

20-F/A 1 y71170e20vfza.htm AMENDMENT NO. 1 TO FORM 20-F

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

Form 20-F/A

**AMENDMENT NO. 1 TO ANNUAL REPORT
PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2007
Commission File Number 0-99

PETRÓLEOS MEXICANOS

(Exact name of registrant as specified in its charter)

Mexican Petroleum

(Translation of registrant's name into English)

United Mexican States

(Jurisdiction of incorporation or organization)

Avenida Marina Nacional No. 329

**Colonia Huasteca
México, D.F. 11311
México**

(Address of principal executive offices)

Celina Torres Uribe
(5255) 1944 9700
ri@dcf.pemex.com

Avenida Marina Nacional No. 329
Torre Ejecutiva Piso 38 Colonia Huasteca
11311 México, D.F., México
(Name, telephone, e-mail and/or facsimile number
and address of company contact person)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

None

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

Title of Each Class

9.50% Global Guaranteed Bonds due 2027

9¹/₄% Global Guaranteed Bonds due 2018

9³/₈% Notes due December 2, 2008

9.125% Notes due 2010

8.00% Notes due 2011

7.875% Notes due 2009

8.625% Bonds due 2022

7.375% Notes due 2014

6.125% Notes due 2008

9³/₈% Guaranteed Notes due 2008

5.75% Notes due 2015

9¹/₄% Guaranteed Bonds due 2018

8.625% Guaranteed Bonds due 2023

9.50% Guaranteed Bonds due 2027

6.625% Bonds due 2035

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act, (Check one):

Large accelerated filer **Accelerated filer** **Non-accelerated filer**

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP IFRS Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

TABLE OF CONTENTS

Explanatory Note	1
Item 18. Financial Statements	2

EXPLANATORY NOTE

We filed our annual report on Form 20-F for the fiscal year ended December 31, 2007 (which we refer to as the Form 20-F) on June 30, 2008. This Amendment No. 1 to our Form 20-F (which we refer to as Amendment No. 1) is being filed solely for purposes of (1) making certain revisions to the presentation of certain supplemental condensed information on a U.S. GAAP basis in the Consolidated Statements of Cash Flows included in Note 21III(1) to the condensed consolidated financial statements for the years ended December 31, 2007, 2006 and 2005, and in the supplemental condensed consolidating financial information in the Statement of Cash Flows included in Note 22 for the years ended December 31, 2007 and 2006, and (2) making certain revisions to the explanation of certain reconciling items, including the presentation of pension and seniority premiums and other post-retirement benefits included in Note 21, Note 21Ib. and Note 21Ic. to the condensed consolidated financial statements for the year ended December 31, 2007.

Except as described above, no other change has been made to the Form 20-F. The filing of this Amendment No. 1 does not, and does not purport to, amend, update or restate the information in any other item of the Form 20-F or reflect any events that have occurred after the filing of the Form 20-F. In addition, the filing of this Amendment No. 1 should not be understood to mean that any statements contained herein are true or complete as of any date subsequent to June 30, 2008.

Item 18. Financial Statements.

See pages F-1 through F-100, incorporated herein by reference.

SIGNATURE

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, as amended, the registrant hereby certifies that it meets all of the requirements for filing on Form 20-F/A and has duly caused and authorized the undersigned to sign this annual report on its behalf.

PETRÓLEOS MEXICANOS

By: /s/ Esteban Levin Balcells

Name: Esteban Levin Balcells

Title: Chief Financial Officer

Date: September 24, 2008

**PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES
AND SUBSIDIARY COMPANIES
CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007, 2006 AND 2005**

INDEX

<u>Contents</u>	<u>Page</u>
Report of KPMG Cárdenas Dosal, S.C., Registered Public Accounting Firm	F-2
Report of PricewaterhouseCoopers, Registered Public Accounting Firm	F-3
Consolidated financial statements	
Consolidated balance sheets	F-4
Consolidated statement of operations	F-5
Consolidated statements of changes in equity	F-6
Consolidated statements of changes in financial position	F-7
Notes to the consolidated financial statements	F-8 through F-100

F-1

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the General Comptroller's Office
And the Board of Directors of
Petróleos Mexicanos:

We have audited the accompanying consolidated balance sheet of Petróleos Mexicanos, Subsidiary Entities and Subsidiary Companies ("PEMEX") as of December 31, 2007 and the related consolidated statements of operations, changes in equity and changes in financial position for the year ended December 31, 2007. These consolidated financial statements are the responsibility of the management of PEMEX. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in Mexico and with the Standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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 audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of PEMEX as of December 31, 2007 and the consolidated results of their operations, the changes in their equity and the changes in their financial position for the year ended December 31, 2007 in conformity with Mexican Financial Reporting Standards.

Mexican Financial Reporting Standards vary in certain significant respects from U.S. generally accepted accounting principles. Information relating to the nature and effect of such differences is presented in note 21 to the consolidated financial statements.

As described in notes 21 and 22 to the consolidated financial statements, cash flow information and other comprehensive income have been restated.

KPMG Cárdenas Dosal, S. C.

/s/ Eduardo Palomino

Eduardo Palomino
Mexico City, Mexico
April 11, 2008, except as to notes 21 and 22
which are as of September 23, 2008.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Mexico City, Mexico, June 29, 2007

To the General Comptroller's Office
and the Board of Directors of
Petróleos Mexicanos:

We have audited the accompanying consolidated balance sheet of Petróleos Mexicanos, Subsidiary Entities and Subsidiary Companies (collectively, "PEMEX") as of December 31, 2006, and the related consolidated statements of operations, changes in equity and changes in financial position for each of the two years in the period ended December 31, 2006. These financial statements are the responsibility of the management of PEMEX. 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 Mexico and with the Standards of the Public Company Accounting Oversight Board (United States of America). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures contained in the consolidated financial statements. An audit also includes assessing the standards of financial information 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.

As described in Note 3l. to the consolidated financial statements, effective January 1, 2005, PEMEX adopted the amendments to Bulletin D-3, "Labor Obligations", issued by the Mexican Institute of Public Accountants ("MIPA"), which establishes the rules for valuation and recording of liabilities arising from other severance payments paid to employees upon dismissal. As of January 1, 2005, the adoption of these amendments resulted in a charge of Ps. 1,427,872,000, which is presented in the consolidated statement of operations as a cumulative effect of adoption of new accounting standards.

As described in Note 3m. to the consolidated financial statements, effective January 1, 2005, PEMEX adopted the provisions of Bulletin C-10, "Derivative Financial Instruments and Hedging Operations", issued by the MIPA, which establishes the criteria for valuation, recording and disclosure applicable to derivative financial instruments for hedging and to embedded derivatives. As of January 1, 2005, the adoption of these provisions resulted in the recognition of an initial cumulative charge of Ps. 477,996,000, recognized in the consolidated statement of operations as a cumulative effect of adoption of new accounting standards.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of PEMEX at December 31, 2006 and the consolidated results of their operations, changes in equity and changes in financial position for each of the two years in the period ended December 31, 2006, in conformity with Mexican Financial Reporting Standards.

Mexican Financial Reporting Standards vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of said differences is presented in Note 21 to the consolidated financial statements.

