

**Free Translation**

**Elektra Noreste, S.A.**

**(a 51% owned subsidiary of Panama  
Distribution Group, S.A.)**

**Financial Statements  
For December 31, 2008 and 2007**

**Elektra Noreste, S.A.****(a 51% owned subsidiary of Panama Distribution Group, S.A.)****Financial Statements December 31, 2008 and 2007**

<b>Table of Contents</b>	<b>Page</b>
Management Report	1
Financial Statements:	
Balance Sheets	2
Statements of Income	3
Statements of Changes in Equity	4
Statements of Cash Flows	5 - 6
Notes to Financial Statements	7 - 27



## **Management Responsibility for Financial Reporting**

The management of Elektra Noreste, S.A. is responsible for the information and representations in the Company's financial statements. The Company prepares the financial statements in accordance with accounting principles generally accepted in the United States of America based upon available facts and circumstances and management best estimates and judgments of known conditions.

The Company maintains an accounting system and related system of internal controls designed to provide reasonable assurance to Elektra's management regarding the preparation of reliable financial statements and that the financial records are accurate and Company's assets are protected. The Company's staff of internal auditors conducts periodic reviews to maintain the effectiveness of internal control procedures, corrective actions are taken to address control deficiencies and other opportunities for improving the system as they are identified.

Based on our knowledge, the financial statements as of December 31, 2008, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented.

Javier Pariente  
Executive Vice-president &  
General Manager

Eric Morales  
Chief Financial Officer  
C.P.A. #1769

February 6, 2009  
Panama, Republic of Panama



**Elektra Noreste, S.A.**

(a 51% owned subsidiary of Panama Distribution Group, S.A.)

**Statements of Income (unaudited)  
For the twelve months ended December 31, 2008 and 2007  
(Expressed in United States dollars)**

	Notes	2008	2007
Revenues:			
Net energy sales		\$ 506,430,023	\$ 348,992,369
Other revenues		<u>8,353,772</u>	<u>7,167,871</u>
Total revenues		514,783,795	356,160,240
Purchase of energy and transmission charges, net	6	<u>433,712,618</u>	<u>280,426,578</u>
Gross distribution margin		<u>81,071,177</u>	<u>75,733,662</u>
Operating expenses:			
Labor and other personnel		9,027,864	8,116,471
Severance expenses		301,258	329,965
Provision for doubtful account, net		3,988,870	3,077,136
Repair and maintenance		2,853,097	2,800,749
Professional services		9,556,987	8,908,255
Management fees		1,951,682	1,861,866
Depreciation and amortization		13,097,654	12,510,175
Administrative and other		8,175,146	7,570,033
Loss on sale of fixed asset		<u>234,213</u>	<u>48,532</u>
Total operating expenses		<u>49,186,771</u>	<u>45,223,182</u>
Operating income		<u>31,884,406</u>	<u>30,510,480</u>
Other income (expense):			
Other income		289,361	366,167
Interest income		1,807,515	1,593,531
Interest expense		<u>(9,268,445)</u>	<u>(8,412,634)</u>
Total other expenses		<u>(7,171,569)</u>	<u>(6,452,936)</u>
Income before income taxes		<u>24,712,837</u>	<u>24,057,544</u>
Income taxes expenses	4	<u>7,328,171</u>	<u>7,292,785</u>
Net income		<u>\$ 17,384,666</u>	<u>\$ 16,764,759</u>

See accompanying notes to financial statements.

**Elektra Noreste, S.A.**

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**Statements of Changes in Equity (unaudited)  
For the twelve months ended December 31, 2008 and 2007  
(Expressed in United States dollars)**

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	<b>Common Stock</b>	<b>Treasury Stock</b>	<b>Retained Earnings</b>	<b>Total Equity</b>
Balance as of January 1, 2007	\$ 106,642,962	\$ (544,087)	\$ 16,954,728	\$ 123,053,603
Dividends declared			(10,000,000)	(10,000,000)
Net income			16,764,759	16,764,759
Accredited complementary dividend tax			380,280	380,280
Complementary dividend tax paid	_____	_____	(550,287)	(550,287)
Balance as of December 31, 2007	106,642,962	(544,087)	23,549,480	129,648,355
Net income			17,384,666	17,384,666
Dividends declared			(23,549,480)	(23,549,480)
Accredited complementary dividend tax			775,202	775,202
Complementary dividend tax paid	_____	_____	(605,196)	(605,196)
Balance as of December 31, 2008	<u>\$ 106,642,962</u>	<u>\$ (544,087)</u>	<u>\$ 17,554,672</u>	<u>\$ 123,653,547</u>

See accompanying notes to financial statements.

## Elektra Noreste, S.A.

(a 51% owned subsidiary of Panama Distribution Group, S.A.)

