit. The GOHT-3 has increased the Refinery's capacity to produce 0.05wt%S Automotive Diesel Oil in compliance with the Clean Air Act. The Isomerization Unit enables us to comply with the 2% benzene and 35% aromatics content of premium gasoline.

To further comply with the Clean Air Act, the installation of portholes and access ladders for close monitoring of air emission levels on boilers and furnace stacks was completed during the year.

The Refinery passed the Clean Air Act emission standards compliance test last October 2005. As a result, the Department of Environment and Natural Resources-EMB Region III (DENR-EMB) will issue in February 2006 a one year permit to operate the air pollution source and control installations.

The Department of Environment and Natural Resources granted the Refinery the Discharge Permit for its Oily Waste Water Treatment Plant from June to December 2005 and this was renewed up to December 2006. Also, the Discharge Permit for the Refinery's Housing Sewage Treatment Plant has been approved for renewal.

The Offsites Automation Project which includes product metering and tankage inventory management was fully operational by the end of the second quarter of 2005. All fourteen custody flowmeters was certified for custody transfer by the Bureau of Internal Revenue in June 2005.

On the Refinery Power Distribution System upgrade, the new 69 kV transformer and cables and switch gear assemblies were commissioned last March 2005. The new transformer will enable the Refinery to draw more power from NPC while the switch gear assemblies will allow the Refinery to operate using NPC power in isolated mode, thereby sealing the Refinery's Power Generation System from NPC Power fluctuations.

The Refinery was issued ISO 14001:1996 certification which is valid until May 2006. This covers crude oil receipt, manufacturing process and distribution process via pier.

On its corporate social responsibility, the Refinery in coordination with the Bataan Medical Society, Limay Community Center and Alangan Health Center, provided medical and dental services to residents of Alangan in Bataan. It was awarded first place in the search for Healthy Work Place, Provincial Level by the Philippine Health Promotion Program Provincial Council. It conducted Kontra Kalat sa Dagat along the shoreline of Kitang, Limay, Bataan and sponsored a tree-planting activity at Hulo Alangan, Limay.

The Refinery will convert its Thermofor Catalytic Cracking Unit (TCCU) to Petrochemical Fluid Catalytic Cracker (PetroFCC) and install a Propylene Recovery Unit. This will allow the recovery of more white products like LPG, gasoline, aviation fuel, etc. in addition to propylene. It will also install a Benzene-Toulene-Xylene (BTX) Recovery Unit to meet the increasing demand for petrochemicals. Both projects are expected to be completed by 2008.

Supply and Operations

In 2005, the Distribution Optimizer (DO) project was implemented. This was done in coordination with the Business System Support Department, and other departments of Marketing, Refinery and Corporate Planning divisions. This project makes use of distribution planning and scheduling tools which can generate a cost effective daily shipment schedule for one month for all depots and direct account deliveries. The volume per product per compartment for each vessel that will be loaded at the refinery and date of loading can be determined. Using these tools, we can come up with the total freight cost per delivery including demurrage and the resulting transshipment cost per liter of product delivered. Furthermore, these will enable us to manage our inventory and assist us in tactical planning and business strategy evaluations such as impact of storage tank re-assignments on freight cost and inventory levels, depot network assessment evaluation, optimization of tanker capacity and sizes, etc.

Training on preparing and implementing security plans were conducted for terminal and depot personnel in compliance with the International Ships and Ports Facility Security (ISPS). To date, a total of 19 depots and terminals are ISPS certified by the Department of Transportation and Communications-Office of Transport Security (DOTC-OTS). Of these, seven (7) domestic ports such as Navotas, Palawan, Mactan, Ormoc, Roxas, Iligan and the Rosario Terminal have been aligned also to ISPS standards. Our port facility security programs particularly in Zamboanga and Mandaue are also used as model by DOTC-OTS in their trainings and presentations, notably during visits of their Australian counterparts.

The Environment Management Quality Systems was instituted in various terminals and depots. They are now working on the necessary training in preparation for ISO 14001 certifications.

Petron terminals and depots have oil spill contingency plans (OSCP) which can be executed whenever necessary. Zamboanga depot's OSCP was the first to be approved by the Philippine Coast Guard in the entire country.

Health, Safety and Environment

The Department of Labor and Employment has given recognition to different Petron facilities for attaining a 5.4 million man-hours without lost-time accident record as a result of their commitment in implementing programs and activities on occupational health and safety. These facilities are the Refinery, Gasul, Davao and Jimenez Depots, Rosario and Limay Terminals.

Petron did not only conduct health and safety training programs for its employees. It also organized and held programs for contractors and customers.

- The Contractor Safety Management program was established in order to set guidelines on the minimum health and safety requirements that contractors should comply with prior to commencement of any activity within Petron premises. Compliance with the program is a requirement before accrediting a contractor. In line with this, they attended courses on Basic Occupational Safety and Health and Safety Orientation.

- Training programs on oil spill and fire control were conducted for employees of different Gasul industrial accounts while personnel of various industrial accounts in Luzon were trained on how to respond to emergency situations.

- Personnel of the Bureau of Fire Protection in Roxas City attended a fire control seminar conducted by Petron employees.

Corporate Social Responsibility

Petron categorizes corporate social responsibility into: 1) community relations and advocacy – refers to immediate support to society; 2) corporate strategic philanthropy- means responding to bigger national social concerns and takes into consideration both national and global agenda; and 3) CSR as core business- pertains to developing business solutions to address social problems and is considered the ideal form of social responsibility.

In 2005, the company started the integration of corporate social responsibility (CSR) into Petron's core business. In line with this, management formed a CSR team with members from key units of the company. The team met regularly for the formulation of ideas on integrating CSR into strategic business units and communicating the program to every employee and business partner.

Petron launched the FUEL HOPE (HELPING FILIPINO CHILDREN AND YOUTH OVERCOME POVERTY THROUGH EDUCATION). Its objective is to strengthen its corporate strategic philanthropy by helping alleviate poverty through education. Through this program, it hopes to promote CSR as a way of life for its employees within and outside the company.

Under this initiative is the continued implementation of Tulong Aral ng Petron. Now on its fourth year, the total number of scholars have reached almost 4,000 with the number increasing by 1,000 every year. The scholars are enrolled in 82 public elementary schools in 12 cities and municipalities of Metro Manila and out of the total, 730 are enrolled in Petron schools in Iligan City, Sarangani and Zamboanga City. The program is recognized by the Department of Social Work and Development as the only partnership with the private sector that has effectively been sustained.

A complementary program and in support of the Department of Education's Adopt-A-School campaign is the Petron School. The company is putting up schools in communities where the need is greatest. By the end of 2005, the company had sponsored the construction of 13 schools in the following areas: Limay, Bataan; Mandaue City, Cebu; Tagoloan, Misamis Oriental; Davao City; Looc, Lamitan, Basilan; Zamboanga City; Pangyan, Sarangani; Jimenez; Iligan City; Nasipit; Sultan sa Barongis, Maguindanao; Datu Paglas, Maguindanao; and Bongao, Tawi –tawi.

In 2006, there is a plan to build six schools in Mindanao and one each for Luzon and Visayas.

The company partnered with Sa Aklat Sisikat Foundation for a reading program in six Petron schools, directly benefiting over 1,000 Grade 4 students and more than a dozen teachers and school administrators.

Petron also introduced the entrepreneurship program for the youth. This envisions a generation of youth who will be wealth creators either as entrepreneurs or as part of a resource pool that can meet the company's need for highly skilled workers in our retail network.

In coordination with the Technical Education and Skills Development Authority (TESDA) and the Muntinlupa Business High School, Petron will develop a curriculum on entrepreneurship, food service management and service station service management. The curriculum will include skills training that will fit into Petron's core business, specifically retail service management. It is envisioned that this program will institutionalize competency and training standards for all business high schools in the country—leading to national assessment and certification of qualified students.

Petron started its support for the WIWAG Business Week Program- a five-day computer assisted business management training. Its sponsorship included the engagement of employees as trainors/resource persons.

The company has been regularly leading coastal clean-ups and tree and mangrove planting and has come up with various environmental awareness programs and initiatives. It has continuously supported the rehabilitation of the La Mesa Watershed. In 2005, it inaugurated the 1.2km. Petron Fitness and Nature Trail and the 2,500-seater Ampitheater at the La Mesa Ecopark inside the watershed.

To promote environmental stewardship, Petron has effectively sustained an integrated coastal management program for Bataan, an integral component of the Manila Bay Environmental Management Project. For the past six years, it has maintained its partnership with the UNDP International Maritime Organization, which recognized the program as the one of the first successful public-private partnership initiatives in the seas of East Asian.

(2) Business of Issuer

(i) Principal products or services and their markets:

Petron's principal business involves the refining of crude oil and the marketing and distribution of refined petroleum products, mainly for the domestic market. It supplies more than one-third of the country's petroleum product requirements. It sells a full range of refined petroleum products, including: industrial fuel oil, diesel, gasoline, liquefied petroleum gas (LPG), jet fuel, kerosene, asphalt, solvent and mixed xylene. Straight-run fuel oil, diesel, and mixed xylene are exported. Lubricating oils and greases are manufactured at Petron's Lube Oil Blending Plant at the Pandacan Terminal. When necessary, some refined petroleum products are imported.

The major markets in the petroleum industry are Reseller, Industrial, Lubes and LPG Trades.

Petron sells its products to both industrial end-users and resellers through a nationwide network of service stations, Gasul dealers and retail outlets.

(ii) Percentage of sales or revenues contributed by foreign sales:

Sales Revenue

	Domestic	Exports	Total
2003, in million pesos	96,472	14,265	110,737
2003, in percent	87%	13%	100%
2004, in million pesos	134,275	13,081	147,356
2004, in percent	91%	9%	100%
2005, in million pesos	167,703	23,525	191,228
2005, in percent	88%	12%	100%

(iii) Distribution methods of products or services:

Petron's petroleum products are refined from crude oil at its refinery in Limay, Bataan. From the Bataan Refinery, products are distributed to the various storage terminals and direct consumer accounts nationwide using a fleet of barges and tankers. Products are distributed via pipeline to the Bataan Combined Cycle Power Plant of NPC. From the storage depots, products are hauled by tank trucks to service stations and to direct consumer accounts. Sometimes products are sourced from "rationalized" depots operated by other oil companies.

Sales to customers within the terminal's tributary area are withdrawn by tank trucks.

Lubes and greases in various packages are also transported via container vans to bulk plants and terminals outside Metro Manila. These are sold through service stations and sales centers.

In the LPG trade, Petron has a nationwide network of retail dealerships and outlets. To guarantee convenience for the customer in purchasing Gasul and accessories, retail outlets are usually situated in the vicinity of residential areas or at service stations. Also, we have "*Tawag Lang Centers*" which the customers can call to place their orders, and these centers will ask the dealer nearest the residence or location of the customer to deliver the product.

(iv) New products or services:

Petron Xtra Unleaded Gasoline is an environment–friendly, premium motor gasoline recommended for high compression engines. The use of this product results in lower fuel consumption, cleaner engine and better vehicle performance.

Petron Farm Trac Oil is a single-grade motor oil recommended for use in farm equipment such as threshers, huskers, reapers, cutters and generators operating under mild to moderate service conditions. It protects engines against corrosive wear and pistons from having carbon deposits.

Petron Marine HD Oil is a marine oil specially formulated and designed as a crankcase oil for in-board engines for small fishing boats and bancas, operating under mild to moderate service conditions. It provides adequate alkalinity and detergency for engines using low sulfur diesel fuel.

These new lubricants are being endorsed and distributed by the association of manufacturers and distributors of farm machineries and small fishing boats.

The formulations of aftermarket specialties like Petromate Oil Saver, Petromate Oil Improver, Petromate Diesel Power Booster, etc. were enhanced. Also, the packaging of these products was changed.

Based on a joint testing and evaluation conducted together with Original Equipment Manufacturers, Petron 2T was approved by Kawasaki Motors Phils. Corporation for use in 2T motorcycles. On the other hand, the Rev-X Trekker was approved for use in vehicle service and maintenance procedures of KIA gasoline and diesel engines.

(v) Competition

The oil industry is very much affected by high crude prices, decreasing oil demand, tight competition, illegal trading practices and activism of local government units.

High Crude Oil Prices- The rise in crude prices started in the second half of 2004 and continued up to 2005 due to high global demand particularly from the U.S., China and India. Dubai crude averaged US$49.5 per barrel in 2005 which was 47% higher than the US$33.7 per barrel in 2004.

Oil Demand- In 2005, oil consumption decreased by 8% compared to 2004 wherein consumption was unusually high because of election-related activities. The lower consumption can also be accounted for by the high regional and domestic prices of petroleum products brought about by high crude prices and product prices in the region and the imposition of VAT starting November 2005.

Tight competition- The entry of new players continues to heat up competition. The new players have captured 14% of the market. They have substantially gained headway in the LPG sector with a market share of 44%.

Illegal Trading Practices- After the market was deregulated, cases of illegal trading practices (e.g. "bote-bote" retailing, illegal refilling) and smuggling increased. This has resulted in unfair competition among the players.

Activism of Local Government Units (LGUs)- The industry continues to be vulnerable to the growing activism of local government units. A specific concern is the ordinance requiring the relocation of oil terminals at Pandacan. Oil companies are given 7-10 years to relocate. Another matter is the imposition of local taxes on oil depots. In line with this, the oil industry is moving for the issuance of a Department of Finance (DOF) circular defining and limiting the taxing powers of LGUs.

Petron participates in the reseller (service station), industrial, lube and LPG sectors, through its network of service stations, terminals & bulk plants, dealers, and distributors nationwide. Its competitors are Pilipinas Shell Petroleum Corporation, Caltex, Philippines, Total Philippines Corporation, Flying V, SeaOil Petroleum Corporation and other new players. The company has continuously developed or adopted initiatives that will improve operational efficiencies; manage costs and risks; and maximize utilization of its assets and opportunities like tapping new markets, engaging in new businesses, etc.

With these initiatives, Petron has maintained its market leadership in 2005 with total market share of 38.3%. Shell and Caltex has 31.8% and 15.2%, respectively and the new oil players' share is 14.7%.

Among the various trades, Petron's market share was highest in Industrial with 43.5%. The rest of the pie was shared by Shell with 33.1%, Caltex with 13.1% and the new players with 10.2%. In the Reseller Trade, Petron was also the market leader with a 34.0% market share which was slightly higher than Shell (32.9%).

In the Gasul Trade, the new players garnered 44.6%. We had 27.6% which is higher than Shell's 21.2% and Caltex's 6.7%.

In the Lube Trade, Shell's market share is 30.9% while Petron and Caltex has 27.2% and 24.9%, respectively.

(vi) Sources and availability of raw materials and the names of principal suppliers

Arab crude accounts for 91% of total crude purchased in 2005 and the remainder like Tapis and Miri were sourced from the Far East. We have a supply agreement with Saudi Aramco which commenced in March 1994 and is in effect for 20 years, and a crude supply agreement with Petronas that is renewed annually.

We have also been sourcing LPG from Petronas for the last six years.

We also have contracts with shipping companies to ensure availability of vessels for our crude shipments.

(vii) Dependence on one or a few major customers and identity of any such major customers

Sales to NAPOCOR account for about 9% of Petron's total sales for 2005. Loss of this account will impact on sales volume.

(viii) Transactions with and/or dependence on related parties

Since 1993, Petron has been leasing from PNOC certain parcels of land where its refinery and most of its bulk plants, terminals, and service stations are located. Petron has also been leasing from New Ventures Realty Corporation some parcels of land where some of its depots, terminals and many service stations are located. Under the Retail Trade Liberalization Law, Petron is allowed to engage in direct retail of its fuel products thru its subsidiaries, namely, PMC and PFC. PMC is also leasing service station sites from NVRC.

Majority of the insurance policies of Petron for 2005 were placed with Petrogen Insurance Corporation.

Also, in 2005, Petron purchased 91% of its crude under the Crude Oil Supply Agreement with Saudi Aramco, a company wholly owned by the Saudi Arabian Government.

(ix) Patents, trademarks, licenses, franchises, concessions, royalty agreements

Petron has trademark registrations for a term of 20 years for its Rev-X, AS, Petrogrease, Cablekote, Gearkote, Gearfluid, Gasulette, Gasulite, Gasulgrille, Gasul, Marinekote, LPG Gasul Cylinder 50 kg., Gasul and Device, LPG Gasul Cylinder 11 kg., Petron STM, Petron Autokote, GEP, Regatta, Petron Old Logo, Hypex, Extra, Petron Old Logo (Tradename), 2T, Turnol, Petromar HD, Spinol, Airlube, Hydrotur, Petromix, Voltran, Stemol, Petrocyl 680, Printsol 600, Overglide, Grease Away, Petrokut, Petron Railroad Extra, Rubbex, Petron Dust Stop Oil, Oil Saver, Petron HD, Petron HD3, DCL 100, Milrol, Petropen, Petron GST, Petron with XCS, With XCS, Super DC, LPG Gasul Cylinder 2.7 kg. Petromul CSS-1, and New Petron Logo. Treats and Rev-X All-Terrain are registered for a term of 10 years.

Petron has pending applications for registration of the following trademarks: Ultron, Oil Improver, Lubritop, Antimist, Power Booster, Grease Solve, Zerflo, Process Oils, Petron XD, TDH 50, Petron 2040, Petrotherm 32, Petrokote, Petrosine, Petron, 2T Motorcycle Oil, Petromate with Logo, Petron Motor Oil, Automatic Transmission Fluid, Engine and Radiator Coolant with Radiator Device, Powerburn 2T, Gasulito with Stylized Letter "P", Gasulito (7kg.) Container, Petron HDX, Molygrease, Petron GX, Asphaltseal, Petron TF, Ropgriz, Cable Lube, Petron DOT-3 Brake Fluid, Petron Engine Flush, Treats, Solvent 3040, Petron Radiator Cleaner, Adgas, Blaze, Ultimax, Petronconnects.com, "Your Friend on the Road", Petron Gasul 11-kg POL-VALVED Cylinder, Ultron Speed, Ultron Rallye, Rev-X Trekker, Rev-X Hauler, Rev-X HD, Bull's Eye, Ultron Race, Ultron Touring, Ultron Extra, Clean 'n Shine, Sprint 4T, Xpert Diesel Oils, Ultimate Release from Engine Stress, Xpert sa Makina Express ang Kita, It's Oil You Need, Pchem, Petrocare, Penetrating Oil, Gas Saver, Super Coolant, Brake and Clutch, Lakbay Alalay, 2T Enviro with Oil Drop, Rover, Petron Freeport Corporation, Petron Marketing Corporation, Fuel Success, Xtra, Power for Extra Miles, Petron Marine HD Oil for Fishing Boat, Petron Farm Trac Oil for Farm Equipment, Petron Connects, Treats (for bottled water), Fuel, Fuel Hope, Fuel Trust, Fuel Experience, Fuel Drive, Fuel Excellence, Fuel Efficiency, Pure Distilled Drinking Water, and Fuel X Fuel Customer.

Petron has copyrights for its 7-kg LPG container, Gasulito with stylized letter "P" and 2 flames, for Powerburn 2T, and for Petron New Logo (22 styles). Copyrights endure during the lifetime of the creator and for 50 years after his death.

(x) Need of government approval of principal products or services

The Downstream Oil Industry Deregulation Act of 1998 (R.A. No. 8479) requires the registration with the DOE of any fuel additive prior to its use in a product. Product specifications have to comply with the requirements of the Department of Trade and Industry (through the Bureau of Product Standards).

In compliance with the Philippine Clean Air Act of 1999 (R.A. No. 8749), Petron produces: (i) unleaded premium gasoline with an anti-knock index (AKI) of not less than 87.5 and Reid vapor pressure of not more than 9 psi; (ii) unleaded gasoline with aromatics not exceeding 35% by volume and benzene not exceeding 2% by volume; (iii) automotive diesel containing a concentration of sulfur not exceeding 0.05% by weight with a cetane number of not less than 50; (iv) industrial diesel containing a concentration of sulfur not in excess of 0.30%.

Government regulations still require the following: Fire Safety Inspection Certificates; Certificates of conformance of facilities to national or accepted international standards on health, safety and environment; Product Liability Insurance Certificates or Product Certificate of Quality; and the Environmental and Compliance Certificate issued by the DENR for service stations and for environmentally-critical projects. These certificates have to be submitted to the Department of Energy for monitoring (not regulation) purposes.

Incidentally, reports to the DOE are required for the following activities/projects relating to petroleum products: (i) refining, processing, including recycling and blending; (ii) storing/transshipment; (iii) distribution/operation; (iv) distribution/operation of petroleum carriers; (v) gasoline stations; (vi) LPG Refilling Plant; (vii) bunkering from freeports and special economic zones.

(xi) Effect of existing or probable government regulations on the business

Clean Air Act (CAA). Petron invested in a Gasoil Hydrotreater Plant and in an Isomerization Plant to enable it to produce fuels compliant with the standards set by law. These plants started operations in the first quarter of 2005 at an investment cost of US$100 million.

Clean Water Act. Signed last March 2004, this law embodies a water pollution control policy to cover all water resources, such as inland surface waters, groundwater, estuaries, and coastal and marine waters. Compliance with effluent standards could entail additional investments in wastewater treatment facilities to comply with stringent limits on discharges.

Increase in Value Added Tax (VAT) Rate. The VAT rate on crude and petroleum products was increased from 10% to 12% beginning February 1, 2006. Higher taxes are seen to weigh on demand.

Alternative Indigenous Fuels. Government's Alternative Fuels Program promotes the use of bio-fuels such as biodiesel, ethanol, natural gas and autogas to reduce dependence on imported fuel and pollution. The Bio-Ethanol Bill proposes a 5% ethanol blend in all gasoline within two years from the law's effectivity and a 10% blend by the end of the fourth year.