PricewaterhouseCoopers

/s/ Ariadna L. Muñiz Patiño

Ariadna L. Muñiz Patiño
Public Accountant

**PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES
AND SUBSIDIARY COMPANIES**

CONSOLIDATED BALANCE SHEETS

(In thousands of Mexican pesos as of December 31, 2007, purchasing power and in thousands of U.S. dollars)

	<u>2007</u>	<u>2007</u>	<u>2006</u>
	(Unaudited)		
ASSETS:			
Current assets:			
Cash and cash equivalents (Note 5)	U.S. \$ 15,736,617	Ps. 170,997,240	Ps. 195,776,457
Accounts, notes receivable and other — Net (Note 6)	13,943,286	151,510,543	137,163,105
Inventories — Net (Note 7)	8,571,822	93,143,136	62,063,798
Derivative financial instruments (Note 11)	1,188,075	12,909,868	4,389,836
	<u>23,703,183</u>	<u>257,563,547</u>	<u>203,616,739</u>
Total current assets	<u>39,439,800</u>	<u>428,560,787</u>	<u>399,393,196</u>
Investments in shares of non consolidated subsidiaries and affiliates (Note 8)	3,042,770	33,063,354	32,760,946
Properties, plant and equipment — Net (Note 9)	73,056,399	793,845,453	737,195,457
Intangible asset derived from the actuarial computation of labor obligations (Note 12)	6,626,864	72,008,835	76,495,133
Other assets — Net	257,880	2,802,177	4,175,692
Total assets	<u>U.S. \$ 122,423,713</u>	<u>Ps.1,330,280,606</u>	<u>Ps.1,250,020,424</u>
LIABILITIES:			
Current liabilities:			
Current portion of long-term debt (Note 10)	U.S. \$ 6,998,778	Ps. 76,050,128	Ps. 66,240,278
Suppliers	3,233,728	35,138,344	37,102,983
Accounts and accrued expenses payable	1,665,488	18,097,530	14,592,081
Taxes payable	13,490,765	146,593,355	45,006,644
Derivative financial instruments (Note 11)	1,250,160	13,584,495	13,372,143
Total current liabilities	<u>26,638,919</u>	<u>289,463,852</u>	<u>176,314,129</u>
Long-term liabilities:			
Long-term debt (Note 10)	39,096,323	424,828,472	524,475,242
Reserve for sundry creditors and others	2,895,883	31,467,252	31,513,072
Reserve for labor obligations (Note 12)	48,609,566	528,201,272	471,665,183
Deferred taxes (Note 18i.)	590,077	6,411,897	4,597,172
Total liabilities	<u>117,830,768</u>	<u>1,280,372,745</u>	<u>1,208,564,798</u>
EQUITY (Note 14):			
Certificates of Contribution "A"	8,922,897	96,957,993	96,957,993
Mexican Government increase in equity of Subsidiary Entities	13,294,217	144,457,629	133,296,805
Surplus in the restatement of equity	16,430,011	178,531,795	159,893,393
Effect on equity from labor obligations (Note 12)	(4,763,352)	(51,759,539)	(48,326,747)
Derivative financial instruments (Note 11)	(101,749)	(1,105,629)	(1,762,328)
	<u>33,782,024</u>	<u>367,082,249</u>	<u>340,059,116</u>
Accumulated losses:			
From prior years	(27,504,262)	(298,866,819)	(345,556,695)
Net income (loss) for the year	(1,684,817)	(18,307,569)	46,953,205
	<u>(29,189,079)</u>	<u>(317,174,388)</u>	<u>(298,603,490)</u>
Total equity	<u>4,592,945</u>	<u>49,907,861</u>	<u>41,455,626</u>
Commitments and contingencies (Notes 15 and 16)	—	—	—
Total liabilities and equity	<u>U.S. \$ 122,423,713</u>	<u>Ps.1,330,280,606</u>	<u>Ps.1,250,020,424</u>

The accompanying notes are an integral part of these consolidated financial statements.

**PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES
AND SUBSIDIARY COMPANIES**

CONSOLIDATED STATEMENT OF OPERATIONS

(In thousands of Mexican pesos as of December 31, 2007, purchasing power and in thousands of U.S. dollars)

	2007 (Unaudited)	2007	2006	2005
Net sales:				
Domestic	U.S. \$ 54,485,281	Ps. 592,047,961	Ps. 567,289,873	Ps. 545,339,433
Export	49,964,740	542,926,858	535,144,048	457,266,832
Services income	97,606	1,060,609	1,075,947	1,224,808
Total revenues	<u>104,547,627</u>	<u>1,136,035,428</u>	1,103,509,868	1,003,831,073
Cost of sales	<u>42,394,374</u>	<u>460,665,742</u>	418,258,210	389,943,899
Gross income	<u>62,153,253</u>	<u>675,369,686</u>	685,251,658	613,887,174
General expenses:				
Transportation and distribution expenses	2,282,172	24,798,539	24,921,656	23,655,910
Administrative expenses	5,534,636	60,140,465	56,052,773	50,527,884
Total general expenses	<u>7,816,808</u>	<u>84,939,004</u>	80,974,429	74,183,794
Operating income	<u>54,336,446</u>	<u>590,430,682</u>	604,277,229	539,703,380
Other revenues (principally IEPS benefit) — Net (Note 18h.)	<u>7,640,114</u>	<u>83,019,010</u>	61,213,533	2,896,394
Comprehensive financing result:				
Interest — Net	(2,896,873)	(31,478,006)	(36,195,263)	(41,500,949)
Exchange (loss) gain — Net	(132,048)	(1,434,868)	(2,470,584)	19,031,585
Gain on monetary position	1,184,064	12,866,287	14,819,222	17,633,273
	<u>(1,844,857)</u>	<u>(20,046,587)</u>	(23,846,625)	(4,836,091)
Profit sharing in non-consolidated subsidiaries and affiliates (Note 8)	<u>510,303</u>	<u>5,545,054</u>	10,073,577	8,658,665
Income before taxes and duties	<u>60,642,006</u>	<u>658,948,159</u>	651,717,714	546,422,348
Hydrocarbon extraction duties and others (Note 18)	61,474,951	667,999,120	587,020,786	538,063,741
Excess gain duties (Note 18d.)	—	—	8,223,820	60,869,738
Hydrocarbon income tax (Note 18i.)	554,965	6,030,367	4,914,859	2,135,245
Income tax (Note 18k.)	296,906	3,226,241	4,605,044	3,981,678
Special tax on production and services (IEPS Tax) (Note 18h.)	—	—	—	21,824,060
	<u>62,326,822</u>	<u>677,255,728</u>	604,764,509	626,874,462
Cumulative effect of adoption of new accounting standards (Notes 3l. and 3m.)	—	—	—	(1,905,868)
Net (loss) income for the year	<u>(U.S.\$ 1,684,816)</u>	<u>(Ps. 18,307,569)</u>	Ps. 46,953,205	(Ps. 82,357,982)

The accompanying notes are an integral part of these consolidated financial statements.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS
ENDED DECEMBER 31, 2007, 2006 AND 2005
(In thousands of Mexican pesos as of December 31, 2007, purchasing power and in thousands of U.S. dollars)

	Certificates of Contribution "A"		Mexican Government increase in equity of Subsidiary Entities	Surplus in the restatement of equity	Derivative financial instruments	Effect on equity from labor obligations	Retained earnings (Accumulated losses)		Total
	From prior years	For the year							
Balances as of December 31, 2004	Ps. 96,957,993	Ps. 36,411,340	Ps. 147,644,457	Ps. —	(Ps. 7,782,166)	(Ps. 207,589,715)	(Ps. 28,443,617)	Ps. 37,198,292	
Transfer to prior years' accumulated losses	—	—	—	—	—	(28,443,617)	28,443,617	—	
Minimum guaranteed dividends paid to the Mexican Government approved by the Board of Directors on June 10, 2006 (Note 14)	—	—	—	—	—	(11,482,869)	—	(11,482,869)	
Increase in equity of the Subsidiary Entities made by the Mexican Government (Note 14)	—	48,157,553	—	—	—	—	—	48,157,553	
Comprehensive loss for the year (Note 13)	—	—	8,184,288	(7,036,437)	(21,672,659)	—	(82,357,982)	(102,882,790)	
Balances as of December 31, 2005	96,957,993	84,568,893	155,828,745	(7,036,437)	(29,454,825)	(247,516,201)	(82,357,982)	(29,009,814)	
Transfer to prior years' accumulated losses	—	—	—	—	—	(82,357,982)	82,357,982	—	
Minimum guaranteed dividends paid to the Mexican Government approved by the Board of Directors on May 18 th , 2005 (Note 14)	—	—	—	—	—	(16,392,606)	—	(16,392,606)	
Increase in equity of the Subsidiary Entities made by the Mexican Government	—	48,727,912	—	—	—	—	—	48,727,912	
Comprehensive income for the year (Note 13)	—	—	4,064,648	5,274,109	(18,871,922)	710,094	46,953,205	38,130,134	
Balances as of December 31, 2006	96,957,993	133,296,805	159,893,393	(1,762,328)	(48,326,747)	(345,556,695)	46,953,205	41,455,626	
Transfer to prior years' accumulated losses	—	—	—	—	—	46,953,205	(46,953,205)	—	
Minimum guaranteed dividends paid to the Mexican Government approved by the Board of Directors on August 29, 2007 (Note 14)	—	—	—	—	—	(263,329)	—	(263,329)	
Increase in equity of the Subsidiary Entities made by the Mexican Government (Note 14)	—	11,160,824	—	—	—	—	—	11,160,824	
Comprehensive loss for the year (Note 13)	—	—	18,638,402	656,699	(3,432,792)	—	(18,307,569)	(2,445,260)	
Balances as of December 31, 2007	Ps. 96,957,993	Ps. 144,457,629	Ps. 178,531,795	(Ps. 1,105,629)	(Ps. 51,759,539)	(Ps. 298,866,819)	(Ps. 18,307,569)	Ps. 49,907,861	
Unaudited	U.S.\$ 8,922,897	U.S.\$ 13,294,217	U.S.\$ 16,430,011	(U.S.\$ 101,749)	U.S.\$ 4,763,352	(U.S.\$ 27,504,262)	(U.S.\$ 1,684,817)	U.S.\$ 4,592,945	

The accompanying notes are an integral part of these consolidated financial statements.