### Statements of Cash Flows (unaudited)

For the twelve months ended December 31, 2008 and 2007

(Expressed in United States dollars)

	2008	2007
Cash flows from operating activities:		
Net income	\$ 17,384,666	\$ 16,764,759
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,097,654	12,510,175
Loss on sale of fixed asset	234,213	48,532
Provision for doubtful accounts	3,988,870	3,077,136
Discount amortization of senior notes	36,067	33,443
Amortization of debt issuance costs	114,668	100,087
Provision for severance payments net of contribution to severance fund	(36,039)	53,392
Deferred income tax	(1,638,948)	4,890,112
Fuel component adjustment	5,023,000	(14,331,000)
Change in operating assets and liabilities:		
Accounts receivable	(18,425,790)	(7,403,414)
Other assets	(218,272)	(290,831)
Inventory	845,867	(1,053,510)
Trade accounts payable and other liabilities	(10,121,650)	13,127,357
Income tax	6,865,105	(8,792,307)
Complementary Tax	170,006	(170,007)
Seniority premium	53,656	(86,349)
Net cash provided by operating activities	<u>17,373,073</u>	<u>18,477,575</u>
Cash flows from investing activities:		
Acquisition of fixed assets	(19,711,985)	(20,510,471)
Proceeds from sales of fixed assets	<u>238,493</u>	<u>165,895</u>
Net cash used in investing activities	<u>(19,473,492)</u>	<u>(20,344,576)</u>

(Continued)

**Elektra Noreste, S.A.**

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**Statements of Cash Flows (unaudited)****For the twelve months ended December 31, 2008 and 2007****(Expressed in United States dollars)**

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## Cash flows from financing activities:

Proceeds from Long-term debt	\$ 20,000,000	\$
Short-term debt, net	25,000,000	
Dividends paid	(23,549,480)	(10,000,000)
Debt issuance costs	<u>(375,814)</u>	<u></u>
Net cash provided (used) in financing activities	<u>21,074,706</u>	<u>(10,000,000)</u>

## Cash and cash equivalents:

Net increase (decrease) in cash for the period	18,974,287	(11,867,001)
Beginning of the period	<u>6,399,567</u>	<u>18,266,568</u>
Cash at the end of the period	<u>\$ 25,373,854</u>	<u>\$ 6,399,567</u>

## Supplemental disclosure of cash flow information:

Interest paid, net of amounts capitalized	<u>\$ 8,507,318</u>	<u>\$ 7,929,759</u>
Income tax paid	<u>\$ 2,102,015</u>	<u>\$ 11,194,962</u>

(Concluded)

See accompanying notes to financial statements.



**Elektra Noreste, S.A.****(a 51% owned subsidiary of Panama Distribution Group, S.A.)****Notes to financial statements****For the twelve months ended December 31, 2008 and 2007****(Expressed in United States dollars)****1. Nature of Organization and Operations*****Nature of Business***

Elektra Noreste, S.A. (the Company) is a corporation formed as a result of the privatization of the Institute for Hydraulic Resources and Electricity (Instituto de Recursos Hidráulicos y Electrificación (“IRHE”) in Spanish). The Company was incorporated by means of Public Deed No.143, dated January 19, 1998, and began operations in January 1998. The authorized capital stock of the Company consists of fifty million common shares without par value. At present, Panama Distribution Group, S.A. (“PDG”) owns 51% of the authorized, issued and outstanding shares of common stock of the Company, while the Panamanian Government and former employees of IRHE own 48.25% and 0.43%, respectively. The remaining amount of shares is held as treasury stock.

The activities of the Company include the purchase of energy in blocks and its transportation through the distribution network to customers. The Company performs voltage transformation, delivers the power to end consumers, and performs meter reading, billing and collections. The Company is also responsible for installing, operating, and maintaining public lighting in the concession zone (as defined in the following paragraph), according to the lighting levels and criteria established by the Public Services Authority (Autoridad Nacional de los Servicios Públicos (“ASEP”) in Spanish). Additionally, the Company is authorized to perform power generation activities up to a limit of 15% of the maximum demand and energy in the concession zone.

According to the concession contract described in Note 7, the Company has exclusivity for the distribution and commercialization of electric power to customers located in the geographical areas of Panama East, Colon, Panama Bay, the Comarca of San Blas and Darien. In regard to “large customers,” defined by Law 6, dated February 3, 1997, as customers with a maximum demand over 100 KW per site that have the option to purchase energy directly from other agents of the electricity market, the Company has exclusivity for only the distribution of electricity.

***Basis of Presentation***

The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”). The financial statements have been prepared on the historical cost basis.

**Elektra Noreste, S.A.**  
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**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

## **2. Significant Accounting Policies**

A summary of the significant accounting policies used in the preparation of the accompanying financial statements follows:

- a. Cash and Cash Equivalents** - All highly liquid investments with original maturities of three months or less are classified as cash equivalents.
- b. Accounts Receivable** - Accounts receivable are recorded at the invoiced amount and bear interest on past due amounts. The interest is recognized up until customer account is closed or terminated, which occurred approximately 60 days after the electric suspension.

It is the Company's policy to review outstanding accounts receivable on a monthly basis and adjust the corresponding allowance for doubtful accounts.

The Company establishes a provision for losses if it determines that amounts may not be collectible. The Company estimates the allowance based on the length of time the receivables are past due, conditions affecting its customers, and historical experience.

Account balances are written off after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance-sheet credit exposure related to its customers.