(xii) Estimate of the amount spent during each of the last three fiscal years on research and development activities:

Every initiative or program the company undertakes would have a research and development aspect to it but it is not always a distinct component. Often, this element is integrated into the other aspects or operational levels of our program.

(xiii) Costs and effects of compliance with environmental laws

Compliance with the various environmental laws like the Clean Air Act and Clean Water Act, etc. will definitely entail costs and additional investments on the part of the company which will in turn result in higher production costs and operating expenses.

(xiv)Total number of employees

As of December 31, 2005, the company's total number of employees was 1,232 which is broken down as follows: Chairman, President, five (5) Vice Presidents, 771 Managerial, Professional and Technical (MPT) employees, and 454 Rank and File employees. It has no plans of increasing its workforce by a significant number for the ensuing 12 months.

Petron has Collective Bargaining Agreements with its three unions, namely: (a) Bataan Refinery Union of the Philippines (BRUP); (b) Petron Employees Labor Union (PELU); and (c) Petron Employees Association affiliated with the National Association of Trade Unions (PEA-NATU). The CBA with BRUP covers the period May 1, 2004 to December 31, 2007. For PELU, the CBA is in effect from July 1, 2004 to December 31, 2007. The CBA with PEA-NATU expired last December 31, 2005 and it is going to be renewed until December 31, 2008.

No strikes occurred for the past three years. However, the BRUP filed a Notice of Strike on August 4, 2003 concerning union leave; appointment in an acting capacity or promotion of a union officer to an MPT position; reclassification of some rank and file positions to MPT positions; assumption by an MPT employee of positions reserved for rank and file employees; and work hours of employees rendering work several hours prior to the end of their second rest day. The matter was resolved by the National Labor Relations Commission (NLRC) in favor of the company. Another Notice of Strike was filed by the same union with the National Conciliation and Mediation Board at its Regional Office in San Fernando, Pampanga on July 6, 2005. The complaint was about unfair labor practices of erosion of the bargaining unit, union busting and arbitrary dismissal. The allegation of the union followed after the completion of the Refinery's Offsites Automation Project. This project included the installation of labor-saving devices and as a natural consequence, some positions were declared redundant. On July 11, 2005, the Secretary of the Department of Labor and Employment certified the dispute for compulsory arbitration by the National Labor Relations Commission (NLRC) and indicated that any strike or lockout is prohibited and that the employees were directed to return to work in case the strike is carried out.

In addition to the statutory benefits, the company provides hospitalization insurance wherein both the employee and the company share in the payment of the insurance premium; life insurance; vacation, sick and emergency leaves; computer, company and emergency loans subject to applicable interests; and provident fund wherein the company matches the contribution of the employee.

Major Risks Involved

Risk Management Framework & Process

Petron Corporation follows an enterprise-wide risk management framework for identifying, mapping and addressing the risk factors that affect or may affect its businesses.

The Company's risk management process is a bottom-up approach, with each division mandated to conduct regular assessment of its risk profile and formulate action plans for managing identified risks. The results of these activities flow up to the Management Committee and eventually, the Board through the Company's annual Business Planning process and quarterly divisional Management Reviews.

Oversight and technical assistance is likewise provided by corporate units with special duties such as the Financial Analysis, Planning & Risk Management Department, the Management Investment Committee, the Health, Safety and Environment Management Committee and the Internal Audit Department.

Major Risks

The Company classifies a risk as major if it is assessed to have both a relatively high probability of occurring and a substantial adverse impact on the Company. The major risks that the Company managed in 2005 were substantially the same as those in the previous year since there were no fundamental changes in the nature of the Company's operations. These risks were the following:

- Foreign exchange risk arising from the difference in the denomination of majority of revenues (i.e., pesos) against that for the bulk of costs (US dollars). Changes in the foreign exchange rate would result in the revaluation of key current assets and liabilities, and could subsequently lead to financial losses for the Company.
- The risk of substantial disruptions in the Company's operations caused by accidents, process or machinery failure, human error or adverse events outside of human control. These disruptions may result to injury or loss of life, as well as financial losses should these disruptions lead to product run-outs, facility shutdown, equipment repair or replacement, insurance cost escalation and/or unplanned inventory build-up.
- Profit margin and cash flow risk arising from fluctuations in the relative prices of input crude oil and output oil and petrochemical products. Changes in output and input prices, particularly when mismatched, may produce significant cash flow variability and cause disruptions in the Company's supply chain, as well as higher financing expenses.
- Regulatory risk, arising from changes in government policies and regulations that may adversely affect the financial viability of the Company, either directly or indirectly.

The Company has determined that none of the risk factors faced by any of its subsidiaries would be a major risk - these have either a low probability of occurring and/or has insignificant potential impact to Petron. Thus, subsidiary-specific risks were considered in the Company's risk management process but since these are relatively minor, have not been included in this report.

Management of Major Risks

- Foreign exchange risk
    - The Company hedges its dollar-denominated liabilities using forwards and the generation of dollar-denominated sales. It avoids the creation of risk from derivative speculation by limiting the use of forwards to 100% of the value of the underlying dollar-denominated liabilities net of dollar-denominated assets.
    - An SAP-based financial software program is used to track dollar-denominated assets and liabilities on a daily basis and the resulting potential foreign exchange loss caused by these. This allows almost real-time awareness and response to contain losses posed by foreign exchange exposure.

- Risk of operational disruptions
    - The risk of operational disruptions is most relevant to the Company's refining unit since disruptions in the Refinery can have severe and rippling effects.
    - The Refinery Division has been implementing programs designed to directly address the avoidance of operational disruptions through effective maintenance practices and the inculcation of a culture of continuous improvement.
    - The Company has a corporate-wide safety program that likewise addresses the risk of operational disruptions.

- Profit margin and cash flow risk
    - Margin hedging strategies are used for some dollar-based contracts in order to eliminate the risk of profit margin compression due to changes in crude and product prices. A margin hedge simultaneously fixes the future dollar prices of Dubai crude oil and that of a selected product (contracted to be sold at the future date) manufactured from the crude.
    - The Company endeavors to arrange long-term contracts for some of its fuel and petrochemical products whenever these are financially attractive. Long-term sales contracts provide a partial hedge on future cash flow uncertainty.
    - The Company makes use of a cash flow projection software that enables it to proactively respond to potential future cash flow imbalances. It likewise maintains access to credit lines in excess of typical requirements so that funds can be readily tapped in case of a cash flow squeeze.

- Regulatory risk
    - The Company maintains strong lines of communication with its various counterparties in government and in the public arena, in both local and national levels. The Company uses these lines of communication to identify potential risk factors and respond to these in a proactive manner.
    - The risk of non-compliance to environmental standards pertaining among others to sulfur content in diesel and lead in gasoline as mandated by the Clean Air Act was virtually eliminated with the Company's US$100 million investment in an LVN Isomerization Unit and a Gas Oil Hydrotreater. These units became operational in 2005.

(B) Description of Property

Petron owns the largest petroleum refinery complex in the Philippines located in Limay, Bataan. This refinery has a crude distillation capacity of 180,000 barrels per day (BPD). It has three Crude Distillation Units, a Vacuum Pipestill Unit, a Thermofor Catalytic Cracking Unit, a Continuous Catalyst Regeneration Platformer Unit, a Powerformer Unit, two Naphtha Hydrotreaters, two LPG Treaters, an Isomerization Unit, a Mixed Xylene Plant, a Kerosene Merox Treater, a Kero Hydrosweetener, three Gas Oil Hydrotreater Units, a Sulfur Recovery Unit, a Caustic Regeneration Unit, Waste Water Treatment Facilities, seven Steam Generators, five Turbo Generators, Flare and Safety Relieving Facilities, Bulk Asphalt Receiving Facilities, several crude storage tanks, as well as several refined petroleum products storage tanks. It has its own piers and other berthing facilities one of which can accommodate very large crude carriers.

Petron also operates an extensive network of terminals and bulk storage and satellite facilities and LPG plants which are located in Luzon, Visayas and Mindanao. Its major terminals and plants are in Limay, Bataan; Pandacan, Manila; Rosario, Cavite; Ugong, Pasig City; Mabini, Batangas; Poro Point, San Fernando, La Union; Mandaue City; Lapuz, Iloilo City; Bacolod City; Tagoloan, Misamis Oriental; Sasa, Davao City; and Zamboanga City. Its bulk plants and sales offices in Luzon are located in Aparri, Cagayan; Calapan, Oriental Mindoro; Pasacao, Camarines Sur; Legaspi City, Albay; Puerto Princesa, Palawan; San Fernando City, Pampanga, and Navotas, Metro Manila. In the Visayas and Mindanao, the bulk plants are in Amlan, Negros Oriental; Culasi, Roxas City; Linao, Ormoc City; Anibong, Tacloban City; Isabel, Leyte; Tagbilaran City, Bohol; Iligan City; Jimenez, Misamis Occidental; Bula and Bawing, General Santos City and Nasipit, Agusan del Norte.

Petron has airport installations at the JOCASP, NAIA, Pasay City; Laoag City; Mactan, Cebu; Iloilo and Davao City. Since Petron is no longer qualified to own the parcels of land where the Bataan Refinery, the terminals, the bulk plants and the service stations are located, these lands are now leased from the Philippine National Oil Company (PNOC) and from New Ventures Realty Corporation (NVRC) on 25-year leases, which are renewable. Petron's lease agreements on those lands owned by private persons vary as to their terms and conditions, including the period of lease.

The lease agreements with PNOC is until August 2018. Lease charges on refinery facilities escalate at 2% a year, subject to increase upon reappraisal. Lease payments amounted to P 145 million in 2005 and P142 million in 2004.

Petron anticipates that it will lease desirable lots from NVRC and third parties to be developed as services stations in the next twelve months.

(C) Legal Proceedings

In 2005, Petron was involved in certain litigation some of which are material as this term is understood under the law. These are:

1. **Petron Corporation v. Commissioner of Internal Revenue and BIR Regional Director of Makati, Region 8**
   Court of Tax Appeals

Date Filed: July 7, 1998

Commissioner of Internal Revenue v. Petron Corporation
Court of Appeals
Date Filed: October 1999

Background: In April 1998, the BIR demanded from Petron payment of alleged delinquent specific taxes, inclusive of surcharges and interest for the years 1993 to 1997. Protesting the collection inasmuch as its excise tax liabilities had been fully paid through the use of validly issued Tax Credit Certificates (TCCs), Petron elevated its protest to the Court of Tax Appeals (CTA) in July 1998. The CTA ruled in favor of Petron. In 1999, the BIR Commissioner elevated this ruling to the Court of Appeals where it is still pending.

Relief sought on Appeal: The BIR seeks a reversal of the CTA decision and prays for judgment ordering Petron to pay P1,107,542,547.08 in excise tax liabilities for 1993-1997 inclusive of surcharges and interest, plus 25% surcharge and 20% annual interest from April 22, 1998.

Status: The Court of Appeals issued a resolution suspending resolution of the case until the termination of the DOF investigation on the TCCs assigned to Petron.

2. **Petron Corporation v. Commissioner of Internal Revenue (CIR)**
Court of Tax Appeals
Date Filed: July 10, 2000

Background: In November 1999, the BIR assessed a deficiency tax of P651,334,263.92 (inclusive of interest, charges and penalties) based on a batch of cancelled Tax Debit Memos (TDMs) issued against TCCs that were assigned and transferred to Petron and used by it to pay excise taxes. The Department of Finance (DOF) One-Stop-Shop and Duty Drawback Center declared that these TCCs were fraudulently issued and transferred.

Protesting this assessment, Petron filed the Petition for Review (with Motion to Stop Collection of Deficiency Excise Taxes, Surcharges and Interest) before the CTA.

Status: The case was submitted for resolution on October 29, 2003. However, on September 24, 2004, the CTA, upon motion of the CIR, and over the objection of Petron, reopened the case and set if for hearing for presentation of further evidence by the CIR. Petron has filed a Motion for Reconsideration of the reopening of the case.

3. **Petron Corporation v. Commissioner of Internal Revenue**
Court of Tax Appeals
Date Filed: April 2002

Background: In January 2002, the BIR issued a tax deficiency assessment against Petron for the total amount of P739,003,036,32 (inclusive of interest and charges) since the TCCs and TDMs used to pay the excise tax liabilities had been identified as cancelled by the DOF One-Stop-Shop and Duty Drawback Center.

In April 2002, Petron filed a Petition for Review with a prayer for a TRO with the Court of Tax Appeals.

Status: The CIR rested its case in May 2004. However, on October 4, 2004, the CTA, upon motion of the CIR, and over the objection of Petron, reopened the case and set it for hearing for presentation of further evidence by the CIR. Petron has filed a motion for reconsideration of the reopening of the case.

4. **Petron Corporation v. Mayor Tobias Tiangco**
Supreme Court, 2nd Division
Date Filed: July 17, 2003

Petron Corporation v. Mayor Tobias M. Tiangco and Municipal Treasurer Manuel T. Enriquez
Regional Trial Court of Malabon
Date Filed: May 20, 2002

Background: On March 4, 2002, the Municipality of Navotas assessed Petron the amount of P10,204,916.17 as business tax on the sale of diesel fuel at Petron depot at the Navotas Fishport. Petron questioned the assessment in an action for Cancellation of Assessment of Deficiency Taxes before the Regional Trial Court of Malabon. The RTC rendered its Decision dated 5 May 2003 dismissing Petron's complaint and ordering Petron to pay the business tax assessed.

On July 17, 2003, Petron filed a petition for review with the Supreme Court with a prayer for a temporary restraining order (TRO).

Relief sought: Reversal of the RTC Decision and the cancellation of the questioned assessment of the Municipality of Navotas.

Status: The Supreme Court issued a TRO against the Mayor and Municipal Treasurer of Navotas on August 6, 2003 which enjoined the latter from closing Petron's Navotas oil depot. The petition is now deemed submitted for decision with the parties' submission of their respective memoranda.

5. **Petron Corporation v. City Council of Manila, et al.**
Regional Trial Court of Manila
Date Filed: April 25, 2003

Background: The City Council of Manila, citing concerns of safety, security and health, passed City Ordinance No. 8027 reclassifying the areas occupied by the Oil Terminals of Petron, Shell and Caltex from Industrial to Commercial, making the operation of the Terminals therein unlawful. Simultaneous with efforts to address the concerns of the City Council with the implementation of a Scale Down Program to reduce tankage capacities and joint operation of facilities with Shell and Caltex, Petron filed this petition to annul city Ordinance No. 8027 and enjoin the City Council of Manila, as well as Mayor Joselito Atienza from implementing the same.

Relief sought: Nullification of Ordinance No. 8027

Status: On May 15, 2003, the RTC, upon agreement of the parties, issued a status quo order which prevents the respondents from enforcing the Ordinance until further orders of the Court or termination of the case. The case was referred to and is undergoing mediation before the Philippine Mediation Center.

6. **Liquefied Petroleum Gas Marketers Association**
Pilipinas Shell, Petron, and Total (Philippines)
Regional Trial Court of Pasig City
Date Filed: November 10, 2004

Background: The petitioner, a group of independent refillers engaged in the business of buying, selling, distributing, and marketing of liquefied petroleum gas (LPG), claims to have acquired ownership of defendants' LPG cylinders in good faith. LPGMA claims that it can exercise all rights of ownership over the cylinders, subject to the intellectual property rights of the defendants.

Relief sought: LPGMA prays for judgment authorizing its members to repaint/obliterate the marks on the defendants' LPG cylinders and all LPG cylinders which now or in the future may come into their possession; or to compel the parties to enter into a swapping arrangement and/or compelling the defendants to buy back the subject LPG cylinders.

Status: On July 18, 2005, the Court dismissed the petition for non-exhaustion of administrative remedies. On March 1, 2006, the RTC denied LPGMA's Motion for Reconsideration.

TCC-Related Cases

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

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

PART II – SECURITIES OF THE REGISTRANT

(A) Market Price of and Dividends on Registrant's Common Equity and Related Stockholder Matters

(1) Market Information

The registrant's common equity is principally traded at the Philippine Stock Exchange. The high and low sales prices for each period are indicated in the table below:

	Highest Close		Lowest Close	
Period	**Price**	**Date**	**Price**	**Date**
2005				
1st Quarter	4.50	09-Mar-05	3.20	03,06 Jan-05
2nd Quarter	3.75	04-Apr-05	2.95	30-June-05
3rd Quarter	3.35	12-Aug-05	2.65	04-July-05
4th Quarter	4.65	08-Dec-05	3.15	05 Oct-05
2004				
1st Quarter	3.55	13-Feb-04	2.34	05,08-Jan-04
2nd Quarter	3.40	27,28-Apr-04	2.75	01-Apr-04
3rd Quarter	3.05	01,02,06-Jul-04	2.42	24-Aug-04
4th Quarter	3.35	08-Nov-04	2.80	13,15,18-Oct-04

The total number of stockholders as of December 31, 2005 is 192,644. Price as of last trading day of the year, December 29, 2005, was P4.50 per share.

As of March 31, 2006, the total number of stockholders is 191,389 and the stock price was P4.40.

(2) Holders

List of Top 20 Stockholders
As of March 31, 2006

Rank	Name	Nationality	No. of shares	%
1	Philippine National Oil Company	Filipino	3,750,000,007	40.00
2	Aramco Overseas Company B.V.	Netherlands	3,750,000,006	40.00
3	PCD Nominee Corp.	Foreign	601,990,823	6.42
4	PCD Nominee Corp.	Filipino	505,739,442	5.39
5	Home Development Mutual Fund	Filipino	18,830,091	0.20
6	Ansaldo, Godinez & Co. Inc. FAO Mark V. Pangilinan	Filipino	8,000,000	0.09
7	Siao Tick Chong	Filipino	7,500,000	0.08
8	Ernesto Chua Chiaco&/or Margaret Sy Chua Chiaco	Filipino	6,000,000	0.06

9	Marciano V. Pangilinan	American	5,000,000	0.05
10	Aristeo Lascano Castillo	Filipino	4,145,000	0.04
11	Sonny Ico Parayno	American	2,613,000	0.03
12	Ching Hai Go &/or Martina Go	Filipino	2,500,000	0.03
13	Remington Tiu &/or Agaton Tiu	Filipino	2,500,000	0.03
14	Aristeo L. Castillo	Filipino	2,326,500	0.02
15	China Banking Corporation	Filipino	2,291,000	0.02
16	Allied Banking Corporation	Filipino	2,145,000	0.02
17	Conrado S. Chua Sr.	Filipino	2,130,000	0.02
18	Ang Ching An	Filipino	1,520,000	0.02
19	Frank Chua &/or Genevieve Lim Chua	Filipino	1,453,588	0.02
20	Vicente Hao Chin Sr.	Filipino	1,350,000	0.01

(3) Dividends

Petron's dividend policy is to declare as dividends out of the company's unrestricted retained earnings at least 25% of its unappropriated net income for the prior fiscal year, payable either in cash, property or shares. The Board shall determine, by resolution, the exact amount, date and shareholders entitled to such dividends.

On May 12, 2005, the company's Board of Directors declared a cash dividend in the amount of P0.10/share. Stockholders on record as of May 26, 2005 were paid their dividend on June 21, 2005.

The previous year, on May 19, the Board also declared a cash dividend of P0.20 per share. All stockholders on record as of June 2, 2004 were entitled to the dividend and the payment date was June 28, 2004.

(4) Sale of Unregistered or Exempt Including Securities Constituting an Exempt Transaction

The Company did not sell any securities within the past three years which were not registered under the Code nor did it sell reacquired securities or new issues or sell securities issued in exchange for property, services, or other securities, and new securities resulting from the modification of outstanding securities.

(B) Description of Petron's Shares

The registrant's securities consist entirely of common stock with par value of P1.00 per share. Total common shares are 9,375,104,497 which are also voting shares.

(C) Stock Ownership Plan

The Stock Ownership Plan (SOP), a one-time program, adopted in 1994 by PNOC, the selling shareholder in Petron's Initial Public Offering, was not a stock option plan which had to be approved by the SEC. Rather, it was a special secondary sale of Petron's shares to a selected group of persons. Entitlement of shares at the listing price of P9.00 per share was made equivalent to the employee's base pay factored by his/her service years with Petron. Petron's Executive Officers, except the Chairman, the President and the Vice President for Corporate Planning, were entitled to own Petron shares under this SOP.

PART III – FINANCIAL INFORMATION

(A) Management's Discussion and Analysis or Plan of Operation.

Financial Condition and Results of Operations

(For convenience, U.S. dollar information in the following discussion has been translated into Philippine pesos at the exchange rate of ₱ 53.062 to US$1.00, the Philippine peso - U.S. dollar rate as quoted by the Philippine Dealing System as of December 31, 2005.)

Results of Operations

2005 vs. 2004

The Company's net income climbed to ₱ 6.04 billion in 2005, recording a growth of 48% from the restated net earnings of ₱ 4.10 billion the year before.

Sales Volume for the year of 51.7 MMB showed a 1.1 MMB (2%) drop from last year's 52.8 MMB level. Domestic sales and supply sales went down by 3.2 MMB (7%) and 0.4 MMB (18%), respectively but significantly offset by the 2.5 MMB incremental volume contributed by the export market.

Sales increased by 30% (₱ 44.06 billion) to ₱ 191.49 billion from the ₱ 147.43 billion revenues in 2004. This was mainly due to the hike in MOPS prices as well as the upward adjustment in WPP to mitigate the effect of the escalation in crude prices.