**PETROLEOS MEXICANOS, SUBSIDIARY ENTITIES
AND SUBSIDIARY COMPANIES**

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

(In thousands of Mexican pesos as of December 31, 2007, purchasing power and in thousands of U.S. dollars)

	2007 (Unaudited)	2007	2006	2005
Operating activities:				
Net (loss) income for the year	(U.S.\$ 1,684,817)	(Ps. 18,307,569)	Ps. 46,953,205	(Ps. 82,357,982)
Charges to operations not requiring the use of funds:				
Depreciation and amortization	6,680,506	72,591,718	65,672,189	56,995,357
Reserve for labor obligations cost	7,850,662	85,306,866	74,493,349	63,787,616
Profit sharing in non-consolidated subsidiaries and affiliates	510,302	5,545,054	10,073,577	8,658,665
Deferred taxes	177,417	1,927,847	904,162	2,135,247
Impairment on fixed assets	—	—	703,247	1,432,691
	<u>13,534,070</u>	<u>147,063,916</u>	198,799,729	50,651,594
Funds generated (used) in operation activities:				
Accounts, notes receivable and other	(1,320,373)	(14,347,438)	(37,177,837)	9,930,406
Inventories	(1,155,331)	(12,554,059)	(2,678,038)	(6,527,714)
Intangible asset derived from the actuarial computation of labor obligations	—	—	23,316,114	(14,672,035)
Other assets	126,403	1,373,515	(576,898)	—
Suppliers	(180,803)	(1,964,639)	3,676,529	6,291,447
Accounts payable and accrued expenses	365,779	3,974,633	3,382,644	(14,317,686)
Taxes payable	9,348,872	101,586,711	(26,857,283)	24,181,434
Reserve for sundry creditors and others	(4,217)	(45,820)	3,744,807	(1,203,805)
Derivative financial instruments	(747,287)	(8,120,165)	(2,541,921)	16,798,338
Funds provided by operating activities	<u>19,967,113</u>	<u>216,966,654</u>	163,087,846	71,131,979
Financing activities:				
Minimum guaranteed dividends paid to the Mexican Government	(24,234)	(263,329)	(16,392,606)	(11,482,869)
(Decrease) Increase in Debt — Net	(8,267,556)	(89,836,920)	10,202,873	65,892,138
Increase in equity of Subsidiary Entities	1,027,114	11,160,824	48,727,912	48,157,553
Retirement, seniority premiums and other post-retirement benefits payments	(2,550,779)	(27,717,270)	(17,042,349)	—
Sale of future accounts receivable	—	—	—	(40,871,801)
Funds (used in) provided by financing activities	<u>(9,815,455)</u>	<u>(106,656,695)</u>	25,495,830	61,695,021
Investing activities:				
Investment in shares	(538,133)	(5,847,462)	(14,153,450)	(7,485,420)
Increase in fixed assets — Net	(11,893,920)	(129,241,714)	(109,103,789)	(89,577,399)
Funds used in investing activities	<u>(12,432,053)</u>	<u>(135,089,176)</u>	(123,257,239)	(97,062,819)
Net (decrease) increase in cash and cash equivalents	(2,280,395)	(24,779,217)	65,326,437	35,764,181
Cash and cash equivalents at beginning of the year	18,017,012	195,776,457	130,450,020	94,685,839
Cash and cash equivalents at end of the year	<u>U.S.\$ 15,736,617</u>	<u>Ps. 170,997,240</u>	Ps. 195,776,457	Ps. 130,450,020

The accompanying notes are an integral part of these consolidated financial statements.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

These financial statements have been translated from the Spanish language for the convenience of the reader.

NOTE 1 —APPROVAL:

On April 11, 2008, the attached consolidated financial statements and the notes thereto were authorized by the following officers: Public Accountant Víctor M. Cámara Peón, Deputy Director of Financial Information Systems and Public Accountant Enrique Díaz Escalante, Associate Managing Director of Accounting.

These consolidated financial statements and the notes thereto will be submitted for approval to the Board of Directors of Petróleos Mexicanos in a meeting scheduled for April 29, 2008, where it is expected that the Board will approve such statements pursuant to the terms Article 104 Fraction III, paragraph a, of the Mexican Securities Market Law, of Article 33 Fraction I, paragraph a section 3 and of Article 78 of the general provisions applicable to Mexican securities issuers and other participants of the securities market.

NOTE 2 — STRUCTURE AND BUSINESS OPERATIONS OF PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES:

Petróleos Mexicanos was created on June 7, 1938, and began operations on July 20, 1938. A decree of the Mexican Congress stated the foreign-owned oil companies in operation at that time in the United States of Mexico (Mexico) were thereby nationalized. Petróleos Mexicanos and its four Subsidiary Entities (as defined below) are decentralized public entities of the Federal Government of Mexico (the “Mexican Government”) and together comprise the Mexican state oil and gas company.

The operations of Petróleos Mexicanos and the Subsidiary Entities are regulated by the *Constitución Política de los Estados Unidos Mexicanos* (Political Constitution of the United Mexican States, or the “Mexican Constitution”), the *Ley Reglamentaria del Artículo 27 Constitucional en el Ramo del Petróleo* (Regulatory Law to Article 27 of the Political Constitution of the United Mexican States concerning Petroleum affairs, or the “Regulatory Law”), effective on November 30, 1958, as amended effective on May 12, 1995, November 14, 1996 and January 13, 2006, and the *Ley Orgánica de Petróleos Mexicanos y Organismos Subsidiarios* (the Organic Law of Petróleos Mexicanos and Subsidiary Entities, or the “Organic Law”), effective on July 17, 1992, as amended effective on January 1, 1994, January 16, 2002 and January 13, 2006. Under the Organic Law and related regulations, Petróleos Mexicanos is entrusted with the central planning activities and the strategic management of Mexico’s petroleum industry. For purposes of these financial statements, capitalized words carry the meanings attributed to them herein or the meanings as defined in the Mexican Constitution or the Organic Law.

The Organic Law establishes a structure that consists of decentralized legal entities of a technical, industrial and commercial nature, with their own corporate identity and equity and with the legal authority to own property and conduct business in their own names. The Subsidiary Entities are controlled by and have characteristics of subsidiaries of Petróleos Mexicanos. The Subsidiary Entities are:

- Pemex-Exploración y Producción (“Pemex-Exploration and Production”);
- Pemex-Refinación (“Pemex-Refining”);
- Pemex-Gas y Petroquímica Básica (“Pemex-Gas and Basic Petrochemicals”); and
- Pemex-Petroquímica (“Pemex-Petrochemicals”).

The strategic activities entrusted to Petróleos Mexicanos and the Subsidiary Entities by the Organic Law, other than those entrusted to Pemex-Petrochemicals, can be performed only by Petróleos Mexicanos and

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

the Subsidiary Entities and cannot be delegated or subcontracted. Pemex-Petrochemicals is an exception and may delegate and/or subcontract certain activities.

The principal objectives of the Subsidiary Entities are as follows:

- I. Pemex-Exploration and Production explores for and produces crude oil and natural gas; additionally, this entity transports, stores and markets such products;
- II. Pemex-Refining refines petroleum products and derivatives thereof that may be used as basic industrial raw materials; additionally, this entity stores, transports, distributes and markets such products and derivatives;
- III. Pemex-Gas and Basic Petrochemicals processes natural gas, natural gas liquids and derivatives thereof that may be used as basic industrial raw materials, and stores, transports, distributes and markets such products; additionally, this entity stores, transports, distributes and markets Basic Petrochemicals; and
- IV. Pemex-Petrochemicals engages in industrial petrochemical processing and stores, distributes and markets Secondary Petrochemicals.