- c. Fuel Component Adjustment** - The regulated system under which the Company operates provides that any excess or deficiency between the estimated energy costs included in the tariff and the actual costs incurred by the Company be included as a compensation adjustment to be recovered from or refunded to customers in the next tariff charges semi annual adjustment. Any excess in energy costs charged to customers is accrued in the accounts payable on the balance sheet and leads to a reduction in the next tariff charges adjustment. Conversely, any deficit in energy cost charged to customers is accrued in the account receivable on the balance sheet and leads to an increase in the next tariff charges adjustment to be recovered from customers.

**Elektra Noreste, S.A.**

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**Notes to financial statements**

**For the twelve months ended December 31, 2008 and 2007**

**(Expressed in United States dollars)**

- d. Inventory** - Inventory consists primarily of materials, spare parts and supplies for the Company's consumption. Inventory is accounted for at the lower of cost or market. Cost is determined using the average cost method.
- e. Property, Plant, and Equipment** - Upon the Company's formation, the IRHE transferred a portion of its productive assets stated at historical cost net of the associated accumulated depreciation. New asset acquisitions and construction in progress are recorded at their original cost which includes materials, contractor costs, construction overhead and financing costs. The Company reports property, plant and equipment on the balance sheet net of accumulated depreciation.

Costs associated with improvements made to property, plant and equipment are capitalized as well as major disbursements for renewals. Costs associated with repairs and minor replacements are expensed as incurred. Major maintenance costs procedures that do not extend the useful life by improving the conditions of the asset to the state it held when it was originally purchased are also expensed. The Company also capitalizes interest during construction in accordance with Statement of Financial Accounting Standards ("SFAS") No.34, "Capitalization of Interest Costs".

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable through operations, in accordance with SFAS No.144, "Accounting for the Impairment or Disposal of Long-Lived Assets." If the carrying amount of the asset exceeds the expected undiscounted future cash flows generated by the asset or group of assets, an impairment loss is recognized and the asset is written down to its fair value. Fair value can be determined by the use of quoted market prices, appraisals or other valuation techniques, such as expected discounted future cash flows. Management judgment is involved in both deciding whether testing for recoverability is necessary and estimating undiscounted cash flows. As of December 31, 2008 and 2007, no impairments of long-lived assets were identified.

Gains or losses on property, plant and equipment are recognized when the assets are retired or otherwise disposed of. The difference between the net book value of the property and any proceeds received for the property is recorded as a gain or loss.

**Elektra Noreste, S.A.****(a 51% owned subsidiary of Panama Distribution Group, S.A.)****Notes to financial statements****For the twelve months ended December 31, 2008 and 2007****(Expressed in United States dollars)**

Depreciation and amortization are calculated on the straight-line method over the estimated useful lives of the assets. Estimated useful lives used for each fixed asset category are shown below:

	<b><u>Estimated Useful Life (in years)</u></b>
Poles, towers and accessories	30 to 40
Electric transformers	30
Underground conductors and ducts	40
Overhead conductors and accessories	25 to 35
Substation equipment	30
Consumer meters	30
Buildings and improvements	25 to 40
Public lighting equipment	25
Transportation and communications equipment	8 and 15
Office furniture and equipment	5 to 20

- f. **Debt Issuance Costs*** - The Company defers all costs related to the issuance of long-term debt. These costs include borrowers' commissions and other costs such as legal, registration and stamp costs. Debt issuance costs are amortized over the term of the debt instrument using the effective interest method.
- g. **Purchased Energy and Transmission Charges*** - The Company records the annual cost of purchased energy obtained under long-term and short-term contracts in the Statements of Income. These contracts are considered executory in nature, since they do not convey to the Company the right to use the related property, plant or equipment. The Company also engages in short-term hourly purchases in the wholesale market, which is administered by the National Dispatch Center (Centro Nacional de Despacho ("CND") in Spanish).

The Company also pays a regulated tariff to ETESA, a company fully-owned by the Panamanian Government for connecting to and for use of the transmission system. ETESA is responsible for expanding and upgrading the interconnecting transmission system to meet the requirements of demand growth and system stability. The current transmission tariff is due to remain in force until June 30, 2009, thereafter the tariff is revised by ETESA and the ASEP for a four-year period.

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**Notes to financial statements**

**For the twelve months ended December 31, 2008 and 2007**

**(Expressed in United States dollars)**

- h. Income Taxes** - Income taxes are accounted for under the asset-liability method as prescribed by SFAS No.109, "Accounting for Income Taxes." Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the Statement of Income in the period that includes the enactment date.
- i. Investment Tax Credit** - The Company accounts for Investment Tax Credit ("ITC") under the flow-through accounting method (full recognition in the period the asset is placed in service). Thus, a future deductible temporary difference exists, with which a deferred income tax asset is associated.
- j. Customer Deposits** - The Company requires customers to provide cash deposits as a guarantee of payment for energy consumed, according to the legislation set forth by the ASEP. The ASEP has issued resolutions JD-219 (March 31, 1998) and JD-761 (June 8, 1998) which provide that in those cases where the customer has established a good payment record, defined as no more than three late payments in a twelve-month period, the deposit shall be returned.
- k. Contingencies** - In the normal course of business, the Company is subject to various regulatory actions, proceedings, and lawsuits related to tax or other legal matters. The Company establishes reserves for these potential contingencies when they are deemed probable and reasonably estimable. For further discussion of contingencies, see Note 7.
- l. Seniority Premium and Severance Fund** - According to the Panamanian Labor Code, upon the termination of any employee contracted for an indefinite period of time, regardless the cause, the employee is entitled to a seniority premium at the rate of one week's salary for every year of work, since they were first employed. Seniority premiums represent 1.92% of total salaries paid.