Cost of goods sold went up to ₱ 176.96 billion, 31% or ₱ 41.52 billion higher than the ₱ 135.44 billion reported last year, prompted by the 40% or $13.99 escalation in FOB per barrel of crude that went into cost. The ₱ 0.97 average appreciation of the peso against dollar partly cushioned the effect of the recorded increase.

Gross margin per liter increased to ₱ 1.77 from ₱ 1.40 last year. However, gross margin rate was lower at 7.59% than the previous year's 8.13% level. This was traceable to lower margins from WPP-based sales (2005-6.79% vs. 2004-7.97%). While the average duty-paid landed cost (DPLC) that was consumed during the year escalated by 37%, Wholesale Posted Prices (WPP) increased by only 33%. On the other hand, MOPS-based prices (Domestic & Exports) rose by 35%.

Refinery operating expenses (which form part of cost of sales) stood at ₱ 3.46 billion, exceeding the ₱ 2.93 billion recorded during the same period last year by ₱ 0.53 billion. The increase from last year's level was largely driven by the provision for obsolescence made for the refinery's storehouse items as well as depreciation expenses related to the ISOM and GOHT units, both of which were commercially operational on the first half of 2005.

Selling and administrative expenses went down to ₱ 4.53 billion from prior year's level of ₱ 4.88 billion. This was mainly a result of the early adoption of the amendments to PAS 19 (Employee Benefits), specifically allowing the recognition of actuarial gains and losses outside of profit and loss statement and instead present a statement of recognized income and expenses under equity.

Net financing costs and other charges amounted to ₱ 1.86 billion, higher than last year's ₱ 1.69 billion due essentially to the increase in interest expense as the escalation in crude prices resulted in higher short-term borrowing level this year.

Provision for income tax of ₱ 2.09 billion was 58% (₱ 0.77 billion) more than the ₱ 1.32 billion a year ago on account of higher taxable income as well as the increase in corporate income tax rate from 32% to 35% effective November 1, 2005.

Basic earnings per share stood at ₱ 0.64, surpassing last year's ₱ 0.44 level by 45%.

2004 vs. 2003

Petron's restated *net income* of ₱ 4.10 billion for the year posted a 32% or ₱ 0.99 billion increase over the ₱ 3.11 billion earnings recorded during the same period last year. This was traceable mainly to higher gross margin, specifically from exports, substantially reduced by the escalation in operating charges.

Overall sales volume of 52.8 MMB was up by 6 % or 2.9 MMB from the year ago level of 49.8 MMB. The incremental volume was contributed by domestic (by 5.6 MMB) and supply sales (by 0.4 MMB), partly reduced by the decline in export sales (by 3.0 MMB). The improvement in domestic market was attributable to the growth in Industrial Civil Trade (by 3.4 MMB) boosted by the climb in retail (by 1.1 MMB) and NPC sales (by 1.1 MMB).

Net revenues reached ₱ 147.43 billion, surpassing the previous year's level by 33% due essentially to higher MOPS-based prices, which rose by an average of 29% complemented by the 26% average increase in domestic Wholesale Posted Price (WPP) as well as the 6% growth in sales volume.

Cost of goods sold surged to ₱ 135.44 billion from the previous year's ₱ 101.35 billion traceable primarily to the combined effects of the $7.88/bbl escalation in FOB of crude that went into production, the $0.74/BBL hike in freight cost and the ₱ 1.83 average deterioration of the peso against the US dollar.

Gross margin of ₱ 11.99 billion showed an improvement of 28% (₱ 2.61 billion) from the ₱ 9.38 billion level last year. However, gross margin rate was lower at 8.1% from the previous year's 8.5% even with the ₱ 3.58 per liter average hike in selling price as the average duty-paid landed cost of crude processed during the period escalated by ₱ 3.46 per liter.

Selling and administrative expenses stood at ₱ 4.88 billion, 27% (₱ 1.04 billion) higher than the recorded operating expenses in 2003 of ₱ 3.84 billion driven by the following:

- Materials and Supplies rose by ₱ 214 million as the company bought more cylinder at higher prices this year. Also, write-on of cylinder deposits was higher in 2003 compared to 2004 (₱ 69 million – 2004 vs. ₱ 224 million - 2003).

- Advertising expenses increased by ₱ 176 million as a result of more aggressive marketing and promotional activities.

- Recognized ₱ 154 million in REAP related expense as mandated under IAS 19 which provides for the accrual of the benefit earned by the employee in the period it is earned rather than when paid or payable.

- Set up of allowance for uncollectible trade and non-trade accounts amounting to ₱ 162 million.

Financing and other charges increased to ₱ 1.69 billion from last year's level of ₱ 1.43 billion basically due to higher hedging cost and forex losses attributed to the escalation in crude and imported fuel prices as well as the ₱ 1.83 average deterioration of the peso against the dollar.

Financial Condition

2005

Petron's consolidated resources as of December 31, 2005 reached ₱ 71.08 billion, 13% or ₱ 7.95 billion higher than end-December 2004 level of ₱ 63.13 billion. The company's debt ratio improved to 0.60 as of December 31, 2005 on account of higher earnings. Current ratio stood at 1.3, better than 1.2 last year.

Financial assets through profit or loss of ₱ 144 million pertain to marketable equity securities and proprietary membership shares which are presented separately as required under PAS 32 (Financial Instruments: Disclosure and Presentation).

Available-for-sale investments (current and noncurrent) of ₱ 455 million consisted of investments in government securities of Petrogen which are deposited with the Insurance Commission in accordance with the provisions of the Insurance Code, for the benefit and security of policyholders and creditors of Petrogen.

Receivables-net went up by ₱ 2.30 billion (20%) on account primarily of higher sales posted for exports and industrial accounts.

Inventory increased by ₱ 4.60 billion traceable to:

- Escalation in finished product cost (12/05 - ₱ 23.25 P/li. vs. 12/04 - ₱ 19.18 P/li.) equivalent to ₱ 2.67 billion.

- Increase in crude cost (12/05 - ₱ 19.85 P/li. vs. 12/04-₱ 15.08 P/li.) resulting in a ₱ 2.89 billion increment.

- Tempered by the drop in inventory level of both finished products (0.17 MMB) and crude (0.03 MMB) translating to ₱ 0.71 billion

Other current assets increased by ₱ 0.51 billion (64%) influenced essentially by the transitional input VAT resulting from the imposition of VAT on crude and finished products under the new E-VAT law which was implemented starting November 1, 2005.

Investment Properties of ₱ 0.21 billion pertained to portions of the building being leased to third parties as well as parcels of land of NVRC intended for service stations which were reclassified from property, plant and equipment in compliance with PAS 40 (Investment Property).

Other noncurrent assets went down by ₱ 0.09 billion (7%) on account primarily of the reclassification of investment in shares of stock and notes/bonds to fair value through profit or loss (FVPL) and available-for-sale (AFS), respectively.

Supplier's credits and *short-term loans* increased by ₱ 4.71 billion (19%) triggered by escalating prices of crude and finished products.

Accounts payable and accrued expenses were reduced by ₱ 0.27 billion (5%) due mainly to retention fees paid to contractors for completed projects/contracts.

Long-term debt went down to ₱ 5.03 billion from year-end 2004 balance of ₱ 7.23 billion as the portion of long-term loans obtained from Citibank, Landbank and NORD that will mature in a year's time was taken up under current liabilities. There was also no long-term loan availment in 2005.

Retained earnings-appropriated increased to ₱ 11.65 billion from the December 2004 level of ₱ 6.91 billion on account of the provisions made for the 2006 capital program. As a result, the increase in *retained earnings-unappropriated* was trimmed down to ₱ 0.73 billion.

Other reserves of ₱ 128 million was traceable largely to net actuarial gain recognized directly to equity.

2004

Total restated resources as of December 31, 2004, aggregated ₱ 63.13 billion, 23% or ₱ 11.93 billion higher than the ₱ 51.20 billion posted in 2003. While Petron's debt ratio deteriorated from 0.61 as of December 31, 2003 to 0.64 as a result of the increases in both short and long-term loans used to finance importations and capital projects, current ratio improved to 1.2 from 1.1 in 2003.

Cash and cash equivalents increased by ₱ 906 million or 28% emanating primarily from month-end collections from customers.

The upward oil price adjustments coupled with higher sales volume accounted primarily for the ₱ 2.27 billion or 24% upturn in *receivables-net*.

The build-up in *inventories* by ₱ 6.74 billion or 43% was attributable essentially to the retroactive effect of the adoption of PAS 2 (Inventories) which prohibits the LIFO method of costing petroleum products. Higher crude and finished product prices also contributed to the increment.

The additional allowance provided by the company for the decline in value of investment for All Asia accounted mainly for the ₱ 59 million decrease in *Investments-net.*

Property, plant and equipment grew by ₱ 0.95 billion or 4% on account largely of the capital expenditures for Gasoil Hydrotreater Plant and Isomerization Unit. This is net of the ₱ 2.2 billion deduction in PPE brought about by the retroactive effect of the adoption of PAS 21 (Effects of Changes in Foreign Exchange Rates) which prohibits the capitalization of foreign exchange losses.

Other non current assets climbed to ₱ 1.27 billion from ₱ 80 million in December 2003 brought about principally by the recognition of transitional pension asset which resulted from the retroactive application of PAS 19 (Employee Benefits).

Short-term loans increased by ₱ 3.09 billion or 20% due mainly to peso and dollar loans obtained from banks to finance importation of crude and petroleum products.

Liabilities for crude oil and petroleum product importation decreased by ₱ 432 million due to lower crude purchases in December 2004 (by 261 MB).

Accounts payable and accrued expenses increased by ₱ 1.12 billion or 28% on account largely of retention payable related to the on-going construction of major capital projects in the refinery as well as liabilities to local suppliers and contractors.

Income tax payable rose to ₱ 278 million since prior years' NOLCO and MCIT were already fully applied in 2003.

The *current portion of long-term debt* totaling ₱ 1.60 billion was more than twice the end-December 2003 level of ₱ 712 million on account of long-term loans obtained from Landbank and Citibank which will be due for payment in a year's time.

Non-current liabilities and deferred credits rose by ₱ 4.35 billion or 89% on account principally of the outstanding dollar denominated loan ($100 million) obtained from NORD for major capital projects.

Increase in *retained earnings-unappropriated* by ₱ 960 million pertained essentially to the ₱ 4.10 billion earnings for the period ended December 2004 less dividends declared of ₱ 1.88 billion and appropriation for future capital projects of ₱ 1.36 billion. Retroactive application of the new Philippine Accounting Standards (PAS) also contributed to the increment.

Cash Flows

2005 vs 2004

Petron registered an operating cash inflow of ₱ 1.96 billion, significantly higher than the YTD December 2004 level of ₱ 191 million owing mainly to better earnings this year.

2004 vs 2003

Petron registered a lower operating cash inflow of ₱ 191 million this year compared with the ₱ 2.91 billion last year driven principally by the build-up in operating assets.

Financial Condition

Item 7. Financial Statements	2005	(As Restated) 2004
b) Cash and Cash Equivalents		
Cash in bank (Peso)	2,821	2,348
Cash in bank ($)	755	1,082
Marketable securities ($)	495	674
Total	**4,071**	**4,104**
c) Accounts Receivables-Others		
Duty drawback, tax credits & other claims	2,126	1,456
Borrow and loan	129	93
Unapplied withholding taxes/ tax certificates	-	30
Others	757	748
Total	**3,012**	**2,327**
d) Selling and Administrative Expenses		
Depreciation and amortization	876	847
Employee costs	1,023	1,225
Purchased services and utilities	748	734
Maintenance and repairs	567	629
Advertising	398	403
Rent expense	306	271
Materials and office supplies	281	260
Taxes and licenses	102	177
Provision for doubtful accounts	106	162
Others	120	169
Total	**4,527**	**4,877**

e) Other Income, Interest Expense and Others		
Interest income	317	344
Interest expense	(2,091)	(1,675)
Rent income	280	274
Derivatives net mark to market (MTM) gain (loss)	(260)	-
Foreign exchange gain (loss)	56	(259)
Reversal of allowance (provision) for decline in value of investments	14	(91)
Miscellaneous	(176)	(280)
Total	**(1,860)**	**(1,687)**

Top Five (5) Key Performance Indicators

Ratio	Dec-05	(As Restated) Dec-04
Current Ratio	1.3	1.2
Debt Equity Ratio	1.5	1.8
Return on Equity (%)	24.2	19.5
Debt Service Coverage		
Citibank	1.9	1.7
NORD	1.8	1.6
Tangible Net worth	₱ 27.6B	₱ 22.3B

Current Ratio - Total current assets divided by total current liabilities.
This ratio is a rough indication of a company's ability to service its current obligations. Generally, the higher the current ratio, the greater the "cushion" between current obligations and a company's ability to pay them.

Debt Equity Ratio - Total liabilities divided by tangible net worth.
This ratio expresses the relationship between capital contributed by creditors and that contributed by owners. It expresses the degree of protection provided by the owners for the creditors. The higher the ratio, the greater the risk being assumed by creditors. A lower ratio generally indicates greater long-term financial safety.

Return on Equity - Net income divided by average total stockholders' equity.
This ratio reveals how much profit a company earned in comparison to the total amount of shareholder equity found on the balance sheet. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. For the most part, the higher a company's return on equity compared to its industry, the better.

Debt Service Coverage - Free cash flows add available closing cash balance divided by projected debt service.
This ratio shows the cash flow available to pay for debt to the total amount of debt payments to be made. It also measures the company's ability to settle dividends, interests and other financing charges.

Tangible Net Worth - Net worth minus intangible assets.
This figure gives a more immediately realizable value of the company.

Exchange Rate Volatility

Any volatility in the exchange rate implies cost uncertainties for Petron, both in terms of operating and capital expenses. As the peso depreciates, the landed cost of imported crude oil and products, and of capital equipment increases.

The peso was the best performing currency in Asia in 2005. It appreciated by 4% from 55.8 in January to 53.6 in December. The local currency drew its strength from record inflows of dollars from Overseas Filipino Workers (OFWs) and portfolio investments, improving outlook on government's fiscal position and the general weakness of the US dollar against regional currencies.

The peso gain however, has its positive and negative side to it. On one hand, Philippine exports become less competitive in the international market as they become relatively more expensive. On the other hand, inflation is tempered by cheaper imports, especially oil and other raw materials used by the manufacturing sector. An appreciating peso is particularly beneficial to companies that import a lot of their raw materials.

Known Trends

Higher crude prices

Oil prices remained high throughout 2005. The rise in crude oil price which started in the second half of 2004, continued well into 2005 on account of high global oil demand (particularly from the US, China and India), amidst marginal supply increases, geopolitical factors, tightening refining capacity and weather disturbances. Increased speculative activity likewise raised the premium on oil prices. And in the latter part of 2005, consumers also had to contend themselves with the price increase associated with the imposition of VAT on oil products.

Inflation and Interest Rates

The rapid rise in oil prices which started in the latter part of 2004 extended itself to much of 2005 pushing inflation to 7.6% from just 6.0% in 2004. The average inflation would have been higher were it not for the high base of prices in the second half of 2004.

The rise of the 91-day Treasury-Bill to keep up with inflation did not happen. Moreover, rates fell from 7.3% in 2004 to 6.2% in 2005. Throughout the year, inflation remained above the 91-day Treasury-Bill rates reflecting negative returns on short-term peso investments. The excess liquidity in the market caused by weak private credit demand had nowhere to go but government securities. Together with government's decision to reduce its short-term borrowings, interest rates on Treasury Bills were bid down.

Any events that will trigger direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation.

TCC Related Cases

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

In November 1999, the Department of Finance (DOF) Center ExCom cancelled Tax Debit Memos (TDMs) worth ₱ 475 million, the related TCCs and their assignments. The BIR implemented this with a letter of assessment worth ₱ 651 million deficiency taxes (inclusive of interest and charges) for the years 1995 to 1997, as a result of the cancellation. The Company contested on the grounds that the assessment has no factual and legal basis and that the cancellation of the TDMs was void. The Company elevated this protest to the CTA on July 10, 2000 where the case is still pending.

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

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

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

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

Pandacan Terminal Operations

The City Council of Manila (City Council), citing concerns of safety, security and health, passed City Ordinance No. 8027 reclassifying the areas occupied by the Oil Terminals of Petron, Shell and Caltex from Industrial to Commercial, making the operation of the Terminals therein unlawful.

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

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

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

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

Simultaneous with the Scale Down Program, Petron filed a petition with the Regional Trial Court (RTC) to annul the City Ordinance and enjoin the City Council of Manila, as well as Mayor of Manila, from implementing the same. The RTC issued a status quo order which prevents the respondents from enforcing the Ordinance until further orders of the Court or termination of the case. The case has been referred to and is undergoing mediation before the Philippine Mediation Center.

Navotas Business Tax

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

Ownership of LPG Cylinders in the Market

Liquefied Petroleum Gas Marketers Association (LPGMA), a group of independent refillers of LPG claims to have acquired ownership of LPG cylinders of Petron, Pilipinas Shell and Total Philippines in good faith. LPGMA claims it can exercise all rights of ownership over the cylinders, praying judgment from the RTC of Pasig City authorizing its members to repaint/obliterate the marks on the oil companies' LPG cylinders and all LPG cylinders which now or in the future may come into their possession; or to compel the parties to enter into a swapping arrangement and/or compelling the oil companies to buy back the cylinders.

On July 18, 2005, the RTC dismissed the petition for non-exhaustion of administrative remedies. LPGMA's Motion for Reconsideration is pending resolution by the RTC. On March 1, 2006, the RTC denied LPGMA's Motion for Reconsideration.

All material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the company with unconsolidated entities or other persons created during the reporting period.

There are no off-balance sheet transactions, arrangements and obligations with unconsolidated entities or persons during the reporting period.

Audit and Audit-Related Fees

For the annual review of the financial statements and other assurance related services, the audit fees in 2004 and 2005 were P2.2 million and P2.8 million, respectively.

Engagement of external auditor's services is bidded out among qualified auditing firms. For audit of annual financial statements, award is endorsed by the Board Audit Committee and approved by the company's shareholders during its annual meeting. Award of other services are approved by the Audit Committee as endorsed by the company's Internal Audit Department.

Material Commitments for Capital Expenditure

The company's proposed capital program for 2006 amounts to ₱ 4.2 billion, ₱ 3.7 billion (88%) for major capital projects, and ₱ 494 million for miscellaneous projects. Major capital projects include the following:

1. Engineering, Procurement and Construction (EPC) of the BTX Facilities Project. The project is expected to capture the potential of producing high-valued petrochemical feedstocks from the refinery. Total investment for the project is estimated at ₱ 3.0 billion.

2. Reseller Funds Pool. The ₱ 319 million project will cover civil works, pumps, underground tanks, various service station equipment and signages for the construction of new stations. It also includes rehabilitation of existing stations and installation of point-of-sale system.

Other major capital projects include various enhancements in supply/ distribution facilities estimated at ₱ 416 million.

To the extent possible, all capital projects would be funded by internally generated cash. The company may resort to medium or long-term financing in cases when additional cash would be necessary.

In February and April 2006 meetings, the Board respectively ratified the contract award for the Engineering, Procurement and Construction (EPC) of the PetroFCC project in favor of contractor Daelim in the total amount of US$178.4 million and authorized Management to borrow up to $200 million or peso equivalent to finance the planned investments including the BTX facilities project.

(B) Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

There are no changes in and disagreements with Accountants on Accounting and Financial Disclosure.

PART IV – MANAGEMENT AND CERTAIN SECURITY HOLDERS

(A) Directors and Executive Officers of the Registrant

Described below are the business experiences of the Company's Directors and Executive Officers for the past five (5) years.

(1) Directors

Nicasio I. Alcantara, Filipino, 63 years old, has been a Director and the Chairman of Petron Corporation since July 30, 2001. Currently, he is also Chairman (without voting rights) of the Board Compensation Committee and a member of the Board Nomination Committee. Before joining Petron Corporation, he was Chairman and/or President of various corporations of the Alcantara Group of Companies, such as Alsons Power Holdings, Inc., Alson Power Holdings Corp., Southern Philippines Power Corp., Western Mindanao Power Corp., Northern Mindanao Power Corp., Alto Power Corporation, MADE (Market Developers), Inc. and Conal Holdings Corporation. He was a Director of United Pulp and Paper Co. from May 1986 to 2003. Mr. Alcantara is currently a Director of Alsons Corporation, Conal Corporation, Alsons Insurance Brokers Corp., Sarangani Agricultural Co., Inc., Alsons Aquaculture Co., Inc., Aquasur Resources Corporation, Finfish Hatcheries, Inc., Buayan Cattle Co. Inc., Alsons Development & Investment Corp., Alsons Land Corporation, Lima Land, Inc., C. Alcantara & Sons, Inc., Refractories Corp. of the Philippines, Bancasia Capital Corporation, Bank One Savings & Trust Corporation, The Philodril Corporation and T'boli Agro Industrial Corporation. He also serves as a member of the Boards of Trustees of the Philippine Institute of Petroleum (PIP), the Philippine Business for Social Progress (PBSP) and the Junior Achievers of the Philippines (JAPI). He earned his Business Administration degree from the Ateneo de Manila University and his Masters degree in Business Administration from Sta. Clara University, California.

Khalid D. Al-Faddagh, Saudi Arabian, 50 years old, has been a Director since July 2001 and was elected President since July 29, 2003. He was elected President and Chief Executive Officer last July 26, 2004. Currently, he is a member of the Board Compensation Committee (without voting rights) and the Board Nomination Committee. Mr. Al-Faddagh has more than 20 years experience in the oil industry and held various professional and management positions in Saudi Aramco. He was the Manager for Facilities Planning Department in Saudi Aramco from January 2001 to July 2003. Mr. Al-Faddagh was also the Manager for the Abqaiq Plants Maintenance Department of Saudi Aramco from July 1983 to January 2001. He has a Doctorate Degree in Mechanical Engineering from the Imperial College, London University and attended several executive programs including a recent one at Harvard Business School.