At its formation, Petróleos Mexicanos assigned to the Subsidiary Entities all the assets and liabilities needed to carry out these activities; these assets and liabilities were incorporated into the Subsidiary Entities' initial capital contribution. Additionally, Petróleos Mexicanos assigned to the Subsidiary Entities all the personnel needed for their operations, and the Subsidiary Entities assumed all the related labor liabilities. There were no changes in the carrying value of assets and liabilities upon their contribution by Petróleos Mexicanos to the Subsidiary Entities.

The principal distinction between the Subsidiary Entities and the Subsidiary Companies (as defined below) is that the Subsidiary Entities are decentralized public entities created by Article 3 of the Organic Law, whereas the Subsidiary Companies are companies that have been formed in accordance with the general corporations law of each of the respective jurisdictions in which they are incorporated, and are managed as any other private corporations subject to the general corporations law in their respective jurisdictions.

As used herein, "Subsidiary Companies" are defined as (a) those companies which are not Subsidiary Entities but in which Petróleos Mexicanos has more than 50% ownership investment and effective control, (b) the Pemex Project Funding Master Trust (the "Master Trust"), a Delaware statutory trust, (c) Fideicomiso Irrevocable de Administración No. F/163 ("Fideicomiso F/163"), a Mexican statutory trust incorporated in 2003 in Mexico (both the Master Trust and Fideicomiso F/163 are controlled by Petróleos Mexicanos) (d) RepCon Lux, S.A., a Luxembourg finance vehicle whose debt is guaranteed by Petróleos Mexicanos ("RepCon Lux") and (e) Pemex Finance, Ltd.

"Non-consolidated subsidiary companies," as used herein, means (a) those non-material subsidiary companies which are not Subsidiary Entities or Subsidiary Companies, as defined above in this note and (b) those companies in which PEMEX has 50% or less does ownership investment and not have effective control.

Petróleos Mexicanos, the Subsidiary Entities and the Subsidiary Companies are referred to as "PEMEX."

On September 14, 2004, the authorities authorized the procedures to merge Pemex-Petrochemicals and its subsidiaries. At the extraordinary Board of Directors' meeting held on February 9, 2006, the merger was formalized with Pemex-Petrochemicals as the surviving company, which acquired the rights and

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

obligations of its merged subsidiaries on April 30, 2006, while the subsidiary companies became petrochemical complexes operating as part of the surviving entity. The foregoing had no effect on the preparation of these consolidated financial statements.

NOTE 3 —SIGNIFICANT ACCOUNTING POLICIES:

The preparation of the financial statements requires the use of estimates and assumptions made by PEMEX's management that affect the recorded amounts of assets and liabilities and the disclosures of contingent assets and liabilities as well as the recorded amounts of income and expenses during the year. The important items subject to such estimates and assumptions include the book value of properties, plant and equipment; the valuation of the allowance for doubtful accounts, inventories and work in progress and the valuation of financial instruments and of the assets and liabilities related to labor obligations. Actual results could differ from those estimates.

References in these financial statements and related notes to "pesos" or "Ps." refers to Mexican pesos and "dollars" or "U.S.\$" refers to dollars of the United States of America.

For accounting purposes the functional currency of PEMEX is the Mexican peso.

Below is a summary of the principal accounting policies followed by PEMEX in the preparation of these consolidated financial statements, including the concepts, methods and criteria pertaining to the effects of inflation on the financial information, are summarized below:

a. Effects of inflation on the financial information

PEMEX recognizes the effects of inflation in accordance with Bulletin B-10 of *Normas de Información Financiera* (Mexican Financial Reporting Standards or "Mexican FRS" or "NIF's"), "Effects of Inflation" ("Bulletin B-10"). All periods presented herein are presented in accordance with Bulletin B-10.

The amounts shown in the accompanying consolidated financial statements include the effects of inflation in the financial information and are expressed in thousands of constant Mexican pesos as of December 31, 2007, based on the Mexican National Consumer Price Index ("NCPI"). The indexes used for the recognition of inflation were as follows:

<u>December 31,</u>	<u>NCPI</u>	<u>Inflation for the Year</u>
2007	125.5640	3.76%
2006	121.0150	4.05%
2005	116.3010	3.33%

b. Consolidation

The consolidated financial statements include the accounts of Petróleos Mexicanos, the Subsidiary Entities and the Subsidiary Companies. All significant intercompany balances and transactions have been eliminated in the consolidation.

The consolidated Subsidiary Companies are as follows: P.M.I. Comercio Internacional, S.A. de C.V. ("PMI CIM"); P.M.I. Trading Ltd. ("PMI Trading"); P.M.I. Holdings North America, Inc. ("PMI HNA"); P.M.I. Holdings Petróleos España ("HPE"); P.M.I. Holdings B.V. ("PMI HBV"); P.M.I. Norteamérica, S.A. de C.V. ("PMI NASA"); Kot Insurance Company AG ("KOT"); Integrated Trade Systems, Inc. ("ITS"); P.M.I. Marine Ltd ("PMI Mar"); P.M.I. Services, B.V. ("PMI-SHO"); Pemex Internacional España, S.A. ("PMI-

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SES”); Pemex Services Europe Ltd. (“PMI-SUK”); P.M.I. Services North America, Inc. (“PMI-SUS”); Mex Gas International, Ltd. (“MGAS”); the Master Trust; Fideicomiso F/163; RepCon Lux and Pemex Finance, Ltd.

The financial statements of foreign Subsidiary Companies classified as integrated foreign operations, as defined by Mexican FRS, are translated into Mexican pesos on the following basis: a) monetary items, at the rate of exchange in effect at the end of the period; b) non-monetary items, at the historical exchange rate; c) income and expense items, at the average exchange rate for each month in the year; and d) the effect of changes in exchange rates is recorded in equity. The financial statements in pesos are restated at the close of the period in accordance with the provisions of Bulletin B-10.

The financial statements of other foreign Subsidiary Companies are translated using the exchange rate effective at year end for monetary assets and liabilities, the historical exchange rate for non-monetary items and the average exchange rate for the statements of operations items. The effects of changes in the applicable exchange rates are included directly in stockholders’ equity as “Surplus in restatement of equity.”

Investment in non-consolidated subsidiary companies and affiliates are accounted for in accordance with paragraph (h) of this note. Other non-material subsidiary companies and affiliates are valued at cost and, based upon their relative importance to the total assets and income of PEMEX, were not consolidated and are accounted for under the equity method.

c. Long-term productive infrastructure projects (PIDIREGAS)

The investment in long-term productive infrastructure projects (“PIDIREGAS”) and related liabilities are initially recorded in accordance with NG-09-B, applicable to *Entidades Paraestatales de la Administración Pública Federal* (“State-owned Entities of the Federal Public Administration”), which requires recording only those liabilities maturing in less than two years.

For the purposes of these consolidated financial statements and in accordance with Mexican FRS, all accounts related to PIDIREGAS were incorporated into the consolidated financial statements for the years ended December 31, 2007, 2006 and 2005. All effects of NG-09-B are therefore eliminated.

The main objective of the Master Trust and Fideicomiso F/163 is to administer financial resources related to PIDIREGAS that have been designated by PEMEX for that purpose.

d. Exploration and drilling costs and specific oil-field exploration and depletion reserve

PEMEX uses the successful efforts method of accounting for oil and gas exploration costs. Exploration costs are charged to income when incurred, except that exploratory drilling costs are included in fixed assets, pending determination of proven reserves. Exploration wells more than 12 months old are expensed unless (a) (i) they are in an area requiring major capital expenditure before production can begin, (ii) commercially productive quantities of reserves have been found, and (iii) they are subject to further exploration or appraisal activity in that either drilling of additional exploratory wells is under way or firmly planned for the near future, or (b) proved reserves are recorded within 12 months following the completion of exploratory drilling. Expenses pertaining to the drilling of development wells are capitalized, whether or not successful.