Law 44 of 1995 introduced reforms to the Panamanian Labor Code by requiring all employers to make a cash contribution to a severance fund that would cover the payment to employees of a seniority premium and severance for unjustified dismissal. The Company maintains a trust fund through an authorized private entity, Progreso, S. A., who acts as trustee to secure the severance fund liability.

**Elektra Noreste, S.A.****(a 51% owned subsidiary of Panama Distribution Group, S.A.)****Notes to financial statements****For the twelve months ended December 31, 2008 and 2007****(Expressed in United States dollars)**

**m. *Related Parties*** - As a result of the restructuring of the electricity sector of Panama, three distribution companies, four generating companies and one transmission company were formed. The Panamanian Government retains an approximate fifty-one percent (51%) interest in the hydraulic generating companies, a forty-nine percent (49%) interest in the thermal generating company and distribution companies, and a one hundred percent (100%) interest in the transmission company. The Panamanian Government retained 48.25% of the Company's stock and 0.43% is owned by former IRHE employees.

In the normal course of business, the Company purchases electricity from the generating and other distribution companies, sells energy to governmental institutions and makes payments to the transmission company. The Company recognizes these activities as related party transactions.

The Company entered into a Management Consulting Agreement with CPI, Ltd., which owns 100% of the PDG shares. PDG owns 51% of the Company's authorized issued and outstanding shares of common stock. The Company records the related fees derived from the agreement as management fees within the Statements of Income and any outstanding unpaid balance with CPI, Ltd. is shown in the balance sheets as accounts payable others.

**n. *Utility Regulation*** - The Company is subject to regulation by the ASEP. This entity regulates and makes the final determination regarding the rates the Company charges to its customers. The Company maintains its accounts in accordance with the Uniform System of Accounts prescribed for electric utilities by the ASEP.

The Company is subject to the provisions of SFAS No.71, "Accounting for the Effects of Certain Types of Regulation". Regulatory assets represent probable future revenues associated with certain costs that are expected to be recovered from customers through the ratemaking process. Regulatory liabilities represent probable future reductions in revenues associated with amounts that are expected to be credited to customers through the ratemaking process.

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**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

Regulatory assets and liabilities reflected in the Company's balance sheets at December 31, 2008 and 2007 relate to the following:

	<u>2008</u>	<u>2007</u>	<u>Note</u>
Fuel component adjustment - asset	\$ 5,807,351	\$ 10,830,351	See Note 6 "Fuel component adjustment"
Deferred income tax - liabilities	<u>(1,742,205)</u>	<u>(3,249,105)</u>	
	<u>\$ 4,065,146</u>	<u>\$ 7,581,246</u>	

In the event that a portion of the Company's operations is no longer subject to the provisions of SFAS No.71, the Company would be required to write off related regulatory assets and liabilities that are not specifically recoverable through regulated rates. In addition, the Company would be required to determine if any impairment to other assets, including plant, exists and, if impaired, write down the assets to their fair value.

***o. Revenue Recognition***

Energy Sales

The Company recognizes its revenues for energy sales when service is delivered to and consumed by customers. The Company bills customers based on meter readings that are performed on a systematic basis throughout the month. The applicable rates used to bill the customers include energy cost and distribution components. The energy cost component operates as a pass-through for the energy purchased and transmission charges while the distribution components in the tariff are set by the ASEP to allow distributors to recover the cost of operating, maintenance, administration and commercial expenses, depreciation, standard energy losses and also to obtain a fair return on their investment. The energy cost component is adjusted every six months to reflect fluctuations in energy costs and the distribution components are adjusted based on the consumer price index.

The Company recognizes revenue for energy sales that have not yet been billed, but where electricity has been consumed by customers. This revenue is recorded as unbilled revenue within the trade receivables on the balance sheet and is

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**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
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calculated based on actual daily average energy consumption and applicable rates to the customers of the Company.

Other Revenues

The Company recognizes connection and reconnection charges, pole rentals, and wheeling charges as service is rendered. These charges are included in other operating revenue in the Income Statements.

- p. Use of Estimates** - The preparation of the financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. These estimates include but are not limited to the useful lives for depreciation and amortization, allowances for doubtful accounts receivable, estimates of future cash flows associated with asset impairments, loss contingencies, collection or reimbursement of the fuel component adjustment account and estimated unbilled revenue. The estimates and assumptions used are based upon management's evaluation of the relevant facts and circumstances as of the date of the financial statements. Actual results could differ from those estimates.
- q. Concentration of Credit Risk** - The Company has exclusivity for the distribution and marketing of electric power to customers located in its concession zone. The Company does not believe that significant risk of loss from a concentration of credit risk exists given the large number of customers that comprise its customer base and their geographical dispersion. The Company also believes that its potential credit risk is adequately covered by the allowance for doubtful account.
- r. Environmental Matters** - The Company is subject to a broad range of environmental, health and safety laws and regulations. In July 1998, the Panamanian Government enacted environmental legislation creating an environmental protection agency (Autoridad Nacional del Medio Ambiente ("ANAM" in Spanish) and imposing new environmental standards affecting the Company's operations. Failure to comply with these applicable environmental standards, stricter laws and regulations may require additional investments or may adversely affect the Company's financial results.  
Accruals for environmental matters are recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on current law.