Basil A. Abul-Hamayel, Saudi Arabian, 41 years old, has been a Director of the company since July 2004 and currently, a member of the Board Audit Committee. Mr. Abul-Hamayel has 24 years of service with Saudi Aramco and has occupied several professional and managerial positions. He is now the Manager for Corporate Finance, Insurance and Asset Management Department in Saudi Aramco. Prior to this position, Mr. Abul-Hamayel was Petron's Vice President for Corporate Planning Division from April 2004 up to September 2005 and at the same time a Director of Petron Foundation, Inc., Petron Marketing Corporation and Petron Freeport Corporation. Prior to his assignment in Petron, he was the leader of the finance team involved in negotiating, on behalf of the Government of Saudi Arabia, the upstream gas exploration concessions with the International Oil Companies (IOCs) which function he held from September 2001 to October 2003. He was also seconded to the World Bank Group in Washington D.C., from 1999 to 2001, where he was a Senior Financial Specialist in the Oil, Gas and Chemicals Division. He holds an undergraduate degree in economics from the University of Texas at Austin (1987) and an MBA in Finance from the Massachusetts Institute of Technology (MIT) Sloan School of Management (1996).

Herminio S. Aquino, Filipino, 56 years old, has been a Director of the company since November 2004 and currently a member of the Board Audit Committee. At present, he is the Chairman of Trackworks, Inc., Interconsult (Asia Pacific), Inc. and 7-Series, Inc. He was the Vice Governor of the Province of Tarlac from 1998-2001 and was Congressman for the 3rd District of Tarlac for three terms from 1987-1998. While in Congress, he was Chairman of the Committee on Energy from 1987-1992 and Vice-Chairman from 1992-1998 and was a member of various other Committees. He also worked under the Executive Branch as Deputy Executive Secretary for Human Settlements and Chairman of various government agencies such as Ministry of Human Settlements, Housing and Urban Development Coordinating Council, Bagong Kilusang Kabuhayan at Kaunlaran and Human Settlements Development Corporation. Mr. Aquino holds a Bachelor of Arts degree, major in Economics from the Ateneo de Manila University and a Masters in Business Administration from the Asian Institute of Management.

Alberto A. Pedrosa, Filipino, 73 years old, has been a Director of the company since March 2005. Presently, he sits as member of the Board Nomination Committee. He is currently the Chairman and Publisher of Republika, a newsmagazine focused on the 42,000 barangays in the country. He is also the Chairman of People's Initiative for Reform, Modernization and Action (PIRMA). He was a Member of the Board of Directors of Philippine Deposit Insurance Corporation and former Ambassador Extraordinary and Plenipotentiary to Belgium, Luxembourg and the European Union from 1992-1995. He also worked as Chairman of the ASEAN Brussels Committee from September 1993-March 1994, Adviser of Philippine Delegation on the 12th ASEAN-EC JCC, Brussels in October 1995, Member of delegation, ASEAN-EU Ministerial Meeting in Karlaruhe, Germany in September 1994 and was Secretary of the Confederation of Philippine Embassies in Europe. He was former Chairman of the Confederation of Filipino Overseas Organizations, London. Mr. Pedrosa was also a trainee in the Foreign Department, Bankers Trust Company; in ocean traffic management and operations, and in sugar trading and brokering under different New York firms. Mr. Pedrosa holds a Bachelor of Arts degree, major in Economics from the University of the Philippines. He also took post-graduate studies at Sciences-Po in Public Economics at the University of Paris and summer seminar in Luxembourg on the European Economic Community, Faculte' d'Economie Comparee, Luxembourg.

Khalid G. Al-Buainain, Saudi Arabian, 46 years old, has been a Director of the company since July 29, 2003. He is a member of the Board Compensation Committee and is currently the Vice-President for Refining of Saudi Aramco since June 2003. Prior to this appointment, from June 2001 to May 2003, he served as Vice President of Medical Services. From May 1999 to May 2001, he was in charge of Saudi Aramco Affairs, first as Executive Director and later as Vice President. He is presently the Chairman of Luberef and a member of the Saudi Aramco Executive Advisory Committee. He has a Bachelor of Science degree in Mechanical Engineering from the University of Petroleum and Minerals and attended the Executive Program at the Harvard Business School in 1999.

Bernardino R. Abes, Filipino, 75 years old, has been a Director of the company since July 2001 and is presently a member of the Board Compensation Committee. At present, he holds the position of the Chairman of the Government Service Insurance System, following a three-year term as Chairman of the Social Security Commission. He was also a Director of Union Bank of the Philippines, First Philippine Holdings, Philex Mining Corporation, Belle Corporation and Clark Development Corporation. He held the position of Presidential Adviser on Legislative Affairs and Head, Presidential Legislative Liaison Office in 2001. Other positions include: Consultant for the Philippine Senate (1992 to 1993), Direction for Bureau of Labor Relations (1957-1961), Secretary of Labor (1962-1964), Administrator and Chairman of SSS (1963-1965). He graduated from the University of Santo Tomas with a Bachelor of Laws degree.

Jose Luis U. Yulo, Jr*., Filipino, 58 years old, has been an Independent Director since July 2001. He is a member of the Board Compensation Committee and Chairman of both the Audit and Nomination Committees. He is currently the Chairman of Insurance of the Philippine Islands Co., Inc., President of Metro Cebu Public Savings Bank and President of Centrex Corporation, among others. Mr. Yulo held the position of President and CEO of the Philippine Stock Exchange until May 2000. Other positions include: President & Co-Founder of the Philippine Chamber of Commerce & Industry (PCCI), President/CEO of the Philippine International Trading Corporation (PITC), and several directorships in the field of mining, sugar, refinery and banking. As Founding Member of the Asia Pacific Business Advisory Council (ABAC), he co-chaired its Cross-Border Flows Committee and helped establish the APEC Business Travel Card. He is also a Co-Founder of the Philippine Center for Trade & Exhibits (Philcite). Mr. Yulo holds a certificate from the Advanced Management College of Stanford University, U. S. A. and has a Master in Business Management degree from the Asian Institute of Management.

Douhan H. Al-Douhan, Saudi Arabian, 70 years old, has been an Independent Director since July 2001. He is a member of the Audit and Nomination Committees. He has been the Managing Director of Randa Trading & Construction in Saudi Arabia since 2004. He is also a Partner and a member of the Board of Directors of Gabas Alkhaleej, also in Saudi Arabia since 2004. He retired as Executive Director of Management Services Organization on December 31, 1995. He was formerly Assistant Secretary to the Board of Directors of Saudi Aramco. He also held several management positions in the Loss Prevention Department, Oil Producing Operations and Maintenance Department & Government Affairs Organization. He was actively involved in several committees like the Corporate Executive Compensation Committee, Management Development & Organization Committee, Services Review Committee, Ethics & Conflict of Interest Committee, Donation Committee, Saudi Manpower Committee & Corporate Task Force for Manpower Review. Mr. Al-Douhan has a Bachelor of Science degree in Engineering Technology with emphasis in Manufacturing from the Memphis State University, Tennessee, U.S.A.

Ahmad O. Al-Khowaiter, Saudi Arabian, 39 years old, was elected as Director on July 25, 2005 and is a member of the Board Compensation Committee. He is at present, the Manager of Facility Planning of Saudi Aramco. Mr. Al-Khowaiter has been a Superintendent in Haradh Gas Plant from 2002 to 2003 and in Hawiyah Gas Plant Engineering Division from 2000 to 2002. He has been a Senior Project Engineer in Exploration Application Services Department from 1997 to 2000. He has a Bachelor of Science degree in Chemical Engineering from King Fahad University of Petroleum & Minerals in Dhahran, Saudi Arabia. He received his M. S. in Chemical Engineering from the University of California and is presently taking an MBA course from the Massachusetts Institute of Technology (MIT) Sloan School of Management.

(2) Other Executive Officers

Sulaiman M. Ababtain, Saudi Arabian, 39 years old, was appointed Officer-in-Charge on September 7, 2005 and elected Vice President for Corporate Planning on November 30, 2005. He has 17 years experience with Saudi Aramco during which he held several managerial positions in Hydrocarbon Supply Planning, Operations, and Sales & Marketing. Before joining Petron, Mr. Ababtain was the Division Head of the Global Crude Oil Sales Coordination Division of Crude Oil Sales & Marketing Dept. He also headed both the Maintenance and Operations Divisions of Northern Area Pipelines Department; as well as Gas & NGL, Oil, and Terminal Divisions of Oil Supply Planning & Scheduling Department (OSPAS). He had also worked with upstream operations as Superintendent of Central Arabia Producing Division. His major work highlights include: having coordinated the introduction of AXL Crude at Juaymah Terminal, the introduction of Sales Gas into the 48" East/West pipeline to Yanbu Industrial Area, and improving the time in port and shiphandling performance at RT & Juaymah Terminals. He has a Bachelor's degree in System Engineering (1988) from King Fahad University of Petroleum & Minerals at Dhahran, Saudi Arabia and a Masters degree in Industrial Engineering (1996) from Purdue University, Indiana, USA.

* Resigned effective March 1, 2006

Jose K. Campos, Jr., Filipino**,** 59 years old, has been the Vice President for Marketing since April 15, 2002 and earlier was the Vice President for Supply & Operations, from June 2001 to April 2002. He started working for the Company (then known as Esso Philippines, Inc.) on October 20, 1969 as an Analyst in the Marketing Economics & Research Department. He transferred to Industrial Trade in June 1972 as an Account Executive and became Government Sales Supervisor in April 1974. He was named Industrial Sales Manager for Visayas and Mindanao, based in Cebu, in May 1977, and returned to Manila as District Sales Manager for Metro Manila in October 1984. He became Reseller Sales Manager for Luzon in 1986 until he assumed stewardship of Industrial Trade in November 1991. He was Reseller Trade Manager from January 1995 until he was appointed Manager of Strategic Planning in January 1999. He is now concurrently Vice President and Chief Operating Officer of two subsidiaries, Petron Marketing Corporation and Petron Freeport Corporation. He has been with the Company for 36 years, and has attended various management courses both in the Philippines and abroad. He has a Bachelor of Science degree in Economics from the Ateneo de Manila University**.**

Antonio G. Pelayo, Filipino, 50 years old, has been the Vice President for Finance and Subsidiaries since May 7, 2002. He is also a Director and President/CEO of New Ventures Realty Corporation and Las Lucas Development Corporation, an NVRC subsidiary ; Director and Vice-President of Petrogen Insurance Corporation; Director of Petron Marketing Corporation and Petron Freeport Corporation; Deputy Director of Overseas Ventures Insurance Corp. Ltd.; and Trustee of Petron Foundation Inc. He was the Controller of the company from May 8, 2001 to May 19, 2004. He has a Bachelor of Science in Commerce degree major in Accounting from the University of Santo Tomas and is a Certified Public Accountant. He earned his MBA units from the Ateneo de Manila University and B. S. Economics units from the De La Salle College Bacolod. He completed executive and leadership programs from Cornell University, University of Virginia and the American Graduate School of International Management (Thunderbird), all in the U.S.A.

Felimon E. Antiporta, Filipino, 58 years old, is the Officer-in-Charge for Supply and Operations since March 16, 2005. He is a Trustee of the Petron Foundation Inc. and a Director of the Pandacan Depot Services, Inc., operator of the Pandacan Oil depot. He was the Operations Manager from April 2003 to March 2005. In his 34-years stay in the Company, he assumed various managerial positions such as Business Development Manager of the Corporate Planning Division, Sales Director, Retail Trade of the Marketing Division, Refinery Manager of Petron Bataan Refinery and Pandacan Terminal Manager. He graduated Magna Cum Laude with a Bachelor of Science degree in Mechanical Engineering from the National University.

Alfred A. Trio, Filipino, 56 years old, has been the Vice President for Refinery Division since December 1999 and is a Trustee of the Petron Foundation inc. Prior to his appointment as Vice President, he was the Manager of the Reseller group. He was hired as OM&S Technician at BRC Operations Department in January 1971. He gradually rose from the ranks to become Process Engineer (1979), Operations Shift Superintendent (1981), OM&S Superintendent (1984), and Engineering Department Manager (1987). In 1990, he was transferred to PNOC-EDC Operations Bacman Geothermal Project as Administrative Manager. In 1993, he assumed various managerial positions in the Refinery's Engineering and Project Management Group before he became the Acting Refinery Manager in 1998. He spearheaded efforts to transform the Petron Refinery to a best in class status in 2005. He attended the Asian Institute of Management's Top Management Program in 1998 and the Saudi Aramco Management Development Program in Washington, D. C. in 2001. He has been with the company for 34 years. He holds a Bachelor of Science degree in Chemical Engineering.

Jose Jesus G. Laurel, Filipino, 50 years old, is currently the General Counsel (since May 12, 2005) and Vice President for Legal and External Affairs (since July 26, 2005). He is also a Director of New Ventures Realty Corporation and Las Lucas Development Corporation and Trustee/Vice-President of Petron Foundation Inc. Prior to Petron, he joined PNOC Energy Development Corporation in 1992 as General Counsel & Corporate Secretary (1992-2001) and as its Vice President for Corporate Services (Law/HR/Finance/Planning/Purchasing from 2001-2005) and was promoted to Vice President/Chief Operating Officer. He was also General Counsel and Corporate Secretary of the PNOC Coal Corporation

& PNOC Exploration Corporation (1992-1999). Prior to these appointments, he worked with the Securities & Exchange Commission (SEC) from 1982 to 1992 as Hearing Officer and later Deputy Executive Director. Atty. Laurel holds an A.B. Economics degree from the Ateneo de Manila University and an LL.B degree also from Ateneo de Manila University (2nd Honors/Silver Medal). He is a 6th-place Bar examinations topnotcher and holds a Master of Laws degree from Yale Law School, Yale University, New Haven, Connecticut, USA.

Ma. Concepcion F. de Claro, Filipino, 48 years old, has been the Accounting Manager since April 2003 and is currently the Controller of the company as well as its subsidiaries such as Petrogen Insurance Corporation, New Ventures Realty Corporation, Petron Foundation Incorporated, Petron Marketing Corporation and Petron Freeport Corporation. She is also the Controller of Las Lucas Development Corporation, a subsidiary of the New Ventures Realty Corporation. She has been with the company for 25 years. She started as a Financial Analyst and held several supervisory positions at the PNOC Energy Development Corporation (PNOC-EDC), a former affiliate of Petron. After 11 years in PNOC-EDC's Finance Division, Ms. De Claro transferred to PNOC's Budget and Control Department, where she was a Supervisor for three years before she was assigned to Petron's Corporate Planning Department when the company was privatized in 1994. She was the Planning Officer for the Department for seven years, after which she became the Manager for Strategic Planning. She graduated Magna Cum Laude with a degree in Bachelor of Science in Commerce, major in Accounting from the Colegio de San Juan de Letran.

Rosario R. Eijansantos, Filipino, 57 years old, was appointed Manager of Treasurer's Department in April 2001 and elected Treasurer of the Company last May 8, 2001. She is also the Treasurer of New Ventures Realty Corporation, Petron Foundation Inc., Petrogen Insurance Corporation, Petron Marketing Corporation, Petron Freeport Corporation and Las Lucas Development Corporation, a subsidiary of NVRC. She has been with the Company for 34 years and has held managerial positions in Controllers, Internal Audit and Human Resources. She graduated Cum Laude with a degree in Bachelor of Science in Commerce , major in Accounting from the Far Eastern University and is a Certified Public Accountant.

Luis A. Maglaya, Filipino, 51 years old, is a Legal Counsel and Corporate Secretary since July 28, 2003 and was appointed thereafter as Compliance Officer. He is also the Corporate Secretary of Petron Foundation, Inc., Petrogen Insurance Corp., New Ventures Realty Corporation, Petron Marketing Corporation and Petron Freeport Corporation as well as Las Lucas Development Corporation which is a subsidiary of NVRC, He has been with the Company for 22 years. He held the position of Legal Counsel and Assistant Corporate Secretary from 1994 to 2003. He earned his Bachelor of Arts degree in Political Science from Ateneo de Manila University in 1975. He obtained his law degree from the University of the Philippines in 1980.

(3) Significant Employees

There is no significant employee or personnel who is not an executive officer but is expected to make a significant contribution to the business.

(4) Family Relationships

None of the directors or executive officers are in any way related between and among each other, either by consanguinity or affinity.

(5) Involvement in Certain Legal Proceedings

None of the directors and executive officers have been the subject of bankruptcy petitions or pending criminal proceedings or have been by judgment or decree found to have violated securities or commodities law and enjoined from engaging in any business, securities, commodities or banking activities.

(B) Executive Compensation

(1) Executive Compensation

Standard Arrangements.

Petron's Executive Officers are also regular employees of the company and are similarly remunerated with a compensation package comprising of twelve (12) months base pay. They also receive whatever gratuity pay the Board extends to the managerial, supervisory and technical employees of the Company.

The members of the Board of Directors who are not Executive Officers are elected for a term of one year. They likewise receive remuneration for 12 months in Director's fees, in addition to compensation on a per meeting participation.

Other Arrangements

There are no other arrangements for which the directors are compensated.

Employment Contract

In lieu of an employment contract, the Directors are elected at the annual meeting of stockholders for a one (1) year term. Any director elected in the interim will serve for the remaining term until the next annual meeting.

(2) Summary Compensation Table

Compensation of Executive Officers and Directors		
Name	**Prinicipal Position**	**Amount (In Million Pesos)**
Nicasio I. Alcantara	Chairman	
Khalid D. Al-Faddagh	President / CEO	
Jose K. Campos, Jr.	Vice President - Marketing	
Alfred A. Trio	Vice President - Refinery	
Antonio G. Pelayo	Vice President - Finance & Subsidiaries	
Jose Jesus G. Laurel	General Counsel, Vice President - Legal & External Affairs	
Basil A. Abul-Hamayel	Vice President- Corporate Planning January 1, 2004-September 6, 2005	
Sulaiman M. Ababtain	Vice President - Corporate Planning September 7, 2005	
Walter A. Tan	Vice President- Supply & Operations January 1, 2004- March 31, 2005	
Felimon E. Antiporta	OIC VP - Supply & Operations April 1, 2005	
Luis A. Maglaya	Corporate Secretary	
Rosario R. Eijansantos	Treasurer	
Concepcion F. de Claro	Controller	
TOTAL (Top 5 Executives)	Aggregate (2004-2005)	111.17
TOTAL (All Executives & Directors)	Aggregate (2004-2005)	189.17
Estimates:		
Estimate 2006 (Top 5 Executives)	Aggregate (2005-2006)	120.91
Estimate 2006 (All Executives/Directors)	Aggregate (2005-2006)	204.00

(C) Security Ownership of Certain Beneficial Owners and Management as of March 31, 2006.

Security Ownership of Certain Record and Beneficial Ownership

Title of Class	**Name & Address of record owner and relationship with issuer**	**Name of Beneficial Owner & relationship with record owner**	**Citizenship**	**No. of shares held**	**Percent**
Common Stocks	Philippine National Oil Co.* PNPC Complex, Merritt Road, Fort Bonifacio, Taguig City, M.M. Major Stockholder	Philippine National Oil Company- Proxy- PNOC Chairman, Raphael Lotilla, Sec. of Dept of Energy	Filipino	3,750,000,007 (r)	40%
Common Stocks	Aramco Overseas Company B.V. ** PO Box 5000, Dhahran 31311, Saudi Arabia Major Stockholder	Aramco Overseas Co. B.V. Proxy- Khalid G. Al-Buainain, Vice President for Refining of Saudi Aramco	Netherlands	3,750,000,006 (r)	40%
Common Stocks	PCD Nominee Corporation (Foreign)*** G/F MSE Bldg., 6767 Ayala Avenue Makati City		Foreign	601,990,823 (r)	6.42%
Common Stocks	PCD Nominee Corporation (Filipino)*** G/F MSE Bldg., 6767 Ayala Avenue Makati City		Filipino	505,739,442 (r)	5.39%

* Beneficial owner is the government of the Republic of the Philippines through the Philippine National Oil Company (PNOC). Shares are voted upon by the proxy of PNOC.

** Beneficial owner is Saudi Aramco which is owned by the Kingdom of Saudi Arabia. Shares are voted upon by the proxy designated by Aramco Overseas Company, B.V.

*** PCD Nominee Corporation, a wholly owned subsidiary of Philippine Central Depository, Inc. (PCD), is the registered owner of the shares in the books of the Company's transfer agent in the Philippines. The beneficial owners of such shares are PCD's participants, who hold the shares on their behalf or in behalf of their clients. PCD is a private company organized by the major institutions actively participating in the Philippines capital market to implement an automated book-entry system of handling securities transactions in the Philippines.