Management makes semi-annual assessments of the amounts included within fixed assets to determine whether capitalization is initially appropriate and can continue. Exploration wells capitalized beyond 12 months are subject to additional scrutiny as to whether the facts and circumstances have changed and therefore whether the conditions described in clauses (a) and (b) of the preceding paragraph no longer apply.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

e. Reserve for abandonment cost of wells

The reserve for abandonment cost of wells (plugging and dismantling), as of December 31, 2007 and 2006 was Ps.17,148,400 and Ps.16,027,307, respectively, and is included as operative reserve in long-term liabilities.

The carrying value of these assets is subject to an annual impairment assessment. (see Note 9).

f. Cash and cash equivalents

Cash and cash equivalents consist of checking accounts, foreign currency and other highly liquid instruments. As of the date of these consolidated financial statements, earned interest income and foreign exchange gains or losses are included in the results of operations, under comprehensive financing result.

g. Inventory and cost of sales

Inventories are valued as follows:

- I. Crude oil and its derivatives for export: at realizable value, determined on the basis of average export prices at year end.
- II. Crude oil, natural gas and their derivatives for domestic sale: at realizable value, in accordance with international market prices at year end.
- III. The refined products inventories: at their acquisition or production cost calculated in accordance with crude oil costs and auxiliary materials.
- IV. Gas and petrochemicals: at direct standard cost of such products without exceeding their market value.
- V. Materials spare parts fittings: at the last purchase price without exceeding their market value.
- VI. Materials in transit: at acquisition cost.

PEMEX records the necessary allowances for inventory impairment arising from obsolescence, slow moving inventory and other factors that may indicate that the realization value of inventory may be lower than the recorded value.

Cost of sales is determined by adding to inventories at the beginning of the year the operating cost of oil fields, refineries and plants (including internally-consumed products), the cost of refined and other products, and deducting the value of inventories at the end of the year. The resulting amount is adjusted for inflation based on factors derived from the NCPI. Cost of sales also includes the depreciation and amortization expense associated with assets used in operations as well as the expense associated with the reserve for abandonment cost of wells.

h. Investment in shares of non-consolidated subsidiary companies affiliates companies

Certain non-material non-consolidated subsidiary companies are accounted for under the equity method (see Note 2).

Investments in shares in which PEMEX holds 50% or less of the issuer's capital stock are recorded at cost and adjusted for inflation using factors derived from the NCPI.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

i. Properties, plant and equipment

Properties, plant and equipment are initially recorded at acquisition cost and adjusted using factors derived from the NCPI. The restated amounts must not exceed the asset market value or replacement cost (see Note 9).

Beginning January 1, 2007, assets acquired during the construction or installation phase of a project include the comprehensive financing result associated with assets as part of the value of assets. Until 2006, interest and foreign exchange losses or gains associated with these assets were also included. (see paragraph (y) of this Note).

Depreciation is calculated using the straight-line method of accounting based on the expected useful lives of the assets, based on calculations from independent appraisals. The depreciation rates used by PEMEX are as follows:

	<u>%</u>	<u>Years</u>
Buildings	3	33
Plants and drilling equipment	3-5	20-33
Furniture and fixtures	10-25	4-10
Offshore platforms	4	25
Transportation equipment	4-20	5-25
Pipelines	4	25
Software/computers	10-25	4-10

Related gains or losses from the sale or disposal of fixed assets are recognized in income for the period in which they are incurred. PEMEX amortizes its well assets using the units-of-production ("UOP") method. The amount to be recognized as amortization expense is calculated based upon the number of equivalent barrels of crude oil extracted from each specific field as compared to the field's total proved developed reserves.

The *Reglamento de Trabajos Petroleros* ("Petroleum Works Law") provides that once a well turns out to be dry, is invaded with salt water, is abandoned due to mechanical failure or when the well's production has been depleted such that abandonment is necessary due to economic unfeasibility of production, it must be plugged to ensure the maintenance of sanitary and safe conditions and to prevent the seepage of hydrocarbons to the surface. All activities required for plugging a well are undertaken for the purpose of properly and definitively isolating the cross formations in the perforation that contains oil, gas or water, in order to ensure that hydrocarbons do not seep to the surface. This law also requires that PEMEX obtain approval from the Ministry of Energy for the dismantlement of hydrocarbon installations, either for the purpose of replacing them with new installations or for permanent retirement.

The costs related to wells subject to abandonment and dismantlement are recorded at their present values as liabilities on a discounted basis when incurred, which is typically at the time the wells first start drilling. The amounts recorded for these obligations are initially recorded by capitalizing the respective costs. Over time the liabilities will be accreted by the change in their present value during each period and the initial capitalized costs will be depreciated over the useful lives of the related assets based on the UOP method. In the case of non-producing wells subject to abandonment and dismantlement, the full dismantlement and abandonment cost is recognized at the end of each period.

The carrying value of these long-lived assets is subject to an annual impairment assessment (see Notes 3j. and 9).

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

j. Impairment of the value of long-lived assets

PEMEX evaluates periodically the values of long-lived assets to determine whether there is any indication of potential impairment. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net revenues expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated net revenues, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. During 2007, no impairment charge was recognized by PEMEX. At December 31, 2006 and 2005, PEMEX recorded an impairment charge related to long-lived assets of Ps. 703,247 and Ps. 1,432,691, respectively. (see Note 9d.).

k. Accruals

PEMEX recognizes, based on management estimates, accruals for those present obligations for which the transfer of assets or the rendering of services is probable and arises as a consequence of past events, primarily the payment of salaries and other employee payments as well as environmental liabilities, in certain cases, such amounts are recorded at their present value.

l. Labor obligations

The accumulated benefits related to pensions, seniority premiums, other post-retirement benefits, and employment termination for causes other than restructuring, to which all employees are entitled are recorded in the income statement for the year in which employees rendered services in accordance with actuarial valuations, using the projected unit-credit method (see Note 12). The amortization of the prior service cost of such services, which has not been recognized, is based on the employees' remaining average years of services. As of December 31, 2007, the remaining average years of services of PEMEX's employees participating in the plan was approximately 11 years.

The plan for other post-retirement benefits includes cash to retired personnel and their dependents for gas, gasoline and necessities, as well as medical services that are provided using PEMEX's infrastructure. (See Note 12).

Effective on January 1, 2005, PEMEX adopted the amendments of Bulletin D-3, which provide additional valuation and disclosure requirements for recognizing severance payments paid to employees upon dismissal. The adoption of these provisions resulted in the recognition of an initial liability related to prior service costs in the amount of Ps. 1,427,872 and a charge to income upon adoption in the same amount, which is presented in the consolidated statement of operations as part of the cumulative effect of adoption of new accounting standards.

m. Derivative financial instruments and hedging operations

As of January 1, 2005, PEMEX adopted the provisions of Bulletin C-10, "Derivative Financial Instruments and Hedging Operations" ("Bulletin C-10") issued by the Mexican Institute of Public Accountants, which provide expanded guidance for the recognition, valuation and disclosure applicable to derivative financial instruments designed as hedges and embedded derivatives. The adoption of these provisions resulted in the recognition of an initial cumulative effect to the comprehensive loss in equity of Ps. 6,824,799 and a charge to income for the year of Ps. 477,996, which is presented in the consolidated statement of operations as part of the cumulative effect of adoption of new accounting standards (see Note 11).

As of December 31, 2007 and 2006, derivative financial instruments shown in the balance sheet are recorded at their fair value in accordance with the provisions of Bulletin C-10 (see Note 11).