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**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

Established accruals are adjusted periodically due to new assessments and remediation efforts or as additional technical and legal information become available.

Environmental costs are capitalized if the costs extend the life of the property, increase its capacity and mitigate or prevent contamination from future operations. Costs related to environmental contamination treatment and clean-up are charged to expense.

**s. *Recent Accounting Pronouncements***

The Company adopted, or will adopt, the recent accounting standards listed below, if applicable, on their respective effective dates.

In September 2006, the FASB issued SFAS No.157, "Fair Value Measurements". SFAS No.157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Under SFAS No.157, fair value refers to the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts. The standard clarifies that fair value should be based on the assumptions market participants would use when pricing the asset or liability. SFAS No.157 is effective for annual periods beginning after November 15, 2007. The adoption of this interpretation did not have any impact in the Company's financial statements.

In February 2007, the FASB issued SFAS No. 159, "Fair Value Option for Financial Assets and Financial Liabilities". This statement permits, but does not require, companies to account for financial instruments at fair value that are not otherwise required to be measured at fair value. The statement is effective for fiscal years beginning after November 15, 2007. The adoption of this interpretation did not have any impact in the Company's financial statements.

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**Notes to financial statements**  
For the twelve months ended December 31, 2008 and 2007  
(Expressed in United States dollars)

**3. Accounts Receivable – Trade**

At December 31, 2008 and 2007, accounts receivable – trade, are as follows:

	<b>2008</b>	<b>2007</b>
Customers	\$ 58,437,236	\$ 44,364,605
Government and municipal entities	<u>6,518,741</u>	<u>5,344,040</u>
	64,955,977	49,708,645
Unbilled revenue	7,150,167	6,429,577
Government subsidy	<u>2,300,158</u>	<u>                    </u>
	74,406,302	56,138,222
Allowance for doubtful accounts	<u>(8,738,343)</u>	<u>(7,145,690)</u>
Total	<u>\$ 65,667,959</u>	<u>\$ 48,992,532</u>

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**Notes to financial statements**  
For the twelve months ended December 31, 2008 and 2007  
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**4. Income Tax**

The provision for income tax is determined based on income before income taxes, adjusted for any non-taxable income and non-deductible expenses. The statutory income tax rate is 30%. Deferred income tax is recognized for the effects of all temporary differences between the financial and tax basis of assets and liabilities. A valuation reserve is recorded to reduce the value of deferred tax assets when it is more likely than not that tax benefits will not be totally realized.

Deferred income tax assets and liabilities recognized on temporary differences that will be reversed in future periods, are as follows:

	<b>2008</b>	<b>2007</b>
Current deferred income tax assets:		
Provision for doubtful accounts	\$ 732,067	\$ 704,730
Investment tax credit		775,343
Other	<u>228,244</u>	<u>171,776</u>
Total deferred income tax assets	<u>960,311</u>	<u>1,651,849</u>
Current liability-fuel component adjustment	<u>(1,742,205)</u>	<u>(3,249,105)</u>
Current deferred income tax liability, net	<u>\$ (781,894)</u>	<u>\$ (1,597,256)</u>
	<b>2008</b>	<b>2007</b>
Non-current deferred income tax assets:		
Provision for contingencies	<u>108,500</u>	<u>217,566</u>
Non-current liability-depreciation expense	<u>(2,929,914)</u>	<u>(3,066,652)</u>
Non-current deferred income tax liability, net	<u>\$ (2,821,414)</u>	<u>\$ (2,849,086)</u>

**Elektra Noreste, S.A.**  
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**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
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Under FIN No. 48, the Company is required to recognize the financial statement effects of tax positions if they meet a “more-likely-than-not” threshold. In evaluating items relative to this threshold, the Company must assess whether each tax position will be sustained based solely on its technical merits assuming examination by a taxing authority. The interpretation requires the Company to establish liabilities to reflect the portion of those positions that cannot be concluded as “more likely than not” of being realized upon ultimate settlement. These are referred to as liabilities for unrecognized tax benefit under FIN No. 48. Upon adoption of this interpretation, the Company identified and evaluated any potential uncertain tax positions and concluded that there are no uncertain tax positions requiring recognition in the financial statements. Management expects the tax authorities to allow these positions when and if examined and has a high confidence level in the technical merits of these positions. Accordingly, Management expects the full amount of the tax position to be ultimately realized in the financial statements.

Years starting with 2006 are subject to examination by tax authorities, although no examination is currently scheduled or in process. Years prior to 2006 are considered closed years.

**Investment Tax Credit**

During 2001, the Company received an investment tax credit of US\$13,673,745 which was granted by the Panamanian Government under an incentive law that promoted investments in infrastructure to enhance the energy distribution network. The tax credit can be used as a reduction of up to 25% of the income tax incurred in any given year, until 100% of the amount pending to be realized in future years is consumed.