(1) Security Ownership of Management as of March 31, 2006

Title of Class	Name of Beneficial Owner	Amount & Nature of Beneficial Ownership (Indicate by "d" or "I")	Citizenship	Percent of Class
Directors				
Common Stock	Nicasio I. Alcantara	1,238,705 (d)	Filipino	0.013%
Common Stock	Khalid D. Al-Faddagh	1 (d)	Saudi Arabian	Nil
Common Stock	Basil A. Abul-Hamayel	1,000 (d)	Saudi Arabian	Nil
Common Stock	Bernardino R. Abes	1 (d)	Filipino	Nil
Common Stock	Khalid G. Al-Buainain	1 (d)	Saudi Arabian	Nil
Common Stock	Herminio S. Aquino	15,000 (d)	Filipino	Nil
Common Stock	Alberto A. Pedrosa	1 (d)	Filipino	Nil
Common Stock	Ahmad O. Al-Khowaiter	1 (d)	Saudi Arabian	Nil
Common Stock	Douhan H. Al-Douhan	1,000 (d)	Saudi Arabian	Nil
Common Stock	Jose Luis U. Yulo, Jr.	3,000 (d)	Filipino	Nil
Executive Officers				
Common Stock	Alfred A. Trio	263,313 (d)	Filipino	Nil
Common Stock	Jose K. Campos, Jr.	1,433,275 (d)	Filipino	0.015%
Common Stock	Antonio G. Pelayo	158,668 (d)	Filipino	Nil
Common stock	Jose Jesus G. Laurel	10,000 (d)	Filipino	Nil
Common stock	Felimon E. Antiporta	222,350 (d)	Filipino	Nil
Common Stock	Rosario R. Eijansantos	235,689 (d)	Filipino	Nil
Common Stock	Ma. Concepcion F. de Claro	22,513 (d)	Filipino	Nil
Common Stock	Luis A. Maglaya	68,550 (d)	Filipino	Nil

As of March 31, 2006, the total number of shares owned by the Directors and officers is 3,673,068.

(2) Voting Trust Holders of 10% or more

There is no voting trust between PNOC and AOC.

(3) Changes in Control

There is no arrangement which may result in a change in control of the Company.

(D) Certain Relationships and Related Transactions

1. The long-term leases between PNOC and Petron since 1994 over various parcels of land.
2. The “Parents” of the Company are:

(a) Philippine National Oil Co. - 40%
(b) Aramco Overseas Co. B.V. - 40%

The basis of control is the number of the percentage of voting shares held by each.

(E) Corporate Governance

Petron's Board of Directors is composed of ten (10) members, two (2) of whom are Independent Directors. Currently, only two (2) of the members are Executive Directors, occupying the positions of the Chairman and the President of the Company. Petron Directors sign Conflict-of-Interest Statements, disclosing their respective business interests, to ensure that these are not in competition with the business of Petron. The schedule of board meetings for the entire year is fixed at the start of the year and board materials are given not later than two weeks prior to every meeting. All Directors, officers and senior managers are required to attend basic corporate governance seminar immediately upon assuming office.

To instill a stable and transparent process of conducting its business and at the same time identifying accountability at all times, a system of approvals is in place whereby only authorized officer(s) may approve a particular business transaction and only up to the authorized amount. Transactions with amounts exceeding the joint approval limit of the Chairman and the President are elevated to the Board for approval. Aside from the Corporate Governance Manual, several other manuals have been instituted by Management to establish company policies and guide the employees in carrying out their respective functions and duties, address business operations, set contracting and bidding procedures, and instill business ethics, office decorum and employee discipline.

Reports required to be given to the stockholders pursuant to its By-Laws and the Securities and Regulation Code and submissions to the SEC/PSE, including quarterly financial reports, annual report and disclosures, GIS, request for explanation or information on news items are complied with. The Company sees to it that queries or requests from shareholders are immediately attended to and that written communications, including notices of stockholders meetings, are properly sent. Pursuant to the requirements of the Securities and Exchange Commission, the Corporate Secretary and Compliance Officer has submitted in January 2006 the required yearly certification to the SEC on the extent of compliance by the Company with its Corporate Governance Manual.

With the election of 2 independent Directors to the Petron Board; the election of members and alternate members, in proper cases, of the Audit, Compensation and Nomination Committees; the conduct of regular quarterly board meetings, special board meetings and board committee meetings and the faithful attendance of and proper discharge of duties and responsibilities of Directors at such meetings; the conduct of training/seminar for Corporate Governance for incoming Directors and Officers; and strict adherence to national and local laws pertaining to its business operations, including applicable accounting standards and disclosure requirements, the Company is in substantial compliance with its Corporate Governance Manual.

A performance evaluation system to assess the performance of Directors, Board Committees and the Board itself is in place and will be carried out periodically. An integrated compliance checklist form to facilitate compliance monitoring is expected to be completed in 2006.

Directors Attendance in Corporate Governance Seminar and Meetings

List of Directors

(As of December 31, 2005)

#	Directors	Executive/ Non-Executive/ Independent Director	Attended Corporate Governance Seminar	Attendance to Meeting						Committee Membership		
				1-Mar	12-May	25-Jul *	25-Jul **	26-Jul ***	30-Nov	Nomi-nation	Audit	Compen-sation
1	Nicasio I. Alcantara	Executive Director	x	x	x	x	x	x	x	x		x
2	Khalid D. Al-Faddagh	Executive Director	x	x	x	x	x	x	x	x		x
3	Jose Luis U. Yulo, Jr.	Independent Director	x	x	x	x	x	x	x	x	x	x
4	Douhan H. Al-Douhan	Independent Director	x	x	x	x	x	x	x	x	x	
5	Bernardino R. Abes	Non-Executive Director	x	x	x	x	x	x	x			x
6	Khalid G. Al-Buainain	Non-Executive Director	x	x	x			x	x			x
7	Basil A. Abul-Hamayel (1)	Non-Executive Director	x	x	x	x	x	x	x	x		
8	Herminio S. Aquino	Non-Executive Director	x	x	x	x	x	x	x		x	
9	Alberto A. Pedrosa (2)	Non-Executive Director	x	x	x	x	x	x	x	x		
10	Motassim A. Al-Ma'ashouq (3) Ahmad O. Al-Khowaiter	Non-Executive Director	x	x	x		x	x	x		x	x

Notes:

* Special Board Meeting

** Annual Stockholders' Meeting

*** Organization Meeting

(1) Resigned as Vice President for Corporate Planning effective September 6, 2005

(2) Elected by the Board of Directors effective March 1, 2005, replacing Mr. Bob D. Gothong

(3) Mr. Al-Maashouq was succeeded by Mr. Al-Khowaiter, who was elected at the July 25, 2005 Annual Stockholders' Meeting

PART V - EXHIBITS AND SCHEDULES

Item 14. Exhibits and Reports on SEC Form 17-C

Exhibits

Exhibit 1 - Audited Financial Statements
Exhibit 2 - Index to Financial Statements & Supplementary Schedules

Reports on SEC Form 17-C

1. Attendees of Petron's Board Meetings for 2004
2. Early retirement of Mr. Walter A. Tan, Petron VP for Supply and Operations effective March 31, 2005.
3. Election of Ambassador Alberto A. Pedrosa as Director of Petron effective March 1, 2005, following the resignation of Director Bob D. Gothong.
4. Reorganization of the Nomination Committee
5. Inter-company advances to NVRC for the SS Site at Megaworld C-5 amounting to P62.125 million
6. Contract awards for the installation of 230 KV substation for Refinery and the construction of a 1,700 MT LPG spherical tank at Mandaue Terminal.
7. Funding in the amount of P572.23 million for its major capital program.
8. Disclosure of 2004 Audited Financial Statements with a net income of P3.425 billion for the full year 2004.
9. Response to Philippine Star news article dated March 7, 2005 entitled "Palace to Study Drilon's Proposal to Reacquire Petron".
10. Amended two (2) Complaints filed before the Regional Trial Court of Manila against its contracted marine haulers, increasing the amount of actual damages from P50 Million to P261 Million. The latter amount represents the shortfalls in delivered petroleum products shipped from Petron's Refinery in Bataan to Petron's depot in Pandacan.
11. Appointment of Atty. Jose Jesus G. Laurel as General Counsel
12. Ratification of the Purchase Award for the Annual Requirement of 1,800 MT of High Density PolyEthylene.
13. Holding of Petron's Annual Stockholders' Meeting on July 25, 2005 and the approval of the Agenda for said meeting, which will be held at the Fiesta Pavilion, Manila Hotel at 9:00 a. m.
14. Setting of May 26, 2005 as the record date for the Annual Stockholders' Meeting and closing of stock transfer books from May 27 to June 10, 2005.
15. Approval of Nomination Committee recommendation for candidates for election as Incoming Directors
16. Award of Contract for Electricity Power Purchase Agreement (EPPA) at the Refinery
17. Declaration of a cash dividend of P0.10 per share to stockholders of record of the Corporation as of the close of trading hours on May 26, 2005, payable on June 21, 2005.
18. Approval of 1st Quarter 2005 Financial Statements and authority to release the same to regulatory agencies. Disclosure also indicate that the Board received the 1st Quarter Financial Performance Report showing a Consolidated Net Income of P870 million.
19. The rank and file employee's union at the Petron Refinery in Bataan filed a Notice of Strike with the National Conciliation and Mediation Board at its Regional Office in San Fernando, Pampanga. On July 11, 2005, the Secretary of Labor certified the labor dispute for compulsory arbitration by the National Labor Relations Commission (NLRC), directing that any strike or lockout be enjoined and ordering the employees to return to work in the event of a strike.
20. Approval of the Interim Financial Report for the first half of 2005, showing a Consolidated Net Income of P2.31 billion.
21. Election of Directors of Petron Corporation
22. Re-appointment of Sycip, Gorres and Velayo as independent auditor of Petron for 2005
23. Election of Executive Officers of Petron Corporation
24. Appointment of members to the Audit Committee, Compensation Committee and Nomination Committee of the Board

25. Appointment of Jose Jesus G. Laurel as General Counsel of the Corporation for a term of one (1) year.
26. Approved the funding of US$183.325 million or approximately P10.656 billion for capital expenditures to cover Refinery projects.
27. Clarification on the re-election of executive officers, particularly the Board's approval on the election of Luis A. Maglaya as Corporate Secretary **and** Compliance Officer.
27. Resignation of Basil A. Abul-Hamayel as Vice President for Corporate Planning effective September 6, 2005, after his new assignment with Saudi Aramco. Nevertheless, he will continue to be a Director for Petron. In view of Mr. Abul-Hamayel's resignation, Mr. Sulaiman M. Ababtain was appointed as Officer-in-Charge of the Office of the Vice President for Corporate Planning effective September 7, 2005.
28. Endorsement by the Board of Directors of the Company's compliance with the terms and conditions of the Board of Investments (BOI) for the application of incentives for its BTX (Benzene, Toluene and Xylene) and Propylene Recovery (PRU) Projects.
29. Endorsement of the 2006-2010 Business Plan and 2006 Capital Program in the amount of P4.224 billion
30. 2006 Operating Plan and Budget in the total amount of P8.92 billion
31. Miscellaneous Capital Budget in the total amount of P494 million
32. Setting-up of appropriated retained earnings to P11.652 billion for fiscal year ending December 31, 2005
33. Deletion of Prior Year's Capital Budget Balances in the total amount of P75.4 million
34. Acceptance of BOI Conditions for Registration for Petro Fluidized Catalytic Cracking Unit and Grease Plant Rehabilitation Projects
35. Ratification of 3rd Quarter Financial Statements
36. Ratification of the election of Sulaiman M. Ababtain as Vice President for Corporate Planning
37. Ratification of the Acceptance of BOI Conditions for Registration of Propylene Recovery Unit (PRU), Benzene, Toluene & Mixed Xylene Projects
38. Attendees of Petron's Board Meetings for 2005

The Company also submitted the following press and photo releases

1. Press Release on January 21, 2005 entitled "Petron Net Income Likely to Exceed 2004 Target".
2. Press Release on January 28, 2005 entitled "Petron Refinery Achieves Another Safety And Environmental Milestone".
3. Press Release on March 23, 2005 entitled "Petron Volunteers Ready For Lakbay-Alalay 2005".
4. Press Release on may 6, 2005 entitled "Investing In The Future: Petron Inaugurates $100-Million Clean Air Facilities At Its Bataan Refinery".
5. Press Release on May 12, 2005 entitled "Petron Corporation Posts P870-M For 1st Quarter 2005".
6. Press Release on May 23, 2005 entitled "Petron, Holcim Establish Energy-From-Waste Collaboration".
7. Press Release on June 1, 2005 entitled "Petron Signs MOU In Support Of National Fuel Ethanol Program".
8. Press Release on June 23, 2005 entitled "Petron Cited for Good Corporate Governance".
9. Press Release on July 25, 2005 entitled "Petron Posts P2.31-Billion Income For 1st Half of 2005".
10. Press Release on August 30, 2005 entitled " From 2004 to 1st Half 2005: Export Sales Comprised 38% Of Petron's Net Income".
11. Press Release on September 27, 2005 entitled "Petron Corp. Joins Philippine Fuel Ethanol Alliance".
12. Press Release on October 21, 2005 entitled « Petron Complies With BOI For Petrochemical Projects".
13. Press Release entitled "Petron Empowers the Youth Through Entrepreneurship Education".
14. Press Release on November 29, 2005 entitled " Petron's Gasul Still The Lowest Priced In The Market".
15. Press Release on December 20, 2005 entitled "Petron Approves $178.4-M Contract for Petrochem Project".

SIGNATURES

Pursuant to the requirements of Section 17 of the Code and Section 141 of the Corporation Code, this report is signed on behalf of the issuer by the undersigned, thereunto duly authorized, in the City of Makati on APR 21 2006, 2006.

By:

NICASIO I. ALCANTARA
Chairman

KHALID D. AL-FADDAGH
President/Chief Executive Officer

MA. CONCEPCION F. DE CLARO
Controller

LUIS A. MAGLAYA
Corporate Secretary

SUBSCRIBED AND SWORN to before me this_____ day of APR 21 2006 2006 affiant(s) exhibiting to me his/their Community Tax Certificates, as follows:

NAMES	CTC#	DATE OF ISSUE	PLACE OF ISSUE
Nicasio I. Alcantara	24808809	January 12, 2006	Makati City
Khalid D. Al-Faddagh	24315726	February 24, 2006	Makati City
Ma. Concepcion F. de Claro	9775562	January 6, 2006	Mandaluyong City
Luis A. Maglaya	21674119	April 11, 2006	Quezon City

JOHN B. ENCARNACION
Notary Public for Makati City
Notary Commission No. M-217
Until December 31, 2007
PTR No. 4193955E 1.10.06 Makati
IBP No. 669783 1.10.06 Pasig
Roll of Attorney No. 43192
PETRON MegaPlaza Bldg. 358 Sen. Gil Puyat Ave.
Makati City

Notary Public

Doc. No. 282
Page No. 56
Book No. XIV
Series of 2006.

COVER SHEET

3 1 1 7 1

SEC Registration Number

PETRON CORPORATION AND SUBSIDIARIES

(Company's Full Name)

Petron MegaPlaza, 358 Sen. Gil Puyat Avenue, Makati City

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

Luis A. Maglaya

(Contact Person)

886-3888

(Company Telephone Number)

1 2	3 1	A A C F S		
Month	*Day*	(Form Type)	*Month*	*Day*
(Fiscal Year)			(Annual Meeting)	

(Secondary License Type, If Applicable)

Dept. Requiring this Doc.

Amended Articles Number/Section

Total Amount of Borrowings

Total No. of Stockholders

Domestic

Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document ID

Cashier

S T A M P S

SGV & Co

SyCip Gorres Velayo & Co.
6760 Ayala Avenue
1226 Makati City
Philippines

Phone: (632) 891-0307
Fax: (632) 819-0872
www.sgv.com.ph

BOA/PRC Reg. No. 0001
SEC Accreditation No. 0012-F

Report of Independent Auditors

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

We have audited the accompanying consolidated balance sheets of Petron Corporation and Subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of income, recognized income and expense and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Philippines. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Petron Corporation and Subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for the years then ended in conformity with the accounting principles generally accepted in the Philippines.

SYCIP GORRES VELAYO & CO.

Wilson P. Tan

Wilson P. Tan
Partner
CPA Certificate No. 76737
SEC Accreditation No. 0100-A
Tax Identification No. 102-098-469
PTR No. 4181277, January 2, 2006, Makati City

April 4, 2006

PETRON CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Amounts in Millions)

	December 31	
	2005	2004 (As restated - Note 3)
ASSETS		
Current Assets		
Cash and cash equivalents (Note 6)	**₱4,071**	₱4,104
Financial assets at fair value through profit or loss (Notes 7, 9 and 12)	**144**	–
Available-for-sale investments (Notes 8 and 12)	**259**	–
Short-term investments (Notes 7 and 9)	**–**	63
Receivables (Note 10)	**14,055**	11,758
Inventories (Notes 11, 25 and 28)	**27,018**	22,414
Other current assets (Note 32)	**1,297**	790
Total Current Assets	**46,844**	39,129
Noncurrent Assets		
Property, plant and equipment (Note 13)	**22,570**	22,446
Investment properties (Note 14)	**207**	202
Available-for-sale investments (Notes 8 and 12)	**196**	–
Other noncurrent assets (Notes 7, 8, 12, 15 and 27)	**1,258**	1,352
Total Noncurrent Assets	**24,231**	24,000
	₱71,075	₱63,129
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Short-term loans (Note 16)	**₱21,407**	₱18,477
Liabilities for crude oil and petroleum product importation (Note 25)	**7,911**	6,128
Accounts payable and accrued expenses (Notes 17 and 32)	**4,818**	5,085
Current portion of long-term debt (Notes 18 and 32)	**1,906**	1,595
Income tax payable	**183**	278
Total Current Liabilities	**36,225**	31,563
Noncurrent Liabilities		
Long-term debt - net of current portion (Note 18)	**5,025**	7,227
Deferred income tax liabilities (Note 24)	**1,513**	1,349
Other noncurrent liabilities (Note 19)	**697**	667
Total Noncurrent Liabilities	**7,235**	9,243
Stockholders' Equity Attributable to Equity Holders of the Parent (Note 20)		
Capital stock	**9,375**	9,375
Retained earnings:		
Appropriated	**11,652**	6,906
Unappropriated	**6,352**	5,623
Other reserves	**128**	309
Stockholders' Equity Attributable to Equity Holders of the Parent	**27,507**	22,213
Minority Interest (Note 20)	**108**	110
Total Stockholders' Equity	**27,615**	22,323
	₱71,075	₱63,129

See accompanying Notes to Consolidated Financial Statements.

PETRON CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Amounts in Millions, Except Per Share Amounts)

	Years Ended December 31	
	2005	2004 (As restated - Note 3)
SALES (Notes 28 and 34)	**₱191,489**	₱147,425
COST OF GOODS SOLD (Notes 21, 25 and 28)	**176,960**	135,437
GROSS PROFIT	**14,529**	11,988
SELLING AND ADMINISTRATIVE EXPENSES (Notes 22, 26 and 27)	**(4,527)**	(4,877)
INTEREST EXPENSE (Notes 16, 18 and 23)	**(2,091)**	(1,675)
INTEREST INCOME (Note 23)	**317**	344
OTHERS (Note 23)	**(86)**	(356)
INCOME BEFORE INCOME TAX	**8,142**	5,424
PROVISION FOR (BENEFIT FROM) INCOME TAX (Notes 24 and 33)		
Current	**2,057**	1,339
Deferred	**34**	(16)
	2,091	1,323
NET INCOME	**₱6,051**	₱4,101
Attributable to:		
Equity holders of the parent	**₱6,044**	₱4,094
Minority interest	**7**	7
	₱6,051	₱4,101
EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT (Note 29)	**₱0.64**	₱0.44

See accompanying Notes to Consolidated Financial Statements.

PETRON CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF RECOGNIZED INCOME AND EXPENSE

(Amounts in Millions) (Note 2)

	Years Ended December 31	
	2005	2004
Actuarial gains on defined pension plan (Note 27)	**₱356**	₱286
Tax effect	**(133)**	(92)
Net actuarial gains on defined pension plan	**223**	194
Less actuarial losses (gains) due to limit on recognized plan asset [net of tax effect of ₱212 and ₱53 in 2005 and 2004, respectively (Notes 20 and 27)]	**(408)**	115
	(185)	309
Unrealized fair value gain on available-for-sale investments [net of tax effect of ₱4 and effect of change in accounting policy - PAS 39 of ₱2 (Notes 3 and 8)]	**4**	–
NET INCOME (LOSS) RECOGNIZED DIRECTLY IN STOCKHOLDERS' EQUITY	**(181)**	309
NET INCOME FOR THE YEAR (Note 20)	**6,051**	4,101
TOTAL RECOGNIZED INCOME AND EXPENSE FOR THE YEAR	**₱5,870**	₱4,410
Attributable to:		
Equity holders of the parent	**₱5,863**	₱4,403
Minority interest	**7**	7
	₱5,870	₱4,410

See accompanying Notes to Consolidated Financial Statements.

PETRON CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in Millions)

	Years Ended December 31	
	2005	2004 (As restated - Note 3)
CASH FLOWS FROM OPERATING ACTIVITIES		
Income before income tax	**₱8,142**	₱5,424
Adjustments for:		
Depreciation and amortization	**2,335**	1,856
Interest expense	**2,091**	1,675
Interest income	**(317)**	(344)
Net unrealized foreign exchange loss (gain)	**(270)**	48
Others	**(111)**	–
Operating income before working capital changes	**11,870**	8,659
Changes in operating assets and liabilities (Note 30)	**(6,326)**	(6,093)
Interest paid	**(2,047)**	(1,643)
Income taxes paid	**(1,850)**	(1,075)
Interest received	**316**	343
Net cash provided by operating activities	**1,963**	191
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to:		
Property, plant and equipment	**(2,313)**	(5,463)
Investment properties	**(16)**	–
Decrease (increase) in:		
Other receivables	**9**	209
Other noncurrent assets	**(67)**	(182)
Reductions from (additions to):		
Financial assets at fair value through profit or loss	**2**	–
Available-for-sale investments	**(118)**	–
Short-term investments	**–**	19
Net cash used in investing activities	**(2,503)**	(5,417)
CASH FLOWS FROM FINANCING ACTIVITIES		
Availments of loans	**78,246**	80,854
Payments of:		
Loans	**(76,879)**	(72,949)
Cash dividends	**(925)**	(1,846)
Others	**78**	101
Net cash provided by financing activities	**520**	6,160
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	**(13)**	(28)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(33)**	906
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**4,104**	3,198
CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 6)	**₱4,071**	₱4,104

See accompanying Notes to Consolidated Financial Statements.