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

n. Financial instruments with characteristics of liability, equity or both

Financial instruments issued by PEMEX with characteristics of equity or liabilities, or both, are recorded at the time of issuance as a liability, equity or both, depending on the components involved. Initial costs incurred in the issuance of those instruments are assigned to liabilities and equity in the same proportion as the amounts of their components. Gains or losses related to the components of financial instruments classified as liabilities are recorded as part of comprehensive financing result. The distribution of profits to the owners of the components of financial instruments classified as equity is charged to equity.

o. Restatement of equity, other contributions and retained earnings

The restatement of equity, other contributions and accumulated losses is determined by applying factors derived from the NCPI from the dates of contributions to the most recent year end.

p. Cumulative effect of the Hydrocarbon tax

The cumulative effect from the hydrocarbon reserve tax represents the effect from the initial recognition of cumulative deferred taxes.

q. Surplus in the restatement of equity

The surplus in the restatement of equity is related to the cumulative results from the initial net monetary position and the results from holding non-monetary assets (mainly inventories and properties and equipment), restated in Mexican pesos with purchasing power as of the most recent balance sheet date.

r. Taxes and federal duties

Petróleos Mexicanos and the Subsidiary Entities are subject to special tax laws, which are based mainly on petroleum production, price forecasts and revenues from oil and refined products. Petróleos Mexicanos and the Subsidiary Entities are not subject to the *Ley del Impuesto Sobre la Renta* ("Income Tax Law"), the *Ley del Impuesto al Activo* ("Asset Tax Law") or the *Ley del Impuesto Empresarial a Tasa Única* ("Flat Rate Business Tax") (see Note 18).

s. Special Tax on Production and Services (IEPS Tax)

The IEPS Tax charged to customers is a tax on domestic sales of gasoline and diesel. The applicable rates depend on, among other factors, the product, producer's price, freight costs, commissions and the region in which the respective product is sold.

t. Revenue recognition

For all export products, risk of loss and ownership title is transferred upon shipment, and thus PEMEX records sales revenue upon shipment to customers abroad. In the case of certain domestic sales in which the customer takes product delivery at a PEMEX facility, sales revenues are recorded at the time delivery is taken. For domestic sales in which PEMEX is responsible for product delivery, risk of loss and ownership is transferred at the delivery point, and PEMEX records sales revenue upon delivery.

u. Comprehensive result

Comprehensive result represents the sum of net income (loss) for the period plus the effect of inflation restatement, the net effect of exchange rate fluctuations, the effect of valuation of financial

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

instruments designated as cash flow hedges, the equity effect of labor reserve and items required by specific accounting standards to be reflected in equity but which do not constitute equity contributions, reductions or distributions, and is restated on the basis of NCPI factors (see Note 13).

v. Comprehensive financing result

Comprehensive financing result includes interest income and expense, foreign exchange gains and losses, monetary position gains and losses and valuation effects of financial instruments, reduced by the amounts capitalized.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of execution or settlement. Foreign currency assets and liabilities are translated at the exchange rate in effect at the balance sheet date. Exchange differences arising from assets and liabilities denominated in foreign currencies are recorded in operations for the year.

Monetary position gains and losses are determined by multiplying the difference between monetary assets and liabilities at the beginning of each month, including deferred taxes, by inflation rates through year end. The aggregate of these results represents the monetary gain or loss for the year arising from inflation, which is reported in operations for the year.

w. Contingencies

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount thereof can be reasonably estimated. When a reasonable estimation cannot be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings or assets are not recognized until realization is assured (see Note 16).

x. Deferred taxes

Deferred taxes are recorded based on the assets and liabilities comprehensive approach method, which consists of the recognition of deferred taxes by applying the tax rate to the temporary differences between accounting and the tax basis of assets and liabilities. Based on the new fiscal regime enacted in 2005 and applicable to Petróleos Mexicanos and the Subsidiary Entities effective January 1, 2006, Pemex-Gas and Basic Petrochemicals established a deferred tax liability primarily as the result of temporary differences related to advances from customers, accruals and fixed assets. In addition, certain Subsidiary Companies have historically recorded deferred tax liabilities based on concepts similar to those discussed above (see Note 18).

y. Accounting changes

The FRS B-3, *Statement of Income*, issued by the Mexican Board for Research and Development of Financial Reporting Standards (*Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera* or "CINIF") became effective beginning January 1, 2007. Accordingly, the accompanying statement of income for 2006, has been modified for reporting as provided under this FRS, which, together with the *Interpretación a las Normas de Información Financiera* (Interpretation of Financial Reporting Standards or "INIF") 4, modified the general guidelines for the presentation and structure of the statement of income, eliminating the special and extraordinary items classifications.

In addition, this FRS requires that ordinary costs and expenses be classified based on their purpose, function, or a combination of both. Since PEMEX is an industrial entity, ordinary costs and expenses are classified in order to present the gross income margin.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

FRS D-6, *Capitalization of Comprehensive Financial Results* (“CFR”) issued by the CINIF, became effective beginning January 1, 2007. This FRS establishes the requirement to capitalize CFR attributable to certain assets having an extended acquisition period prior to being put into use (see Note 9a.)

Certain line items in the consolidated financial statements as of December 31, 2006 have been reclassified in order to make the presentation comparable to the corresponding line items in the consolidated financial statements as of December 31, 2007.

In addition certain reclassifications have been made to 2006 and 2005 amounts presented in the consolidated financial statements and related notes to conform such amounts and disclosures to the December 31, 2007 consolidated financial statement presentation.

z. Convenience translation

U.S. dollars shown in the balance sheets, the statements of operations, the statements of changes in equity and statements of changes in financial position have been included solely for the convenience of the reader. Such amounts are translated from pesos, as a matter of arithmetic computation only, at the exchange rate for the settlement of obligations in foreign currencies provided by *Banco de México* and the SHCP at December 31, 2007 of 10.8662 pesos per one U.S. dollar. Translations herein should not be construed as a representation that the peso amounts have been or could be converted into U.S. dollars at the foregoing rate or any other rate.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 4 —FOREIGN CURRENCY EXPOSURE:

As of December 31, 2007 and 2006, the consolidated financial statements of PEMEX included the following assets and liabilities denominated in foreign currencies and were as follows:

	Amounts in foreign currency (Thousands)			Year-end Exchange rate	Amounts in pesos
	Assets	Liabilities	Net liability position		
2007:					
U.S. dollars	16,950,060	(30,083,877)	(13,133,817)	10.8662	(Ps.142,714,682)
Japanese yen	—	(142,217,370)	(142,217,370)	0.0973	(13,837,750)
Pounds sterling	230	(402,411)	(402,181)	21.6074	(8,690,086)
Euros	9,371	(5,932,198)	(5,922,827)	15.8766	(94,034,355)
Swiss francs	—	(260)	(260)	9.5957	(2,495)
Currency Danish crowns	—	(250)	(250)	2.0075	(502)
Total liability position, before foreign currency hedging					<u>(Ps.259,279,870)</u>

	Amounts in foreign currency (Thousands)			Year-end Exchange rate	Amounts in nominal pesos
	Assets	Liabilities	Net liability position		
2006:⁽¹⁾					
U.S. dollars	20,872,208	(46,944,810)	(26,072,603)	10.8810	(Ps.283,695,982)
Japanese yen	—	(150,040,948)	(150,040,948)	0.0913	(13,698,739)
Pounds sterling	711	(401,812)	(401,101)	21.3061	(8,545,898)
Euros	23,635	(4,201,854)	(4,178,219)	14.3248	(59,852,152)
Swiss francs	562,443	(443,338)	119,105	8.9064	1,060,797
Total liability position, before foreign currency hedging					<u>(Ps.364,731,974)</u>

(1) The figures of December 31, 2006 in pesos are stated in thousands of Mexican pesos as of December 31, 2006 purchasing power (nominal value). Furthermore, as of December 31, 2007 and 2006, PEMEX had foreign exchange hedging instruments, which are discussed in Note 11.

NOTE 5 —CASH AND CASH EQUIVALENTS:

At December 31, cash and cash equivalents were as follows:

	2007	2006
Cash on hand and in banks	Ps. 64,578,352	Ps. 95,760,432
Marketable securities	106,418,888	100,016,025
	<u>Ps. 170,997,240</u>	<u>Ps. 195,776,457</u>

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 6 —ACCOUNTS, NOTES RECEIVABLE AND OTHER:

At December 31, accounts, notes receivable and other receivables were as follows:

	<u>2007</u>	<u>2006</u>
Domestic customers	Ps. 40,506,098	Ps. 34,729,334
Export customers	25,430,178	19,625,463
Negative IEPS Tax pending to be credited (Note 18)	32,943,613	13,372,968
Advance payments to Mexican Government of minimum guaranteed dividends (Note 14)	4,270,225	268,990
Specific funds (Note 14)	11,858,575	35,589,790
Employees and officers	3,648,372	3,174,902
Tax credits	4,035,632	1,505,183
Other accounts receivable	30,308,784	31,570,645
	<u>153,001,477</u>	<u>139,837,275</u>
Less allowance for doubtful accounts	<u>(1,490,934)</u>	<u>(2,674,170)</u>
	<u>Ps. 151,510,543</u>	<u>Ps. 137,163,105</u>

NOTE 7 —INVENTORIES:

At December 31, inventories were as follows:

	<u>2007</u>	<u>2006</u>
Crude oil, refined products, derivatives and petrochemical products	Ps. 87,971,050	Ps. 56,796,075
Materials and supplies in stock	6,370,017	6,673,156
Materials and products in transit	148,376	300,123
	<u>94,489,443</u>	<u>63,769,354</u>
Less allowance for slow-moving and obsolete inventory	<u>(1,346,307)</u>	<u>(1,705,556)</u>
	<u>Ps. 93,143,136</u>	<u>Ps. 62,063,798</u>

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 8 — INVESTMENT IN SHARES OF NON-CONSOLIDATED SUBSIDIARIES AND ASSOCIATED:

The investments in shares of non-consolidated subsidiaries affiliates and others were as follows:

<u>Subsidiaries and Affiliates Shares:</u>	<u>Percentage of Investment</u>	<u>Carrying Value at December 31,</u>	
		<u>2007</u>	<u>2006</u>
Repsol YPF, S.A.(1)	5.00%	Ps. 23,146,258	Ps. 23,192,819
Deer Park Refining Limited(2)	50.00%	7,113,824	5,924,890
Instalaciones Inmobiliarias para Industrias, S.A. de C.V.	100.00%	1,122,215	1,110,643
Servicios Aéreos Especializados Mexicanos, S.A. de C.V.	49.00%	5,147	5,147
Other-net		1,675,910	2,527,447
Total investments		<u>Ps. 33,063,354</u>	<u>Ps. 32,760,946</u>

<u>Profit Sharing in Non-Subsidiaries and Affiliates:</u>	<u>For the Year Ended December 31,</u>		
	<u>2007</u>	<u>2006</u>	<u>2005</u>
Repsol YPF, S.A.(1)	Ps. 588,729	Ps. 3,621,872	Ps. 2,610,657
Deer Park Refining Limited(2)	4,944,329	6,419,178	6,004,199
Instalaciones Inmobiliarias para Industrias, S.A. de C.V.	11,996	32,527	43,809
Total profit sharing	<u>Ps. 5,545,054</u>	<u>Ps. 10,073,577</u>	<u>Ps. 8,658,665</u>

(1) PEMEX owned 59,884,453 and 59,404,128 shares of Repsol YPF, S.A. at December 31, 2007 and 2006, respectively.

(2) PMI NASA has a 50% joint venture with Shell Oil Company, through which it owns a 50% interest in a petroleum refinery located in Deer Park, Texas. The investment is accounted for under the equity method. During 2007, 2006 and 2005, PEMEX recorded Ps. 4,944,329, Ps. 6,419,178 and Ps. 6,004,199 of profits, respectively, related to its equity in the results of the joint venture, which has been recorded under "profit sharing in non-consolidated subsidiaries and affiliates" in the statement of operations. In 2006 and 2005, PEMEX paid the joint venture Ps. 11,078,973 and Ps. 10,742,295, respectively, for the processing of crude oil. As of December 31, 2006 the contract between PMI NASA and Pemex-Refining, was concluded and it was not renewed.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 9 —PROPERTIES, PLANT AND EQUIPMENT:

At December 31, components of properties, plant and equipment were as follows:

	<u>2007</u>	<u>2006</u>
Plants	Ps. 379,268,733	Ps. 357,366,268
Pipelines	296,304,941	278,873,434
Wells	466,157,259	412,518,087
Drilling equipment	22,226,019	22,363,980
Buildings	47,681,968	42,210,278
Offshore platforms	160,543,843	139,223,391
Furniture and equipment	36,440,294	34,809,700
Transportation equipment	14,146,501	14,008,239
	1,422,769,558	1,301,373,377
Less:		
Accumulated depreciation and amortization	(760,177,709)	(693,295,137)
Net value	662,591,849	608,078,240
Land	39,842,669	42,164,885
Construction in progress	90,720,481	86,150,194
Fixed assets to be disposed of	690,454	802,138
Total	Ps. 793,845,453	Ps. 737,195,457

- a) PEMEX capitalized interest associated with the construction or installation of property, plant and equipment, totaling Ps. 6,996,305 and Ps. 5,541,036, as of December 31, 2007 and 2006, respectively. Starting in 2007, as part of the adoption of NIF-6, PEMEX capitalized Ps 5,350,849 of comprehensive financing costs related to qualified fixed assets, as these costs were directly related to investments during the acquisition phase of a project.
- b) Total depreciation of fixed assets and amortization of wells for the years ended December 31, 2007, 2006 and 2005 were Ps. 72,591,718, Ps. 65,672,189 and Ps.56,995,357, respectively, which includes amortization costs related to dismantlement and abandonment cost for the years ended December 31, 2007, 2006 and 2005 of Ps. 2,554,062, Ps. 508,361 and Ps. 1,370,730, respectively.
- c) As of December 31, 2007 and 2006, the capitalized portion related to dismantlement and abandonment costs, net of accumulated amortization, and determined based on the present value (discounted) of the project cost, was Ps. 17,148,400 and Ps. 16,027,307, respectively.
- d) During 2007 PEMEX performed its impairment review of the value of long-live assets and concluded that there was no impairment for the year. As of December 31, 2006 and 2005, PEMEX recognized cumulative impairment charges in the value of the long-lived assets amounting to Ps. 14,593,955 and Ps. 13,890,780, respectively. (see Note 3j).

NOTE 10 —DEBT:

Under the *Ley General de Deuda Pública* (“General Law of Public Debt”), the *Secretaría de Hacienda y Crédito Público* (Ministry of Finance and Public Credit or “SHCP”) authorizes the Mexican

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Government entities, in this case Petróleos Mexicanos and the Subsidiary Entities, to negotiate and execute external financing agreements, defining the requirements that must be observed in each case.

In addition, PEMEX is authorized to enter into and manage public debt of the Mexican Government and to guarantee these transactions to international organizations of which Mexico is part of and to national and international public and private entities.

In 2007, significant financing activities of Petróleos Mexicanos were as follows:

Petróleos Mexicanos obtained U.S.\$7,310 under lines of credit granted by export credit agencies. These loans bear interest at fixed and variable rates with various maturity dates through 2012.

During 2007, the Master Trust undertook the following financing activities for PIDIREGAS:

- a. The Master Trust obtained credit lines from export credit agencies totaling U.S.\$1,002,629.
- b. During the second quarter of 2007, the Master Trust repurchased, in the open market certain amount of its outstanding U.S. dollar-denominated debt securities with maturities between 2008 and 2027. The total principal amount repurchased in this program was equal to U.S.\$1,139,696. These securities were cancelled after their repurchase.
- c. On October 18, 2007, the Master Trust utilized the full amount of its syndicated revolving credit facility in the amount of U.S.\$2,500,000. This credit line was signed on September 14, 2007; it may be used either by Petróleos Mexicanos or the Master Trust; the credit line consists of two tranches, A and B, with terms of three and five years, respectively and bears interest at rates of LIBOR plus 20 basis points for tranche A and 25 basis points for tranche B; and matures in 2010 and 2012, respectively; and each of the tranches may be extended twice, by one year. This credit line replaces the two previously syndicated revolving credit lines, each in the amount of U.S.\$1,250,000.
- d. On October 22, 2007, the Master Trust issued notes for the amount of U.S.\$2,000,000, of which U.S.\$1,500,000 notes were issued at a coupon rate of 5.75% due in 2018 and U.S.\$500,000 bonds at a coupon rate of 6.625%, due in 2035. This issuance was a second reopening of an issuance which took place on June 8, 2005.
- e. During the fourth quarter of 2007, the Master Trust repurchased in the open market U.S.\$5,763,333, of notes, which represent a part of its own debt in notes with maturities between 2008 and 2027, as well as certain amount of its U.S. dollar-denominated perpetual notes. These securities were cancelled after their repurchase.

In 2006, significant financing activities of Petróleos Mexicanos were as follows:

- a. Petróleos Mexicanos obtained credit lines from export credit agencies totaling U.S.\$56,241. These loans bear interest at fixed and variable rates with various maturity dates through 2012.
- b. Petróleos Mexicanos drew a total amount of U.S.\$3,300,000 of under its revolving credit lines. These credit lines may be utilized by Petróleos Mexicanos and the Master Trust.
- c. On February 13, 2006, the Master Trust completed an exchange offer pursuant to which the Master Trust issued notes with a principal amount totaling U.S.\$185,310 in exchange for an equal principal amount of notes previously issued by Petróleos Mexicanos, through a reopening of an original exchange offer made in December 2004. As a result of this second exchange, the Master

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Trust issued new notes and subsequently received cash payments from Petróleos Mexicanos upon the cancellation of the Petróleos Mexicanos notes acquired by the Master Trust.