Due to the benefit received, the Company is not allowed to deduct for tax purposes, the depreciation on the US\$13,673,745 of infrastructure invested. The tax effect of this is US\$4,102,123 (US\$13,673,745 x 30%).

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

**5. Debt**

At December 31, 2008 and 2007, bank debts and notes are as follows:

**Short-term debt**

At December 31, 2008 and 2007, borrowings under revolving credit facilities are as follows:

	2008	2007
<b>Promissory notes</b>		
The Bank of Nova Scotia	\$ 15,000,000	\$ -
HSBC Bank (Panama), S.A.	<u>10,000,000</u>	<u>-</u>
Total short-term debt	<u>\$ 25,000,000</u>	<u>\$ -</u>

The Company has available revolving credit lines with The Bank of Nova Scotia, Banco General, S. A. and HSBC Bank (Panama), S.A., with an aggregated credit line of US\$50,000,000 in 2008, and annual interest rates ranging between 1 to 6 months LIBOR plus 1.50% and 2.50%. The Company had revolving credit lines with The Bank of Nova Scotia, Banco Bilbao Vizcaya Argentina (Panamá), S.A., Banco General, S.A., and Citibank, N.A. with an aggregated credit line of US\$60,500,000 in 2007, with annual interest rates ranging between 1 to 6 months LIBOR plus 1.20% and 1.50%. These unsecured credit facilities are available with a maximum term of up to one year. The Company uses these facilities as needed for working capital and other needs.

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

**Long-term Notes**

At December 31, 2008 and 2007, the balance of the long-term notes is as follows:

	2008	2007
<b>Long-Term Notes</b>		
Senior Notes	\$ 100,000,000	\$ 100,000,000
Corporate Bonds	20,000,000	-
Less:		
Senior notes discount	<u>(778,692)</u>	<u>(814,759)</u>
Total Long-term debt	<u>\$ 119,221,308</u>	<u>\$ 99,185,241</u>

The Company has notes payable under a senior debt agreement ("Senior Notes") totaling US\$100,000,000 which is recorded at US\$99,221,308, net of US\$778,692 unamortized discount at December 31, 2008. The notes have a fixed interest rate of 7.6%, payable semiannually, and mature in 2021. Principal payment is due upon maturity. The notes maintain a senior credit position and are unsecured. The Company may redeem the Senior Notes, in whole or in part, at any time prior to their maturity.

On October 20, 2008, in a public offering, the Company submitted a US\$40,000,000 aggregate principal amount of unsecured and unsubordinated corporate bonds ("Bonds") due October 20, 2018. On such date, US\$20,000,000 of this corporate bond offering was subscribed and issued with Banco General. The bonds rank pari passu among equal in right of payment with all other unsecured and unsubordinated obligations. The bonds will bear interest at LIBOR plus 2.375% per annum, payable on a quarterly basis. Principal is due upon maturity. The proceeds from the offering of the bonds will be used to fund current and future capital expenditures and for general corporate purposes. The bonds are subject to additional terms and conditions which are customary for this transaction. Bonds covenants include debt coverage ratios and other provisions. The Company may redeem the Bonds, in whole or in part, at the third anniversary from the date of the offer.

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

**6. Purchase of Energy and Transmission Charges, Net**

The Company recorded purchase of energy and transmission charges as follows:

	<b>2008</b>	<b>2007</b>
Purchase of energy	\$ 418,059,103	\$ 284,253,158
Transmission charges	10,630,515	10,504,420
Fuel component adjustment	<u>5,023,000</u>	<u>(14,331,000)</u>
 Total net purchase of energy and transmission charges	 <u>\$ 433,712,618</u>	 <u>\$ 280,426,578</u>

***Fuel Component Adjustment***

Changes in the under/over collection of these energy costs are reflected under net energy purchased and transmission costs in the Statements of Income. The cumulative amount receivable/payable is presented as a fuel component adjustment receivable/payable on the balance sheets until these amounts are billed or reimbursed to customers. The fuel component adjustment includes six months with actual fuel price information, plus six months of estimated fuel price information.

For the last several years, the fuel component adjustment has not been fully passed through to distribution company customers in the form of a tariff increase; the amount not billed to customers has been subsidized by the Panamanian Government.

At December 31, 2008, a net receivable balance of US\$5,807,351 was determined as a consequence of the variance resulting from the energy cost considered in the electric tariff for 2008 over the actual cost of energy purchased. The balance is comprised of receivables of US\$16,559,000, accumulated from January to June 2008 to be recovered from customers in the first semester of 2009, and a payable of US\$10,751,649 consequence of the variance resulting from July to December 2008, to be return to customers in the first semester of 2009.

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

## **7. Commitments and Contingencies**

The Company maintains commitments and obligations as result of issues generated from the ordinary course of business, is not expected to have a material impact on the Company's financial position, result of operations or liquidity. At December 31, 2008 and 2007, the Company had total reserves for loss contingencies in the amount of US\$361,666 and US\$725,218 respectively; these reserves are reported in the Balance Sheets in "Reserve for contingencies". Following are the most representative matters:

### ***Litigations***

The ASEP through Resolution JD-5956 dated April 11, 2006 ordered the Company to return US\$4,033,188 to the customers as a monthly credit on their bills starting May 2006 until December 2006 on grounds of a supposedly excess in the authorized Maximum Allowed Income, charged by the Company to its customers from July 2002 through June 2006.