PETRON CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

1. Corporate Information

Petron Corporation (the Parent Company or Petron) was incorporated on December 15, 1966 under the laws of the Republic of the Philippines. Petron is the Philippines' largest oil refining and marketing company, supplying more than one-third of the country's oil requirements. Its 180,000 barrel per day refinery located in Limay, Bataan processes crude oil into a full range of petroleum products, including liquefied petroleum gas (LPG), gasoline, diesel, jet fuel, kerosene, industrial fuel oil, lubes and greases, asphalts and mixed xylene (a high value petrochemical product). From its refinery, Petron moves its products mainly by sea, using tankers and barges to distribute products to a nationwide network of depots and terminals. Through this network, it sells fuel oil, diesel and LPG to industrial customers.

Petron also retails gasoline, diesel and kerosene to motorists, public transport operators and households through more than a thousand service stations - the largest network in the country. Petron also sells its LPG brand "Gasul" to consumers through a dealership network.

Petron is also expanding its non-fuels business which includes its convenience store "Treats" to add other revenue streams to its core business.

In line with its efforts to increase its presence in the regional market and take advantage of favorable prices abroad, Petron exports various petroleum products to other Asian countries such as Cambodia, Korea, China and Australia.

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

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

The consolidated financial statements for the years ended December 31, 2005 and 2004 were approved and authorized for issue by the Board of Directors (BOD) on April 4, 2006.

2. Basis of Preparation

The consolidated financial statements of Petron and subsidiaries (collectively referred to as "the Company") have been prepared in compliance with accounting principles generally accepted in the Philippines as set forth in Philippine Financial Reporting Standards (PFRS). PFRS include standards named PFRS and Philippine Accounting Standards (PAS), including interpretations issued by the Philippine Accounting Standards Council (PASC). This is the Company's first consolidated financial statements prepared in compliance with PFRS.

The Company prepared its consolidated financial statements until December 31, 2004 in conformity with previous Statements of Financial Accounting Standards (SFAS) and Statements of Financial Accounting Standards/International Accounting Standards (SFAS/IAS) issued by the PASC.

The Company applied PFRS 1, “First-time Adoption of Philippine Financial Reporting Standards,” in preparing the consolidated financial statements, with January 1, 2004 as the date of transition. The Company applied the accounting policies set forth in Note 3 to all the years presented, except those relating to financial instruments. An explanation of how the transition to PFRS has affected the reported financial position, financial performance and cash flows of the Company is also discussed in Note 3.

The consolidated financial statements of the Company have been prepared on the historical cost basis, except for financial assets at fair value through profit or loss (FVPL), available-for-sale (AFS) investments and derivative financial instruments, which are measured at fair value.

The consolidated financial statements are presented in Philippine pesos, which is the Company’s functional and presentation currency under PFRS, and all amounts are rounded to the nearest millions (₱000,000), except when otherwise indicated.

Basis of Consolidation

The consolidated financial statements comprise the financial statements of Petron and its subsidiaries as of December 31 of each year. The financial statements of the subsidiaries are prepared for the same reporting year as the Parent Company.

The purchase method of accounting is used for acquired businesses. Subsidiaries are consolidated from the date on which control is transferred to the Company and cease to be consolidated from the date on which control is transferred out of the Company.

The consolidated subsidiaries include:

Subsidiaries	Percentage of Ownership	Country of Incorporation
Overseas Ventures Insurance Corporation (Ovincor)	100	Bermuda
Petrogen Insurance Corporation (Petrogen)	100	Philippines
Petron Freeport Corporation (PFC)	100	Philippines
Petron Marketing Corporation (PMC)	100	Philippines
New Ventures Realty Corporation and Subsidiary (NVRC)	79.95	Philippines

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

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

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

The consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. Intercompany balances and transactions, including intercompany profits and unrealized profits and losses are eliminated.

Minority interest represents the portion of net income and net assets of NVRC, not held by the Company and are presented separately in the consolidated statements of recognized revenue and expense, consolidated statements of income and within equity in the consolidated balance sheets, separately from Parent stockholders' equity.

In prior years, the Company presented separate statements of changes in stockholders' equity. Starting 2005 and in compliance with its early adoption of Amendments to PAS 19, "Employee Benefits - Actuarial Gains and Losses, Group Plans and Disclosures," the Company presents comparative consolidated statements of recognized income and expense, which show changes in stockholders' equity attributable to total income and expense, including gains and losses, whether recognized in the consolidated statements of income or directly as changes in stockholders' equity, generated by the Company's activities for the years ended December 31, 2005 and 2004. Changes resulting from transactions with equity holders of the parent and minority interest holders acting in their capacity as equity holders (such as equity contributions, re-acquisitions of the Company's own equity instruments and dividends) and transaction costs directly related to such transactions, are disclosed in Note 20 - Other Changes in Stockholders' Equity.

3. Changes in Accounting Policies

Explanation of Transition to PFRS

The transition to PFRS resulted in certain changes to the Company's previous accounting policies [referred to in the following tables and explanations as "previous Generally Accepted Accounting Principles (GAAP)"]. The comparative figures for the 2004 consolidated financial statements were restated to reflect the changes in accounting policies, except those relating to financial instruments. The Company availed of the exemption under PFRS 1 and applied PAS 32, "Financial Instruments: Disclosure and Presentation" and PAS 39, "Financial Instruments: Recognition and Measurement" effective January 1, 2005.

An explanation of the effects of the transition to PFRS is set forth in the following tables and notes.

Reconciliation of Accounts at January 1, 2004 and December 31, 2004

		At January 1, 2004 (date of transition)			At December 31, 2004 (end of last period presented under previous GAAP)		
	Notes	Previous GAAP	Effect of transition to PFRS	PFRS	Previous GAAP	Effect of transition to PFRS	PFRS
ASSETS							
Current Assets							
Cash and cash equivalents		₱3,198	₱–	₱3,198	₱4,104	₱–	₱4,104
Short-term investments		69	–	69	63	–	63
Receivables		9,468	–	9,468	11,758	–	11,758
Inventories	a	15,674	2,424	18,098	19,235	3,179	22,414
Other current assets		753	–	753	790	–	790
Total Current Assets		29,162	2,424	31,586	35,950	3,179	39,129
Noncurrent Assets							
Property, plant and equipment	b, d, f, g	₱21,497	(₱2,657)	₱18,840	₱24,862	(₱2,416)	₱22,446
Investment properties	f	–	199	199	–	202	202
Other noncurrent assets	c, f, g	542	480	1,022	605	747	1,352
Total Noncurrent Assets		22,039	(1,978)	20,061	25,467	(1,467)	24,000
		₱51,201	₱446	₱51,647	₱61,417	₱1,712	₱63,129
LIABILITIES AND STOCKHOLDERS' EQUITY							
Current Liabilities							
Short-term loans		₱15,385	₱–	₱15,385	₱18,477	₱–	₱18,477
Liabilities for crude oil and petroleum product importation		6,560	–	6,560	6,128	–	6,128
Accounts payable and accrued expenses		3,872	–	3,872	5,085	–	5,085
Income tax payable		14	–	14	278	–	278
Current portion of long-term debt		712	–	712	1,595	–	1,595
Total Current Liabilities		26,543	–	26,543	31,563	–	31,563
Noncurrent Liabilities							
Long-term debt - net of current portion		3,288	–	3,288	7,227	–	7,227
Deferred income tax liabilities	g, i	1,207	91	1,298	882	467	1,349
Other noncurrent liabilities	b	390	225	615	411	256	667
Total Noncurrent Liabilities		4,885	316	5,201	8,520	723	9,243
Stockholders' Equity Attributable to Equity Holders of the Parent							
Capital stock		9,375	–	9,375	9,375	–	9,375
Retained earnings:							
Appropriated		5,551	–	5,551	6,906	–	6,906
Unappropriated	h	4,663	211	4,874	4,858	765	5,623
Other reserves	c, d	81	(81)	–	85	224	309
Stockholders' Equity Attributable to Equity Holders of the Parent		19,670	130	19,800	21,224	989	22,213
Minority Interest		103	–	103	110	–	110
Total Stockholders' Equity		19,773	130	19,903	21,334	989	22,323
		₱51,201	₱446	₱51,647	₱61,417	₱1,712	₱63,129

Reconciliation of Income for the Year Ended December 31, 2004

	Notes	Previous GAAP	Effect of transition to PFRS	PFRS
Sales		₱147,425	₱–	₱147,425
Cost of goods sold	a, d	136,444	(1,007)	135,437
Gross profit		10,981	1,007	11,988
Selling and administrative expenses	b, c	(4,866)	(11)	(4,877)
Interest income		344	–	344
Interest expense	b	(1,647)	(28)	(1,675)
Others	d, g	(366)	10	(356)
Income before income tax		4,446	978	5,424
Provision for income tax	a, b, c, d	1,014	309	1,323
Net income		₱3,432	₱669	₱4,101
Attributable to:				
Equity holders of the parent		₱3,425	₱669	₱4,094
Minority interest		7	–	7
		₱3,432	₱669	₱4,101
Earnings per share attributable to equity holders of the parent		₱0.37	₱0.07	₱0.44

Notes to the Reconciliation of Equity at January 1 and December 31, 2004 and Income for 2004

a. PAS 2, "Inventories." PFRS reduces the alternatives for measurement of inventories. It does not permit the use of the last-in, first-out (LIFO) formula to measure the cost of inventories. In 2005, the Parent Company changed its inventory costing method for petroleum products (except for lubes and greases, waxes and solvents) from LIFO to first-in, first-out (FIFO) method. The impact of this change increased retained earnings by ₱1,648 (net of tax effect of ₱776) as of January 1, 2004 and ₱2,162 (net of tax effect of ₱1,017) as of December 31, 2004 and increased inventories by ₱2,424 as of January 1, 2004 and ₱3,179 as of December 31, 2004. This accounting change also decreased cost of goods sold by ₱755 for 2004.

b. PAS 16, "Property, Plant and Equipment." Property, plant and equipment under PFRS include the estimated costs of dismantling or removing structures used in operation for which the Company is liable. Under previous GAAP, dismantling or removal costs were recognized when incurred.

   Adoption of this standard increased (decreased) the following accounts:

	At January 1, 2004			At December 31, 2004		
	Gross	Tax Effect	Net	Gross	Tax Effect	Net
Property, plant and equipment	₱54	₱–	₱54	₱53	₱–	₱53
Other noncurrent liabilities	225	–	225	256	–	256
Retained earnings	(171)	55	(116)	(204)	65	(139)

This also increased selling and administrative expenses by ₱4 and interest expense by ₱28 for 2004.

c. PAS 19, “Employee Benefits.” Adoption of PAS 19 requires recognition of defined benefit liability or net pension asset in the consolidated balance sheets. This resulted to the recognition of transition pension asset under the Company’s defined benefit plan which increased retained earnings by ₱343 (net of tax effect of ₱162) as of January 1, 2004 and ₱338 (net of tax effect of ₱160) as of January 1, 2005. The adoption also resulted to an increase in other noncurrent assets by ₱505 and ₱783 as of January 1, 2004 and December 31, 2004 respectively and also increase in selling and administrative expenses by ₱7 for 2004.

   The Company also early adopted the Amendments to PAS 19, “Employee Benefits - Actuarial Gains and Losses, Group Plans and Disclosures.” The standard permits the recognition of actuarial gains and losses outside profit and loss and instead present a statement of recognized income and expense. Actuarially computed gains amounted to ₱309 (net of tax effect of ₱145) for the year ended December 31, 2004 and actuarial losses due to limit in plan assets to be recognized amounted to ₱115 (net of tax effect of ₱53) for the year ended December 31, 2004. The latter is recognized immediately in retained earnings (see Note 20).

d. PAS 21, “The Effects of Changes in Foreign Exchange Rates.” Under PFRS, capitalization of foreign exchange losses is prohibited. Any undepreciated capitalized foreign exchange losses allowed under previous GAAP was adjusted against January 1, 2004 retained earnings and prior years’ consolidated financial statements presented were restated. The effect is a reduction in retained earnings of ₱1,784 (net of tax effect of ₱627) as of January 1, 2004 and ₱1,612 (net of tax effect of ₱570) as of December 31, 2004. This also reduced property, plant and equipment by ₱2,411 as of January 1, 2004 and ₱2,182 as of December 31, 2004. Cost of sales also decreased by ₱252 for 2004.

   PAS 21 also requires each individual entity to determine its functional currency and evaluate whether the activities of its foreign operations are carried out as an extension of the Parent Company. Ovincor was assessed to be an extension of the Parent Company and, as a result, the cumulative translation adjustment of ₱81 (net of tax effect of ₱38) and ₱85 (net of tax effect of ₱40) in prior years were reversed against retained earnings as of January 1, 2004 and December 31, 2004, respectively, while other income increased by ₱6 for 2004.

e. PAS 32, “Financial Instruments: Disclosure and Presentation” and PAS 39, “Financial Instruments: Recognition and Measurement.” Under PFRS, financial assets at FVPL, AFS investments and derivative financial instruments (including embedded derivatives) are recognized as assets or liabilities and measured at fair value. Moreover, PFRS requires more stringent impairment assessment for financial assets. Under previous GAAP, investments in marketable equity securities and investments in shares of stock were measured at the lower of aggregate cost or market.

   The Company availed of the exemption under PFRS 1 and account for PAS 32 and PAS 39 starting January 1, 2005. The cumulative effect of adopting this accounting standard was adjusted to January 1, 2005 stockholders’ equity.

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

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

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

f. PAS 40, “Investment Property.” The Company’s investment properties amounting to ₱183 as of January 1, 2004 and ₱171 as of December 31, 2004 were reclassified from “Building and related facilities” and “Land and leasehold improvements” accounts to “Investment properties” account in the consolidated balance sheets. Idle properties and properties purchased awaiting transfer of titles amounting to ₱16 as of January 1, 2004 and ₱31 as of December 31, 2004, previously presented as “Other noncurrent assets,” were also reclassified to investment properties. The Company opted to carry its investment properties using the cost model (see Note 4).

g. PFRS 3, “Business Combination.” Under previous GAAP, goodwill was amortized over 20 years. Under PFRS, the Company ceased annual goodwill amortization and commenced testing for impairment annually from January 1, 2004. The adoption of PFRS 3 has resulted in the reversal of a business combination previously accounted for under the purchase method. Since the acquisition does not qualify as business acquisition but a purchase of an asset, the resulting goodwill and subsequent amortization were reversed. The effect is an addition to retained earnings and reduction of other noncurrent assets by ₱9 as of January 1, 2004 and ₱5 as of December 31, 2004 and reduction of property, plant and equipment by ₱117 as of January 1, 2004 and December 31, 2004. The adoption of this standard also reduced deferred income tax liabilities by ₱126 in 2004, while other expenses was reduced by ₱4 for 2004.

h. The above adjustments increased (decreased) retained earnings at January 1, 2004 and December 31, 2004 as follows:

	January 1, 2004	December 31, 2004
Inventories (see Note a)	₱2,424	₱3,179
Property, plant and equipment (see Notes b and d)	(2,357)	(2,129)
Other noncurrent assets (see Notes c and g)	505	479
Other noncurrent liabilities (see Note b)	(225)	(256)
Other reserves (see Note d)	81	85
Increase in deferred income tax liabilities (see Notes a, b, c, d and g)	(217)	(593)
	₱211	₱765

i. The above changes decreased (increased) the deferred income tax liabilities as follows:

	January 1, 2004	December 31, 2004
Inventories (see Note a)	(₱776)	(₱1,017)
Property, plant and equipment (see Notes b and d)	610	554
Other noncurrent assets (see Note c)	(161)	(251)
Other noncurrent liabilities (see Note b)	72	81
Other reserves (see Note d)	38	40
	(₱217)	(₱593)

Effect on the Consolidated Cash Flows Statement for 2004

There are no material differences between the consolidated statement of cash flows prepared under PFRS and under previous GAAP.

Other Adopted PFRS

The Company has also adopted the following other PFRSs. Comparative presentation and disclosures have been amended as required by the standards. Adoption of these standards has no effect on stockholders' equity at January 1 and December 31, 2004.

- PAS 1, "Presentation of Financial Statements";
- PAS 8, "Accounting Policies, Changes in Accounting Estimates and Errors";
- PAS 10, "Events after the Balance Sheet Date";
- PAS 17, "Leases";
- PAS 24, "Related Party Disclosures";
- PAS 33, "Earnings per Share";
- PAS 36, "Impairment of Assets";
- PAS 38, "Intangible Assets";
- PFRS 2, "Share-based Payments";
- PFRS 4, "Insurance Contracts"; and
- PFRS 5, "Noncurrent Assets Held for Sale and Discontinued Operations."

Standards Not Yet Effective
The Company did not early adopt the following standards that have been approved but are not yet effective:

- PFRS 6, "Exploration for and Evaluation of Mineral Resources," effective 2006 — This standard is not relevant to the Company's business operations.

- PFRS 7, "Financial Instruments - Disclosures" — Additional disclosure requirements will be included when this standard takes effect in 2007.

4. Summary of Significant Accounting Policies

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

Financial Assets and Liabilities

Accounting Policies Effective January 1, 2005

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

The Company recognizes a financial asset or liability in the consolidated balance sheet when it becomes a party to the contractual provisions of the instrument. A financial liability (or a part of a financial liability) is derecognized when the obligation is extinguished. In the case of a regular way purchase or sale of financial assets, recognition and derecognition, as applicable, is done using settlement date accounting.

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

Financial assets are classified into the following categories: financial asset at FVPL, loans and receivables, held-to-maturity (HTM) investments, and AFS investments. The Company determines the classification at initial recognition and, where allowed and appropriate, re-evaluates this designation at every reporting date.

a. Financial Asset at FVPL

A financial asset is classified in this category if acquired principally for the purpose of selling or repurchasing in the near term or upon initial recognition, it is designated by the management as FVPL. Derivatives are also categorized as held at FVPL, except those derivatives designated and considered as effective hedging instruments. Assets classified under this category are carried at fair value in the consolidated balance sheet. Changes in the fair value of such assets are accounted for in earnings. Financial instruments held at FVPL are classified as current if they are expected to be realized within 12 months from the balance sheet date.

Classified as financial assets at FVPL are the Company's investments in marketable equity securities and proprietary membership shares (see Note 7).

b. Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments and are not quoted in an active market. Such assets are carried at cost or amortized cost in the consolidated balance sheet. Amortization is determined using the effective interest method. Loans and receivables are included in current assets if maturity is within 12 months from the balance sheet date. Otherwise, these are classified as noncurrent assets.

Classified as loans and receivables are the Company's trade and other receivables (see Note 10).

c. HTM Investments

HTM investments are quoted non-derivative financial assets with fixed or determinable payments and fixed maturities wherein the Company has the positive intention and ability to hold to maturity. HTM investments assets are carried at cost or amortized cost in the consolidated balance sheet. Amortization is determined by using the effective interest method. Assets under this category are classified as current assets if maturity is within 12 months from the balance sheet date and as noncurrent assets if maturity date is more than a year from the balance sheet date.

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

d. AFS Investments

AFS investments are those nonderivative financial assets that are designated as AFS or are not classified in any of the three preceding categories. After initial recognition, AFS sale financial assets are measured at fair value with gains or losses being recognized as a separate component of stockholders' equity until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the consolidated statement of income.

Classified as AFS investments are Petrogen's investments in government securities (see Note 8).

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

e. Derivative Financial Instruments

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

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

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

Accounting Policies Prior to January 1, 2005

a. Investments in Marketable Equity Securities

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

b. Investments in Shares of Stock

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

c. Derivative Financial Instruments

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

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

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

Gains and losses are recognized in net profit or loss when the liabilities are derecognized as well as through the amortization process.

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

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

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

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

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

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

Effective January 1, 2005

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

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

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

- the Company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

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

<u>Receivables</u>
Trade receivables are recognized and carried at original invoice amount less an allowance for any uncollectible amount. Provision is made when there is objective evidence that the Company will not be able to collect the debts. Bad debts are written off when identified.

Inventories

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

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

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

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

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

Interest in a Joint Venture

The Company's 33.33% joint venture interest in Pandacan Depot Services Inc. (PDSI) (see Note 12), incorporated on September 29, 2004 under the laws of the Republic of the Philippines, is accounted for under equity method of accounting. The interest in joint venture is carried in the consolidated balance sheets at cost plus post-acquisition changes in the Company's share of net assets of the joint venture, less any impairment in value. The consolidated statements of income reflect the Company's share in the results of operations of the joint venture.

Property, Plant and Equipment

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

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

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

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

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

The useful lives and depreciation and amortization method are reviewed periodically to ensure that the periods and method of depreciation and amortization are consistent with the expected pattern of economic benefits from the items of property, plant and equipment. The residual value, if any, is also reviewed and adjusted if appropriate, at each year end.

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

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

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

Investment Properties

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

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

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

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

Asset Impairment
The carrying values of long-lived assets are reviewed for impairment when events or changes in circumstances indicate that the carrying values may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amounts, the assets or cash-generating units are written down to their recoverable amounts. The recoverable amount of the asset is the greater of net selling price and value in use. The net selling price is the amount obtainable from the sale of an asset in an arm's-length transaction. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the smallest cash-generating unit to which the asset belongs. Impairment losses are recognized in the consolidated statements of income.

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

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

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

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

Borrowing Costs
Borrowing costs generally are expensed as incurred. For financial reporting purposes, interest on loans used to finance capital projects is capitalized as part of project costs (shown as part of "Construction in-progress" account in the consolidated balance sheets) during construction period. Capitalization of interest commences when the activities to prepare the asset are in progress and expenditures and interest are being incurred. Interest costs are capitalized until the assets are substantially ready for their intended use. If the carrying amount of the asset exceeds its

recoverable amount, an impairment loss is recognized. For income tax reporting purposes, such interest is treated as deductible expense in the period the interest is incurred.

Cylinder Deposits

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

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

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

Provisions

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

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

Revenue Recognition.

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

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

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

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

Operating Leases

Company as a Lessee. Operating lease payments are recognized as an expense in the consolidated statements of income on a straight-line basis over the lease terms.

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

Foreign Currency-Denominated Transactions and Translations

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

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

Income Taxes

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

Deferred Tax. Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not recognized if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted at the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

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

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

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

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

Earnings Per Share Attributable to the Equity Holders of the Parent
Basic earnings per share is computed based on the weighted average number of outstanding shares after giving retroactive effect to any stock split and stock dividends declared during the year. There are no dilutive potential common shares outstanding that would require disclosure of diluted earnings per share in the consolidated statements of income.

Segments
The Company's operating businesses are recognized and managed separately according to the nature of the products and invoices provided, with each segment representing a strategic business unit that offers different products and serves different markets. Financial information on business and geographical segments is presented in Note 34.

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

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

5. Significant Accounting Judgments and Estimates

The Company's financial statements prepared in accordance with PFRS require management to make judgments and estimates that affects amounts reported in the financial statements and related notes.

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

Operating Lease Commitments - Company as Lessor/Lessee. The Company has entered into commercial property leases on its investment property portfolio. The Company has determined that it retains all the significant risks and rewards of ownership of the properties leased out on operating leases while the significant risks and rewards for properties leased from third parties are retained by the lessors. Total lease income amounted to ₱280 and ₱274 in 2005 and in 2004, respectively (see Note 23), while lease expense amounted to ₱306 and ₱271 in 2005 and in 2004, respectively (see Note 22).

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

Financial Assets and Liabilities. PFRS requires that certain financial assets and liabilities be carried at fair value, which requires the use of accounting estimates and judgments. While significant components of fair value measurement are determined using verifiable objective evidence (i.e., foreign exchange rates, interest rates, volatility rates), the timing and amount of changes in fair value would differ with the valuation methodology used. Any change in the fair value of these financial assets and liabilities would directly affect income and stockholders' equity.

The aggregate fair value of the financial assets carried at fair value amounted to ₱599 as of December 31, 2005 (see Notes 7 and 8).

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

An increase in allowance for doubtful accounts would increase the Company's recorded selling and administrative expenses and decrease current assets. Provisions for doubtful accounts amounted to ₱106 in 2005 and ₱162 in 2004 (see Note 22). Receivables, net of allowance for doubtful accounts, amounted to ₱14,055 and ₱11,758 as of December 31, 2005 and 2004, respectively (see Note 10).

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

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

Inventories, net of allowance for obsolescence, amounted to ₱27,018 and ₱22,414 as of December 31, 2005 and 2004, respectively (see Note 11).

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

Property, plant and equipment and investment properties, net of accumulated depreciation and amortization as of December 31, 2005 and 2004 amounted to ₱22,777 and ₱22,648, respectively (see Notes 13 and 14).

Asset Impairment. Except for intangible assets with indefinite useful lives, PFRS requires that an impairment review be performed when certain impairment indicators are present. For intangible assets with indefinite useful lives, impairment testing is performed on an annual basis. Determining the net recoverable value of assets requires the estimation of cash flows expected to be generated from the continued use and ultimate disposition of such assets. While it is believed that the assumptions used in the estimation of fair values reflected in the consolidated financial statements are appropriate and reasonable, significant changes in these assumptions may materially affect the assessment of recoverable values and any resulting impairment loss could have a material adverse impact on the results of operations.

No impairment loss was recognized in 2005 and 2004. The aggregate carrying amount of property, plant and equipment and investment properties, net of accumulated depreciation amounted to ₱22,777 and ₱22,648 as of December 31, 2005 and 2004, respectively (see Notes 13 and 14).

Pension Costs. The determination of the obligation and cost for pension and other retirement benefits is dependent on the selection of certain assumptions used by actuary in calculating such amounts. Those assumptions are described in Note 27 and include, among others, discount rate and rate of compensation increase. In accordance with PAS 19, as amended, the Company recognizes all actuarial gains and losses in the consolidated statements of recognized income and expense, and therefore generally affects the recorded obligation. While it is believed that the Company's assumptions are reasonable and appropriate, significant differences in actual experience or significant changes in assumptions may materially affect the Company's pension obligations.

Net pension plan assets amounted to ₱1,137 and ₱783 as of December 31, 2005 and 2004, respectively (see Note 27). Actuarial gains or losses as of December 31, 2005 and 2004, included under "Other reserves" account in the consolidated balance sheets, amounted to ₱185 and ₱309, respectively.

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

Deferred income tax assets as of December 31, 2005 and 2004 amounted to ₱1,082 and ₱878, respectively (see Note 24).

Asset Retirement Obligation. Determining asset retirement obligation requires estimation of the costs of dismantling, installations and restoring leased properties to their original condition. The Company determined the amount of asset retirement obligation by obtaining estimates of dismantling costs from proponent who is responsible for the operation of the asset discounted at the Company's current borrowing rates ranging from 9.94% to 15.29% depending on the life of the capitalized costs. While it is believed that the assumptions used in the estimation of such costs are reasonable, significant changes in these assumptions may materially affect the recorded expense or obligation in future periods.

The Company has an asset retirement obligation arising from leased service stations and bulk plants. Such obligation is not expected to be settled for the foreseeable future and therefore a reasonable estimate of fair value cannot be determined. However, given the impact of discounting, any estimate of the asset retirement obligation may not likely be significant.

Asset retirement obligation as of December 31, 2005 and 2004 amounted to ₱298 and ₱256, respectively (see Note 19).

Contingencies. The Company currently has various tax assessments and legal claims. The Company develops estimate of the probable costs for the assessments and resolution of these claims in consultation with in-house as well as outside counsel handling the prosecution and defense of these cases and is based upon an analysis of potential results. The Company currently does not believe these tax assessments and legal claims will have a material adverse effect on its consolidated financial position and results of operations. It is possible, however, that future results of operations could be materially affected by changes in the estimates or in the effectiveness of strategies relating to these proceedings (see Note 35). No provision for contingencies was recognized in 2005 and 2004.

6. Cash and Cash Equivalents

	2005	2004
Cash on hand and in banks	**₱3,576**	₱3,430
Money market placements	**495**	674
	₱4,071	₱4,104

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

7. Financial Assets at FVPL

As of December 31, 2005, this account consists of:

Marketable equity securities	₱82
Proprietary membership shares	62
	₱144

In 2004, marketable equity securities are classified as short-term investments (see Note 9) and proprietary membership shares are classified as investments (see Note 12).

8. AFS Investments

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

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

Due in one year or less	₱259
Due after one year through five years	196
	₱455

In 2004, these are classified under "Investments" account (see Note 12).

9. Short-term Investments

As of December 31, 2004, this account consisted of:

Marketable equity securities	₱60
Short-term cash investments	3
	₱63

In 2005, the marketable equity securities are classified as financial assets at FVPL (see Note 7). In 2004, these securities are carried at the lower of aggregate cost or market value.

10. Receivables

	2005	2004
Trade	**₱11,890**	₱10,136
Others	**3,012**	2,327
	14,902	12,463
Less allowance for doubtful accounts	**847**	705
	₱14,055	₱11,758

Trade receivables are non-interest bearing and generally on 45-day term.

11. **Inventories**

	2005	2004 (As restated - see Note 3)
At cost:		
Petroleum	**₱14,624**	₱12,552
Crude oil and others	**11,947**	9,151
At net realizable value -		
TBA products, materials and supplies	**447**	711
	₱27,018	₱22,414

Using the moving-average method, the cost of petroleum, crude oil and other products would have increased by ₱619 as of December 31, 2005 and ₱242 as of December 31, 2004.

Cost of TBA products, material and supplies amounted to ₱881 as of December 31, 2005 and ₱980 as of December 31, 2004.

12. **Investments**

This account, included under "Other noncurrent assets" account in 2004 (see Note 15), consists of the following:

Notes and bonds - at amortized cost (see Note 8)	₱330
Shares of stock - at lower of cost or market (see Note 7)	69
Joint venture interest in PDSI	4
Other investment (net of allowance for decline in value of ₱594 in 2005 and ₱580 in 2004)	–
	₱403

- Investments in notes and bonds pertain to Petrogen's investment in government securities, which are classified as AFS investments in 2005 (see Note 8).

- Investments in shares of stock comprise of proprietary membership shares. In 2005, these are classified as financial assets at FVPL (see Note 7).

- The Company has a 33.33% joint venture interest in PDSI, which is involved in receiving, storing and handling the out-loading of petroleum products of the three major oil companies to serve the fuel requirements of their respective customers. PDSI was incorporated on September 29, 2004. In 2005, this joint venture interest is included under "Other noncurrent assets" account.

- Other investment consists of redeemable preferred voting shares of an institution under a court-approved rehabilitation plan. The Company provided full allowance for the cost of investment. In 2005, this is included under "Other noncurrent assets" account.

13. Property, Plant and Equipment

	Buildings and Related Facilities	Refinery and Plant Equipment	Service Stations and Other Equipment	Computers, Office and Motor Equipment	Land and Leasehold Improvements	Construction-in-Progress	Total
Net carrying amount, at January 1, 2005, as restated (Note 3)	₱5,510	₱9,358	₱540	₱433	₱917	₱5,688	₱22,446
Additions	195	–	16	8	1,861	368	2,448
Transfers	288	3,687	328	150	61	(4,514)	–
Depreciation and amortization for the year	(408)	(1,476)	(177)	(146)	(117)	–	(2,324)
Net carrying amount, at December 31, 2005	₱5,585	₱11,569	₱707	₱445	₱2,722	₱1,542	₱22,570
At January 1, 2005, as restated (Note 3)							
Cost	₱7,601	₱18,423	₱2,698	₱1,656	₱1,749	₱5,688	₱37,815
Accumulated depreciation and amortization	(2,091)	(9,065)	(2,158)	(1,223)	(832)	–	(15,369)
Net carrying amount	₱5,510	₱9,358	₱540	₱433	₱917	₱5,688	₱22,446
At December 31, 2005							
Cost	₱8,081	₱22,105	₱3,037	₱1,796	₱3,667	₱1,542	₱40,228
Accumulated depreciation and amortization	(2,496)	(10,536)	(2,330)	(1,351)	(945)	–	(17,658)
Net carrying amount	₱5,585	₱11,569	₱707	₱445	₱2,722	₱1,542	₱22,570

The Company has asset retirement obligation arising from leased service stations and bulk plants. Such obligation is not expected to be settled for the foreseeable future and therefore a reasonable estimate of fair value cannot be determined. However, given the impact of discounting, any estimate of the asset retirement obligation may not likely be significant.

Interest capitalized in 2005 amounted to ₱46 using a capitalization rate of 6.94% for peso loans. Interest capitalized in 2004 amounted to ₱98 using a capitalization rate of 8.24% for peso loans and 3.16% for dollar loans.

14. Investment Properties

	Land	Office Units	Total
Net carrying amount, at January 1, 2005, as restated	₱32	₱170	₱202
Additions	16	–	16
Depreciation and amortization for the year	–	(11)	(11)
Net carrying amount, at December 31, 2005	₱48	₱159	₱207
At January 1, 2005, as restated:			
Cost	₱32	₱235	₱267
Accumulated depreciation and amortization	–	(65)	(65)
Net carrying amount	₱32	₱170	₱202

	Land	Office Units	Total
At December 31, 2005:			
Cost	₱48	₱235	₱283
Accumulated depreciation and amortization	–	(76)	(76)
Net carrying amount	₱48	₱159	₱207

There are no available fair values for office units located in Petron Megaplaza and for the parcels of land in various locations intended for service stations.

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

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

15. Other Noncurrent Assets

	2005	2004 (As restated - see Note 3)
Net pension plan assets (see Note 27)	**₱1,137**	₱783
Others	**121**	569
	₱1,258	₱1352

In 2005, "Others" account includes joint venture interest in PDSI and other investments (see Note 12).

16. Short-term Loans

This account pertains to unsecured peso and dollar loans obtained from local banks at interest rates ranging from 5.5% to 8.3% for peso loans and 2.5% to 3.2% for dollar loans, intended to fund the importation of crude oil and petroleum products, capital expenditures and working capital requirements.

17. Accounts Payable and Accrued Expenses

	2005	2004
Accrued expenses	**₱1,406**	₱1,575
Accounts payable	**472**	1,208
Specific and other taxes payable	**336**	482
Derivative liabilities (see Note 32)	**5**	–
Others	**2,599**	1,820
	₱4,818	₱5,085

Terms and conditions of the above financial liabilities:

- Accounts payable are non-interest bearing and are normally settled on 30-day term.
- Accrual of unpaid interest, selling and administrative expenses which are normally settled within a year.
- Other payables include unearned income arising from trade related transactions.

18. **Long-term Debt**

	2005	2004
Syndicated dollar bank loan (net of debt issue costs amounting to ₱80 in 2005 and ₱100 in 2004)	**₱5,258**	₱5,534
Unsecured peso loans	**1,673**	3,288
	6,931	8,822
Less current portion (net of debt issue costs amounting to ₱21 in 2005 and ₱20 in 2004)	**1,906**	1,595
	₱5,025	₱7,227

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

Original Amount	NORD - LB US$100 million	Landbank - ₱2 billion	Citibank - ₱2 billion
Payment Terms	Six semi-annual installments starting on the 30th month from June 2004 up to June 2009	Eight equal quarterly installments starting December 2004 up to September 2006	13 equal quarterly installments starting April 2004 up to April 2007
Interest (2005)	4.2% to 5.9%	7.2% to 8.7%	7.8% to 9.7%
Security	None	None	None
Major Covenants	Maintenance of certain financial ratios	None	Maintenance of certain financial ratios

As of December 31, 2005, the Company is in compliance with its loan covenants. Loan maturities (gross of ₱80 debt issue costs) for the next 4 years are as follows:

Year	Amount
2006	₱1,927
2007	1,767
2008	2,122
2009	1,195
	₱7,011

19. **Other Noncurrent Liabilities**

	2005	2004 (As restated - see Note 3)
Asset retirement obligation	**₱298**	₱256
Cylinder deposits	**244**	274
Cash bonds	**119**	108
Others	**36**	29
	₱697	₱667

Movement of asset retirement obligation follows:

	2005	2004 (As restated - see Note 3)
Beginning balance	**₱256**	₱228
Additions for the year	**9**	–
Accretion	**33**	28
Ending balance	**₱298**	₱256

20. **Other Changes in Stockholders' Equity**

	Attributable to Equity Holders of the Parent			
		Retained Earnings		Minority
	Capital Stock	Appropriated	Unappropriated	Interest
Balance at December 31, 2004, as previously reported	₱9,375	₱6,906	₱4,858	₱110
Effect of changes in accounting policies (see Note 3)	–	–	765	–
Balance at December 31, 2004, as restated	9,375	6,906	5,623	110
Effect of change in accounting policy - PAS 39 (see Note 3)	–	–	(39)	(9)
Balance at January 1, 2005	9,375	6,906	5,584	101
Net income for the year	–	–	6,044	7
Actuarial gains due to limit on recognized plan asset - net of tax effect	–	–	408	–
Appropriated for capital projects	–	4,746	(4,746)	–
Cash dividends - ₱0.10 per share	–	–	(938)	–
Balance at December 31, 2005	₱9,375	₱11,652	₱6,352	₱108
Balance at December 31, 2003, as previously reported	₱9,375	₱5,551	₱4,663	₱103
Effect of changes in accounting policies (see Note 3)	–	–	211	–
Balance at December 31, 2003, as restated	9,375	5,551	4,874	103
Net income for the year	–	–	4,094	7
Actuarial losses due to limit on recognized plan asset - net of tax effect	–	–	(115)	–
Appropriated for capital projects	–	1,355	(1,355)	–
Cash dividends - ₱0.20 per share	–	–	(1,875)	–
Balance at December 31, 2004, as restated	₱9,375	₱6,906	₱5,623	₱110

a. Capital Stock

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

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

b. Retained Earnings

i. Declaration of Cash Dividends

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

ii. Appropriation for Capital Projects

Petron appropriated ₱4,746 in 2005 and ₱1,355 in 2004 for future capital projects.

21. **Cost of Goods Sold**

	2005	2004 (As restated - see Note 3)
Direct materials	**₱173,539**	₱132,850
Depreciation and amortization	**1,459**	1,009
Employee costs	**390**	353
Others	**1,572**	1,225
	₱176,960	₱135,437

22. Selling and Administrative

	2005	2004 (As restated - see Note 3)
Employee costs (see Note 27)	**₱1,023**	₱1,225
Depreciation and amortization	**876**	847
Purchased services and utilities	**748**	734
Maintenance and repairs	**567**	629
Advertising	**398**	403
Rental (see Note 26)	**306**	271
Materials and office supplies	**281**	260
Provision for doubtful accounts/accounts receivable written-off	**106**	162
Taxes and licenses	**102**	177
Others	**120**	169
	₱4,527	₱4,877

23. Interest Expense, Interest Income and Others

	2005	2004 (As restated - see Note 3)
Interest expense:		
Loans	**(₱1,615)**	(₱1,326)
Product borrowings	**(57)**	(87)
Accretion on asset retirement obligation (see Note 19)	**(33)**	(28)
Amortization of debt issue costs (see Note 18)	**(20)**	(10)
Others	**(366)**	(224)
	(₱2,091)	(₱1,675)
Interest income:		
Money market placements	**₱249**	₱180
Trade receivables	**42**	124
Product loaning	**13**	28
Cash in banks	**9**	8
Investment bonds	**–**	2
Others	**4**	2
	₱317	₱344

	2005	2004 (As restated - see Note 3)
Others:		
Rent income	**₱280**	₱274
Derivatives net fair value loss (see Note 32)	**(260)**	–
Foreign exchange gain (loss)	**56**	(259)
Reversal of allowance (provision) for decline in value of investments	**14**	(91)
Miscellaneous	**(176)**	(280)
	(₱86)	(₱356)

24. **Income Taxes**

The major components of income tax expense for the years ended December 31, 2005 and 2004 are:

	2005	2004 (As restated - see Note 3)
Current income tax -		
Current income tax charge	**₱2,057**	₱1,339
Deferred income tax:		
Relating to origination and reversal of temporary differences	**102**	(16)
Change in tax rate	**(68)**	–
	₱34	(₱16)

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

	2005	2004 (As restated - see Note 3)
Deferred tax assets:		
Inventory differential	**₱217**	₱77
Rental	**205**	195
Asset retirement obligation	**90**	77
Various allowances, accruals and others	**565**	529
Total (Carried Forward)	**1,077**	878

	2005	2004 (As restated - see Note 3)
Total (Brought Forward)	**₱1,077**	₱878
Deferred tax liabilities:		
Excess of double-declining over straight-line method of depreciation and amortization	**1,267**	1,098
Capitalized taxes and duties on inventories deducted in advance	**411**	431
Net pension plan asset	**341**	251
Capitalized interest, duties and taxes on property, plant and equipment deducted in advance and others	**571**	447
	2,590	2,227
	₱1,513	₱1,349

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

	2005	2004 (As restated - see Note 3)
Income tax computed at statutory income tax rates	**₱2,646**	₱1,736
Additions (reductions) resulting from:		
Income subject to income tax holiday (see Note 33)	**(440)**	(410)
Provision (reversal of allowance) for decline in value of investments	**(5)**	29
Interest income subjected to lower final tax and others	**(110)**	(32)
Provision for income tax	**₱2,091**	₱1,323

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

On May 24, 2005, the President of the Republic of the Philippines signed into law Republic Act No. 9337, which took effect on July 1, 2005. Introducing the following changes:

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

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

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

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

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

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

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

25. **Related Party Transactions**

The significant transactions with related parties are as follows:

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

			2004	
Name of Company	Relationship	Nature of Transaction	Transaction Amount	Balance at end of Year
Saudi Aramco	Ultimate parent of Aramco Overseas Company B.V. (Stockholder)	Crude purchases	₱73,711	₱3,963
PNOC	Stockholder	Leases	142	–

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

- Petron has long-term lease agreements with PNOC until August 2018 covering certain lots where its refinery and other facilities are located. Lease charges on refinery facilities escalate at 2% a year, subject to increase upon reappraisal (see Note 26).

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

	2005	2004
Salaries and other short-term employee benefits	**₱248**	₱232
Post-employment benefits	**42**	46
	₱290	₱278

26. Operating Lease Commitments

Company as Lessee

The Company entered into commercial leases on certain parcels of land. These leases have an average life of between 1 to 16 years with renewal options included in the contracts. There are no restrictions placed upon the Company by entering into these leases. The lease agreements include upward escalation adjustment of the annual rental rates.