According to the ASEP, this alleged excess was generated from the difference between the breakdown by tariff type of the forecast used to determine the tariff structure and the actual breakdown. The Company appealed this decision due to a lack of legal grounds and in addition presented a revision of the study developed by the ASEP in which the difference in the "Maximum Allowed Income" caused by tariff type of the forecast used to determine the tariff structure and the actual breakdown proved to be in favor of the Company. The ASEP decided as of June 14, 2006 to suspend any further action on Resolution JD-5956 until the Supreme Court pronounce on a related counterclaim that alleged for illegality against Resolution JD-5845, filed by the other distribution company. On December 22, 2008, the regulatory entity issued Resolution No.2269, revoking in all its parts Resolution JD-5956 of April 11, 2006. The decision by the regulatory entity was originated by the fact that the Company was able to fully prove that its approach related to the calculation of tariffs and variances presented by the Company in the legal appeal were correct.

The ASEP through Resolution JD-5863, dated February 17, 2006 approved Title IV of the Distribution and Commercialization Regimen enacted from July 2006 through June 2010, which contains a provision on its article number 22, requiring that excess earnings considered above a reasonable margin of the company's Maximum Allowed Income at the end of the July 2006- June 2010 tariff period will cause an adjustment by reducing the approved Maximum Allowed Income to be applied in the July 2010 – June 2014 period. However and even though the procedure to calculate and adjust an unreasonable excess has yet to be defined by the regulatory body, the Company's management position is that as of December 31, 2008 there is no contingency loss to



**Elektra Noreste, S.A.****(a 51% owned subsidiary of Panama Distribution Group, S.A.)****Notes to financial statements****For the twelve months ended December 31, 2008 and 2007****(Expressed in United States dollars)**

be recorded in the Financial Statements as a consequence of this particular provision under the above mentioned resolution. This conclusion is based on: i) a final outcome still in progress at the Supreme Court related to the appeal of this article filed in the Supreme Court by the other power distribution company; ii) in case the regulatory entity approves a resolution to adjust any unreasonable excess, the company has the right to file an appeal in the Supreme Court which is the independent body and final instance that will decide on this particular matter; and iii) there is no written nor approved procedure to calculate and adjust what could be deemed by the regulatory body as an unreasonable excess, ergo, any calculation will be highly subjective.

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

***Commitments***

As of December 31, 2008, the Company had energy and long-term firm capacity purchase contracts with the following generation companies:

<u>Company</u>	<u>MW (Monthly)</u>	<u>Begins</u>	<u>Ends</u>
Térmica del Noreste, S.A.	as requested capacity	June 19, 2000	July 19, 2010
ESTI – AES	48.72	November 20, 2003	November 20, 2013
La Mina Hidro - Power	28	January 1, 2008	December 31, 2015
Bontex	19.8	January 1, 2008	December 31, 2015
Paso Ancho Hidro-Power	4	January 1, 2008	December 31, 2015
Empresa de Generacion Fortuna	80	January 1, 2009	December 31, 2012
Empresa de Generacion Fortuna	120	January 1, 2013	December 31, 2018
Pedregal Power Co.	10; 1; 1	January 1, 2007	December 31, 2009
Semper Group.	30	January 1, 2009	December 31, 2010
Pan Am	16; 16; 45; 45	January 1, 2007	December 31, 2010
Empresa de generacion Fortuna	25; 5; 15	January 1, 2007	December 31, 2009
Pegregal Power Co.	42	January 1, 2009	December 31, 2009
Pan Am	32	January 1, 2009	December 31, 2009
Semper Group	0.0075	January 1, 2009	December 31, 2010
Semper Group	23	January 1, 2011	December 31, 2012
Bahía Las Minas	0.001	January 1, 2009	December 31, 2009
Bahía Las Minas	108	January 1, 2010	December 31, 2018
Bahía Las Minas	108	January 1, 2019	December 31, 2023
Pan Am	20	January 1, 2010	December 31, 2019
Pan Am	60	January 1, 2011	December 31, 2020
Térmica del Caribe	2.85	March 1, 2009	March 31, 2014
Inversiones y Desarrollo Balboa	24.6	January 1, 2009	December 31, 2011
Energía y Servicios de Panamá	0.96	July 1, 2009	June 30, 2014
Generadora del Atlántico	30	July 1, 2009	June 30, 2014
Empresa de Generacion Fortuna	59	January 1, 2009	December 31, 2009
Pedregal Power Co.	4	January 1, 2009	December 31, 2009
Empresa de Generacion Fortuna	55.5	January 1, 2010	December 31, 2011
Bahía Las Minas	10.13	January 1, 2009	December 31, 2009
Pegregal Power Co.	15	January 1, 2010	December 31, 2011
Autoridad del Canal de Panama	30; 22	January 1, 2010	December 31, 2011
AES Panamá	39	January 1, 2012	December 31, 2012
AES Panamá	23	January 1, 2013	December 31, 2021
Empresa de Generacion Fortuna	8.05	January 1, 2013	December 31, 2022
AES Panamá	9.43	January 1, 2013	December 31, 2022
Hidro Caisan	5.09	January 1, 2013	December 31, 2022
Electron Investment	10.35	January 1, 2013	December 31, 2022
Alternegy	18.4	January 1, 2013	December 31, 2022
Bontex	4.6	January 1, 2013	December 31, 2022

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

In accordance with the 1997 Electricity Law, the Company enters into long-term power purchase agreements with electricity generators that cover most of its regulated customers' contributions to the total peak customer demand of electricity and work towards limiting any associated energy costs. Historically, the Company contracts annually for approximately 79% to 95% of its total energy requirements via purchase agreements on the contract market. At December 31, 2008 and 2007, the Company purchased approximately 81% and 93%, respectively, of its total energy requirements via power purchase agreements on the contract market. These purchase agreements include both a fixed charge based on energy capacity requirements and a variable charge based on energy use.

The company maintains several unconditional long term contracts related to the purchase of energy capacity the aggregate amount of future payments required under such unconditional long term contracts, is as follows:

<b>Year</b>	<b>Payment Obligation</b>
2009	\$ 59,673,866
2010	88,752,248
2011	88,556,668
2012	73,085,868
2013	83,005,313
Thereafter	<u>638,872,007</u>
<b>Total</b>	<b><u>\$ 1,031,945,970</u></b>

As of December 31, 2008 and 2007, the Company has expensed the amount of US\$38,455,131 and US\$36,087,982 respectively, on such unconditional long-term contracts, recorded under Purchase of energy and transmission charges, net on the Statement of Income.

On October 20, 2003, the Company and the workers' union signed its second Labor Collective Agreement for a four-year term that expired on October 20, 2007. On January 30, 2008 negotiations with the worker's union were concluded and a new Labor Collective Agreement was signed. These agreements do not maintain or

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

considered additional material commitments besides those established in the labor law. The new Labor Collective Agreement is effective as from February 2008 and is valid for the term of four years.

***Operating Leases***

The Company has entered into a seven year non-cancelable lease agreement which will provide for the use of office and operating facilities. As of December 31, 2008 the future minimum rental payments required under this operating lease with initial or remaining non-cancelable lease terms in excess of one year are:

<b>Year</b>	<b>Amount</b>
2009	\$ 460,133
2010	473,936
2011	488,155
2012	502,799
2013	517,883
Thereafter	<u>174,320</u>
Total minimum payments required	<u>\$ 2,617,226</u>

As of December 31, 2008 and 2007 the total rental expense for all operating leases is US\$1,577,674 and US\$1,555,885 respectively.

***Guarantees***

The Company has provided limited guarantees to generating companies in order to provide for credit assurance and performance obligations under the power purchase agreements. These guarantees are not recognized on the balance sheets, because the Company believes that it is able to perform under these contracts and that is not probable that payments will be required. The guaranteed amounts are limited to a month's estimate of energy capacity and associated energy consumption and are established for a twelve-months period with automatic renewals as long as the power purchase agreement is in place. The aggregate guarantee amount for the performance obligation is US\$19,069,258. The Company has also issued a guarantee in favor of the ASEP for US\$8,000,000 in compliance with clause 53 of the Concession Contract.

The Company has several standby letters of credit for US\$8,992,935 in favor of ETESA to guarantee the payment of transmission costs and energy purchases in the energy exchange market. The Company also has a standby letter of credit for US\$797,471 in

**Elektra Noreste, S.A.**  
**(a 51% owned subsidiary of Panama Distribution Group, S.A.)**

**Notes to financial statements**  
**For the twelve months ended December 31, 2008 and 2007**  
**(Expressed in United States dollars)**

favor of Telvent Energía y Medio Ambiente, S.A. to guarantee the payment of a software development.

***Concession Contract***

The Company has exclusive rights to install, own and operate an energy distribution network, and to supply energy to end customers other than large customers, currently defined as those with peak demand on a site-by-site basis of over 100kW. Large customers can choose to buy energy directly from generators or from the energy exchange market.

The Company's concession contract has a 15-year term and expires in October 2013. One year prior to the expiration of the concession period, the ASEP will hold a competitive tender offer for the sale of the 51% ownership share currently held by Panama Distribution Group, S.A., and who owns the right to set the asking price for the tender (by making its own bid) and will only be required to sell its share of the Company if a higher offer is made, in which case, Panama Distribution Group, S.A. will be entitled to retain the sale proceeds. If no higher offer is made, Panama Distribution Group, S.A. will retain its ownership for another 15-year term, subject to the same renewal procedure thereafter with no requirement to make any payment to the Panamanian Government.

The concession contract establishes provisions related to the Concessionaire's obligation in service supply issues, the non separation of the majority shares package, the delivery of periodic, technical and financial information to the ASEP, compliance with the technical quality standards (quality standards, measurement standards and operation regulations of the CND), and payment of the control, supervision and monitoring tariff of the ASEP, which may not be transferred to the users through the tariff.

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