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

	2005	2004
Within one year	**₱377**	₱382
After one year but not more than five years	**1,518**	1,508
After five years	**2,620**	3,102
	₱4,515	₱4,992

Company as Lessor

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

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

	2005	2004
Within one year	**₱168**	₱195
After one year but not more than five years	**175**	220
After five years	**141**	161
	₱484	₱576

27. **Pension Plan**

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

Net Pension Costs (Recognized in Selling and Administrative Expenses)

	2005	2004 (As restated - see Note 3)
Current service cost	**₱101**	₱106
Interest cost on benefit obligation	**239**	206
Expected return on plan assets	**(338)**	(305)
Net pension costs	**₱2**	₱7
Actual return on plan assets	**₱437**	₱394

Actuarial Gain (Loss) Recognized Directly in Stockholders' Equity

	2005	2004 (As restated - see Note 3)
Actuarial gain (loss) for the year due to present value of obligation	**(₱363)**	₱364
Actuarial gain for the year	**99**	90
Actuarial gains (losses) due to limit on recognized plan assets	**620**	(168)
Net actuarial gain recognized	**₱356**	₱286

Net Pension Asset

	2005	2004 (As restated - see Note 3)
Defined benefit obligation	**₱2,330**	₱1,709
Fair value of plan assets	**3,737**	3,382
Pension asset	**1,407**	1,673
Less unrecognized assets due to limit	**270**	890
Net pension asset recognized (see Note 15)	**₱1,137**	₱783

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

	2005	2004 (As restated - see Note 3)
Opening defined benefit obligation	**₱1,709**	₱1,821
Interest cost	**239**	206
Current service cost	**101**	106
Benefits paid	**(82)**	(60)
Actuarial loss (gain) on obligation	**363**	(364)
Closing defined benefit obligation	**₱2,330**	₱1,709

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

	2005	2004 (As restated - see Note 3)
Opening fair value of plan assets	**₱3,382**	₱3,047
Expected return	**338**	305
Contributions by employer	**–**	–
Benefits paid	**(82)**	(60)
Actuarial gains on plan assets	**99**	90
Closing fair value of plan assets	**₱3,737**	₱3,382

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

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

	2005	2004
Cash	**5%**	– %
Government securities	**71**	76
Stocks	**15**	14
Real estate	**8**	9
Others	**1**	1
	100%	100%

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

The principal assumptions used in determining obligations for the Company's plans are shown below:

	2005	2004
Discount rate	**11%**	14%
Expected rate of return on assets	**10%**	10%
Future salary increases	**8.5%**	9%

28. Supplementary Information

a. Processing License Agreement

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

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

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

In the bidding held last January 6, 2006 for NPC fuel requirements from January to April 2006, Petron won a total of 26,782 kilo-liters (KL) of diesel fuel and 199,617 KL of bunker fuel worth ₱772 and ₱4,066, respectively.

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

29. Earnings Per Share Attributable to Equity Holders of the Parent

	2005	2004 (As restated - see Note 3)
Net income attributable to equity holders of the parent	**₱6,044**	₱4,094
Weighted average number of shares	**9,375,104,497**	9,375,104,497
Earnings per share	**₱0.64**	₱0.44

30. Supplemental Disclosures of Cash Flow Information

Changes in operating assets and liabilities:

	2005	2004 (As restated - see Note 3)
Increase in assets:		
Receivables	**(₱2,084)**	(₱2,503)
Inventories	**(4,769)**	(4,316)
Other current assets	**(1,796)**	(69)
Increase (decrease) in liabilities:		
Liabilities for crude oil and petroleum product importation	**1,814**	(445)
Accounts payable and accrued expenses	**158**	706
	(6,677)	(6,627)
Provisions for doubtful accounts, inventory obsolescence and others	**351**	534
	(₱6,326)	(₱6,093)

31. Financial Risk Management Objectives and Policies

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

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

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

<u>Foreign Exchange Risk</u>
Foreign exchange risk occurs due to currency differences in the Company's assets and liabilities. The Company's foreign currency-denominated assets and liabilities were predominantly in US dollars in 2005 and 2004.

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

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

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

Interest Rate Risk
The Company's exposure to interest rate risk is mainly related to its long-term debt instruments which are all on a floating rate basis as of December 31, 2005.

In the future, the Company may enter into hedging arrangements to fix the interest rate for all or part of the long-term debt. Hedging decisions would be guided by an assessment of the over-all interest rate risk profile of the Company's balance sheets and the net effect on this of possible interest rate movements.

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

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

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

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

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

32. **Financial Instruments**

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

Freestanding Derivatives. The Parent Company uses IFO-Dubai crack spread swaps to protect its margin on export and domestic sales of industrial fuel oil products. The cost base of the Parent Company's industrial fuel is that of the crude oil, most of which is supplied by Saudi Aramco and is priced based on Dubai/Oman crude price. On the other hand, the selling price of the industrial fuel is based on MOPS. Under the crack spread swap, the Parent Company and its counterparties agree to a monthly exchange of cash settlements based on a specified reference price, depending on the commodity being hedged. For the IFO portion of the crack spread swap that hedges the price risks on industrial fuel oil products, the Company acts as the floating rate payer and the reference price index is the monthly MOPS for HSFO 180 CST. For the Dubai portion that hedges the price risks on crude oil, the Parent Company acts as the fixed rate payer and the reference price index is the monthly average for Platt's Dubai Crude. The swap agreements effectively hedge the Parent Company's margin on industrial fuel oil. As of December 31, 2005 and 2004, there are no outstanding commodity swaps.

The Parent Company also enters into deliverable and non-deliverable short-term currency forward contracts to hedge its foreign currency exposure on crude oil importations. As of December 31, 2005, the Parent Company has outstanding currency forward contracts with an aggregate notional amount of US$45, and weighted average contracted forward rate of ₱53.206 to US$1.00. The net fair value loss on these currency forward contracts as of December 31, 2005 amounted to ₱5. As of December 31, 2004, the Parent Company has no outstanding deliverable and non-deliverable short-term currency forward contracts.

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

Fair Value Changes on Derivatives

The net movements in fair value changes of all derivative transactions in 2005 are as follows:

	MTM Loss (Gain)
Fair values at January 1, 2005, as restated (see Note 3e)	₱31
Net changes in fair value during the year (see Note 23)	260
Less fair value of settled instruments	346
Balance at December 31, 2005 - net	(₱55)

Included in the consolidated balance sheets as:

Derivative assets (included under “Other current assets” account)	₱60
Derivative liabilities (see Note 17)	(5)
Net	₱55

Interest Rate Risk

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

	Interest Rates	Within 1 Year	1-2 years	2-3 Years	3-4 years	4-5 Years	More than 5 Years	Total
2005 Fixed Rate:								
Short-term debt (PHP)	7.0%	₱21,407	–	–	–	–	–	₱21,407
2005 Floating Rate:								
Long-term loan (Landbank)	7.2%	₱750	–	–	–	–	–	₱750
Long-term loan (Citibank)	8.0%	₱615	₱308	–	–	–	–	₱923
Long-term loan (NORD)	5.8%	$10	$28	–	$62	–	–	$100
2004 Fixed Rate:								
Short-term debt (USD)	2.8%	$30	–	–	–	–	–	$30
Short-term debt (PHP)	7.2%	₱16,787	–	–	–	–	–	₱16,787
2004 Floating Rate:								
Long-term loan (Landbank)	10.0%	₱1,000	₱750	–	–	–	–	₱1,750
Long-term loan (Citibank)	10.0%	₱615	₱615	₱308	–	–	–	₱1,538
Long-term loan (NORD)	3.7%	–	$10	$28	–	$62	–	$100

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

The Company has interest-bearing assets of ₱4,526 as of December 31, 2005 and ₱4,437 as of December 31, 2004, of which ₱4,330 and ₱4,174, respectively, have maturities within 1 year (see Notes 6, 8, 9 and 12). Financial assets at FVPL are non-interest bearing investments and are therefore not subject to interest rate volatility.

The following table sets forth the carrying values and estimated fair values of the Company's financial assets and liabilities recognized as of December 31, 2005.

	Carrying Value	Fair Value
Current financial assets:		
Cash and cash equivalents	₱4,071	₱4,071
Financial assets at FVPL	144	144
AFS investments	259	259
Receivables	14,055	14,055
Derivative assets (included under "Other current assets" account)	60	60
Total current financial assets	18,589	18,589
Noncurrent financial assets - AFS investments	196	196
Total financial assets	₱18,785	₱18,785
Current financial liabilities:		
Short-term loans	₱21,407	₱21,407
Liabilities for crude oil and petroleum product importation	7,911	7,911
Accounts payable and accrued expenses (including derivative liabilities)	2,219	2,219
Total current financial liabilities	31,537	31,537
Noncurrent financial liabilities:		
Cash bonds (included under "Other noncurrent liabilities" account)	119	98
Long-term debt (including current portion)	6,931	7,032
Total financial liabilities	₱38,587	₱38,667

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

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

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

Cash Bonds. Fair value is estimated as the present value of all future cash flows discounted using the applicable rates for similar types of instruments. Discount rate used is 9.97%.

Long-term Debt - Floating Rate. For variable rate loans that reprice every three months, the carrying value approximates the fair value because of recent and regular repricing based on current market rates. For variable rate loans that reprice every six months, the fair value is determined by discounting the principal amount plus the next interest payment using the prevailing market rate for the period up to the next repricing date. Average discount rate used is 4.41%.

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

33. Registration with the BOI

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

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

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

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

c. Simplified custom procedures and others.

In October 2003, the BOI approved Petron's application under Republic Act 8479, otherwise known as the Downstream Oil Industry Deregulation Act (RA 8479), for new investments at its Bataan Refinery for an Isomerization Unit and a Gas Oil Hydrotreater (Project). The BOI is extending the following major incentives:

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

b. Duty of three percent and value added tax (VAT) on imported capital equipment and accompanying spare parts;

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

d. Exemption from contractor's tax.

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

On October 20, 2005, Petron registered with the BOI under the Omnibus Investments Code of 1987 (Executive Order 226) as (1) a non-pioneer, new export producer status of Mixed Xylene (2) a pioneer, new export producer status of Benzene and Toluene and (3) a pioneer, new domestic producer status of Propylene. Under the terms of its registration, Petron is subject to certain requirements principally that of producing required metric tons of the mentioned petrochemical products every year.

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

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

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

c. Simplification of custom procedures and others.

On October 21, 2005, the BOI approved Petron’s application under RA 8479 for new investment at its Bataan Refinery for a Petro Fluid Catalytic Cracking Unit. Subject to Petron’s compliance with the terms and conditions of registration, the BOI is extending the following major incentives:

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

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

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

d. Exemption from contractor’s tax.

In December 2005, the BOI approved Petron’s application under RA 8479 as an Existing Industry Participant with New Investment in Modernization of the firm’s Grease Manufacturing Plant in Pandacan, Manila. The BOI is extending the following major incentives:

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

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

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

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

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

f. Exemption from contractor's tax.

34. Segment Information

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

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

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

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

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

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

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

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

	Petroleum	Insurance	Leasing	Marketing	Elimination	Total
Year Ended December 31, 2005						
Revenue:						
Total revenue	**₱191,228**	**₱539**	**₱316**	**₱2,026**	**(₱2,620)**	**₱191,489**
Segment results	**9,436**	**512**	**303**	**21**	**(270)**	**10,002**
Net income	**5,765**	**166**	**34**	**29**	**57**	**6,051**
Assets and liabilities:						
Segment assets	**69,403**	**1,369**	**2,347**	**587**	**(2,631)**	**71,075**
Segment liabilities	**41,711**	**150**	**1,800**	**205**	**(1,919)**	**41,947**
Other segment information:						
Property, plant and equipment	**19,871**	**1**	**1**	**429**	**2,268**	**22,570**
Depreciation and amortization	**2,315**	**–**	**–**	**20**	**–**	**2,335**
Year Ended December 31, 2004 (As restated - see Note 3)						
Revenue:						
Total revenue	₱147,356	₱531	₱249	₱663	(₱1,374)	₱147,425
Segment results	6,588	505	229	–	(211)	7,111
Net income	3,887	158	35	13	8	4,101
Assets and liabilities:						
Segment assets	61,561	1,222	2,231	419	(2,304)	63,129
Segment liabilities	39,285	137	1,674	81	(1,720)	39,457
Other segment information:						
Property, plant and equipment	20,029	2	–	163	2,252	22,446
Depreciation and amortization	1,848	–	–	8	–	1,856

The following tables present additional information on the petroleum business segment of the Company for 2005 and 2004:

	Retail	Lube	Gasul	Industrial	Marketing	Total
Year Ended December 31, 2005:						
Revenue	**₱82,621**	**₱1,406**	**₱8,351**	**₱68,776**	**₱30,074**	**₱191,228**
Property, plant and equipment	**4,450**	**603**	**195**	**52**	**14,497**	**19,797**
Capital expenditures	**327**	**–**	**30**	**–**	**1,058**	**1,415**
Year Ended December 31, 2004 (As restated - see Note 3):						
Revenue	₱65,075	₱1,107	₱7,650	₱54,594	₱18,930	₱147,356
Property, plant and equipment	4,608	12	206	65	15,255	20,146
Capital expenditures	577	2	37	21	4,996	5,633

Geographical Segments

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

	Petroleum	Insurance	Leasing	Marketing	Elimination/ Others	Total
Year Ended December 31, 2005						
Revenue:						
Local	**₱167,703**	**₱464**	**₱316**	**₱2,026**	**(₱2,619)**	**₱167,890**
Export/International	**23,525**	**74**	**–**	**–**	**–**	**23,599**
Year Ended December 31, 2004 (As restated - see Note 3)						
Revenue:						
Local	₱134,275	₱463	₱249	₱663	(₱1,374)	₱134,276
Export/International	13,081	68	–	–	–	13,149

35. **Other Matters**

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

In November 1999, the Department of Finance (DOF) Center ExCom cancelled Tax Debit Memos (TDMs) worth ₱475, the related TCCs and their assignments. The BIR implemented this with a letter of assessment worth ₱651 deficiency taxes (inclusive of interest and charges) for the years 1995 to 1997, as a result of the cancellation. The Company contested on the grounds that the assessment has no factual and legal basis and that the cancellation of the TDMs was void. The Company elevated this protest to the CTA on July 10, 2000 where the case is still pending.

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

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

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

Petron officers who were already arraigned in the first Sandiganbayan case went up to the SC after the Sandiganbayan reversed an earlier ruling dismissing the case for failure on the part of the Ombudsman to prosecute.

b. Petron has unused letters of credit totaling approximately ₱30 as of December 31, 2005 and ₱12 as of December 31, 2004.

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

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

Beyond CAA compliance, Petron is the only oil company that has invested substantial resources to upgrade its production capabilities to meet CAA specifications. In January 2005, it commissioned its Isomerization Unit that will enable the Company to produce isomerates for blending with gasoline to meet current specifications. The unit is part of the US$100 million refinery project that also includes a Gas Oil Hydrotreater that was commissioned in April 2005. With these two units, Petron is the only domestic oil firm that can serve the local market's demand for CAA-compliant fuels entirely from local production.

d. Pandacan Terminal Operations

The City Council of Manila (City Council), citing concerns of safety, security and health, passed City Ordinance No. 8027 reclassifying the areas occupied by the Oil Terminals of Petron, Shell and Caltex from Industrial to Commercial, making the operation of the terminals therein unlawful.

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

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

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

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

Simultaneous with the Scale Down Program, Petron filed a petition with the Regional Trial Court (RTC) to annul the City Ordinance and enjoin the City Council of Manila, as well as the Mayor of Manila, from implementing the same. The RTC issued a status quo order which prevents the respondents from enforcing the Ordinance until further orders of the Court or termination of the case. The case has been referred to and is undergoing mediation before the Philippine Mediation Center.

e. Navotas Business Tax

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

f. Ownership of LPG Cylinders in the Market

Liquefied Petroleum Gas Marketers Association (LPGMA), a group of independent refillers of LPG claims to have acquired ownership of LPG cylinders of Petron, Pilipinas Shell and Total Philippines in good faith. LPGMA claims it can exercise all rights of ownership over the cylinders, praying judgment from the RTC of Pasig City authorizing its members to repaint/obliterate the marks on the oil companies’ LPG cylinders and all LPG cylinders which now or in the future may come into their possession; or to compel the parties to enter into a swapping arrangement and/or compelling the oil companies to buy back the cylinders.

On July 18, 2005, the RTC dismissed the petition for non-exhaustion of administrative remedies. LPGMA’s Motion for Reconsideration is pending resolution by the RTC. On March 1, 2006, the RTC denied LPGMA’s Motion for Reconsideration.

COVER SHEET

3	1	1	7	1

SEC Registration Number

PETRON CORPORATION AND SUBSIDIARIES

(Company's Full Name)

Petron MegaPlaza, 358 Sen. Gil Puyat Avenue, Makati City

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

Luis A. Maglaya
(Contact Person)

886-3888
(Company Telephone Number)

1	2		3	1

Month *Day*
(Fiscal Year)

1	7	-	A	

(Form Type)

Month *Day*
(Annual Meeting)

(Secondary License Type, If Applicable)

Dept. Requiring this Doc.

Amended Articles Number/Section

Total Amount of Borrowings

Total No. of Stockholders

Domestic

Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document ID

Cashier

S T A M P S

PETRON CORPORATION AND SUBSIDIARIES

SUPPLEMENTARY SCHEDULES
TO THE CONSOLIDATED FINANCIAL STATEMENTS
REQUIRED BY THE SECURITIES AND EXCHANGE COMMISSION
FOR THE YEAR ENDED DECEMBER 31, 2005
AND AUDITORS' REPORT

Philippine Pesos

PETRON CORPORATION AND SUBSIDIARIES
INDEX TO SUPPLEMENTARY SCHEDULES
FORM 17-A, Item 7

PETRON

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

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

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

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

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

NICASIO I. ALCANTARA
Chairman

KHALID D. AL-FADDAGH
President and Chief Executive Officer

MA. CONCEPCION F. DE CLARO
Controller

SUBSCRIBED AND SWORN TO before me, a Notary Public for and in the City of Makati, Metro Manila, this April 18 2006, affiants being personally known to me and signed this instrument in my presence and avowed under penalty of law to the whole truth of contents thereof.

Doc. No. 569;
Page No. 75;
Book No. VII;
Series of 2006

ROMMEL L. BAWALAN
Notary Public for Makati City
Notary Commission No. M-218
Until December 31, 2007
PTR No. ...45DAV 1.11.06 Cavite
Roll of Attorney No. 42921
PETRON MegaPlaza Bldg. 358 Sen. Gil Puyat Ave.
Makati City

SGV & Co

■ SyCip Gorres Velayo & Co.
6760 Ayala Avenue
1226 Makati City
Philippines

■ Phone: (632) 891-0307
Fax: (632) 819-0872
www.sgv.com.ph

BOA/PRC Reg. No. 0001
SEC Accreditation No. 0012-F

Report of Independent Auditors
On Supplementary Schedules

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

We have audited in accordance with generally accepted auditing standards, the consolidated financial statements of Petron Corporation and Subsidiaries included in this Form 17-A and have issued our report thereon dated April 4, 2006. Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedules listed in the Index to Financial Statements and Supplementary Schedules are the responsibility of the Company's management. These schedules are presented for purposes of complying with the Securities Regulation Code (SRC) Rule 68.1 and are not part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

SYCIP GORRES VELAYO & CO.

Wilson P. Tan

Wilson P. Tan
Partner
CPA Certificate No. 76737
SEC Accreditation No. 0100-A
Tax Identification No. 102-098-469
PTR No. 4181277, January 2, 2006, Makati City

April 4, 2006

PETRON CORPORATION AND SUBSIDIARIES
SCHEDULE E. INTANGIBLE ASSETS - OTHER ASSETS
DECEMBER 31, 2005

Description	Beginning Balance	Additions at Cost	Charged to Cost and Expenses	Charged to Other accounts	Other Changes Additions (Deductions)	Ending balance
SAP Software						
Cost	₱ 50,395,608	₱ -	₱	₱ -	₱ -	₱ 50,395,608
Less amortization for the year	-	-	40,316,486	-	-	40,316,486
Net book value	50,395,608	-	40,316,486	-	-	10,079,122
Franchise Fee						
Cost	2,116,140	2,777,273	-	-	-	4,893,413
Less amortization for the year	189,518	-	401,713	-	-	591,231
Net book value	1,926,622	2,777,273	401,713	-	-	4,302,182
BALANCE	₱ 52,322,230	₱ 2,777,273	₱ 40,718,199	₱ -	₱ -	₱ 14,381,304

PETRON CORPORATION AND SUBSIDIARIES
SCHEDULE F. LONG TERM DEBT
DECEMBER 31, 2005

Title of Issue and Type of Obligation	Amount Authorized by Indenture	Amount Shown as Current	Amount Shown as Long-term	Terms
Syndicated dollar bank loan (net of debt issue costs amounting to P79,647,825)	₱ 5,258,422,175	₱ 540,154,204	₱ 4,718,267,972	interest - 4.2% to 5.9%; periodic installments - six semi-annual installments; maturity date - June 2009
Unsecured peso loans				
Landbank	750,000,000	750,000,000	-	interest - 7.2% to 8.7%; periodic installments - eight equal quarterly installments; maturity date - September 2006
Citibank	923,076,923	615,384,615	307,692,308	interest - 7.8% to 9.7%; periodic installments - 13 equal quarterly installments; maturity date - April 2007
TOTAL	₱ 6,931,499,098	₱ 1,905,538,819	₱ 5,025,960,280	

PETRON CORPORATION AND SUBSIDIARIES
SCHEDULE I. CAPITAL STOCK
DECEMBER 31, 2005

Title of Issue	Number of Shares Authorized	Number of Shares Issued and Outstanding	Number of Shares Reserved for Options, Warrants, Conversions, and Other Rights	Number of Shares Held By		
				Affiliates	Directors, Officers and Employees	Others
Common Stock	10,000,000,000	9,375,104,497		7,500,000,000	3,709,068	1,871,395,429