Cash payments were made on the following dates and in the following amounts:

June 1, 2006	U.S.\$	41,254
June 2, 2006		54,011
August 3, 2006		90,045
Total	<u>U.S.\$</u>	<u>185,310</u>

During 2006, the Master Trust undertook the following financing activities for PIDIREGAS:

- a. The Master Trust obtained credit lines from export credit agencies totaling U.S.\$1,914,184 and U.S.\$4,250,000 by refinancing a syndicated loan in two tranches of U.S.\$1,500,000 and U.S.\$2,750,000 due in five and seven years, respectively.
- b. On February 2, 2006, the Master Trust reopened two series of notes issued on June 8, 2005 under its Medium-Term Notes Program Series A in two tranches: U.S.\$750,000 of 5.75% Notes due in 2015, and U.S.\$750,000 of 6.625% Notes due in 2035, both of which are guaranteed by Petróleos Mexicanos.
- c. The Master Trust drew a total aggregate amount of U.S.\$2,250,000 of its revolving credit lines guaranteed by Petróleos Mexicanos. These credit lines may be utilized by Petróleos Mexicanos and the Master Trust.

During 2006, the Fideicomiso F/163 undertook the following financing activity:

On June 16, 2006, the Fideicomiso F/163 issued publicly-traded notes (*certificados bursátiles*) in the amount of Ps. 10,000,000 (in nominal terms), due in seven years, with a monthly interest rate of *Tasa de Interés Interbancaria de Equilibrio* (the Mexican Interbank Interest Rate or "TIIE") less 0.07% and guaranteed by Petróleos Mexicanos.

Various credit facilities require compliance with various operating covenants which, among other things, place restrictions on the following types of transactions:

- The sale of substantial assets essential for the continued operations of the business;
- Liens against its assets; and
- Transfers, sales or assignments of rights to payment under contracts for the sale of crude oil or gas not yet earned, accounts receivable or other negotiable instruments.

As of December 31, 2007 and 2006, PEMEX was in compliance with the operating covenants described above.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

As of December 31, 2007 and 2006, long-term debt was as follows:

	Rate of Interest ⁽²⁾	Maturity	December 31, 2007		December 31, 2006				
			Pesos (Thousands)	Foreign currency (Thousands)	Pesos (Thousands)	Foreign currency (Thousands)			
U.S. dollars:									
Bonds	Fixed from 4.75% to 9.5% and LIBOR plus 0.425% to 1.8%	Various to 2035	Ps.163,225,526	12,119,761	Ps.238,931,860	21,163,109			
Financing assigned to PIDIREGAS	Fixed from 3.23% to 7.69% and LIBOR plus 0.02% to 2.25%	Various to 2017	72,163,251	6,641,075	76,624,927	6,786,963			
Purchasing loans and project financing	Fixed from 3.32% to 5.04% and LIBOR plus 0.0625% to 2%	Various to 2014	2,108,662	194,057	3,229,236	286,026			
Leasing contracts	Fixed from 8.05% to 9.91%	Various to 2012	—	—	793,645	70,296			
Credit lines	LIBOR plus 0.20% and 0.25%	Various to 2023	27,165,500	2,500,000	—	—			
External trade loans	LIBOR plus 0.325% to 0.475%	Various to 2013	46,181,350	4,250,000	48,659,972	4,310,000			
Bank loans	Fixed from 5.44% to 5.58% and LIBOR plus 0.7% to 1.9%	Various to 2013	5,107,114	470,000	7,056,260	625,000			
Total financing in U.S. dollars			315,951,403	26,174,893	375,295,900	33,241,394			
Euros:									
Bonds	Fixed from 5.5% to 6.62%, and floating of 8.21467%	Various to 2025	50,857,376	3,203,291	60,800,196	4,090,634			
Unsecured loans, banks and project financing	Fixed from 2%	2016	5,544	349	5,977	402			
Total financing in Euros			50,862,920	3,203,640	60,806,173	4,091,036			
Japanese yen:									
Direct loans	Fixed from 4.2%	2009	468,081	4,810,695	683,590	7,216,043			
Bonds	Fixed from 3.5%	2023	2,919,000	30,000,000	2,841,959	30,000,000			
Project financing	Prime 2.9081% and Fixed from 1% to 2.4%	Various to 2017	10,871,232	111,729,003	9,772,409	103,158,512			
Total financing in Yen			14,258,313	146,539,698	13,297,958	140,374,555			
Sterling pound:									
Bonds	Fixed 7.5%	2013	8,642,960	400,000	8,842,798	Various			
Pesos:									
Certificates	TIIE less 0.07% and CETES plus 0.35% to 0.65%	Various to 2019	81,918,416		98,019,896				
Syndicated bank loans	TIIE plus 0.35% and fixed from 8.4%	2008	3,500,000		7,263,130				
Project financing and syndicated bank loans	Fixed from 11% and TIIE plus 0.4% to 0.48%	Various to 2012	12,333,333		14,872,123				
Total financing in pesos			97,751,749		120,155,149				
Total principal in pesos ⁽¹⁾			487,467,345		578,397,978				
Plus: Accrued interest			58,565		1,563,831				
Notes payable to contractors			13,352,690		10,753,711				
Total principal and interest			500,878,600		590,715,520				
Less: Short-term maturities			71,499,353		62,745,288				
Current portion of notes payable to contractors			4,550,775		3,494,990				
Total short-term debt			76,050,128		66,240,278				
Long-term debt			Ps.424,828,472		Ps.524,475,242				
			2008	2009	2010	2011	2012	2013 and Thereafter	Total
Maturity of the principal outstanding for each of the years ending December 31,			Ps.76,050,128	Ps.67,453,662	Ps.70,150,790	Ps.56,261,413	Ps.38,928,853	Ps.192,033,754	Ps.500,878,600

Notes to table:

(1) Includes financing from foreign banks of Ps. 355,682,481 and Ps. 418,347,126 as of December 31, 2007 and 2006, respectively.

(2) As of December 31, 2007 and 2006 the rates were as follows: LIBOR, 4.59625% and 5.37%, respectively; the Prime rate in Japanese yen, 1.875% and 1.625%, respectively; the *Cetes* rate, 7.62% for 91 days and 7.71% for 182 days and 7.17% for 91 days and 7.20% for 182 days, respectively; TIIE 7.37% and 8.95%, respectively.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The total amount of notes payable to contractors at December 31, 2007 and December 31, 2006 are as follows:

	<u>2007</u>	<u>2006</u>
Total notes payable to contractors ⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾	Ps. 13,352,690	Ps. 10,753,711
Less: Current portion of notes payable to contractors	4,550,775	3,494,990
Notes payable to contractors (long-term)	<u>Ps. 8,801,915</u>	<u>Ps. 7,258,721</u>

- (1) On November 26, 1997, Petróleos Mexicanos and Pemex-Refining entered into a financed public works contract and a unit-price public works contract with Consorcio Proyecto Cadereyta Conproca, S.A. de C.V. The related contracts are for the reconfiguration and modernization of the Ing. Héctor R. Lara Sosa refinery in Cadereyta, N.L. The original amount of the financed public works contract was U.S.\$1,618,352, plus a financing cost of U.S.\$805,648, due in twenty semi-annual payments of U.S.\$121,200. The original amount of the unit-price public works contract was U.S.\$80,000, including a financing cost of U.S.\$47,600 payable monthly based on the percentage of completion. At December 31, 2007 and 2006, the outstanding balances of the respective contracts were Ps. 5,854,295 and Ps. 8,186,797, respectively.
- (2) On June 25, 1997, PEMEX entered into a 10-year service agreement with a contractor for a daily fee of U.S.\$82.50 for the storage and loading of stabilized petroleum by means of a floating system ("FSO"). At December 31, 2007 and 2006, the outstanding balances were Ps. 242,888 and Ps. 531,296, respectively.
- (3) PEMEX has Financed Public Works Contracts ("FPWC") (formerly known as Multiple Services Contracts or "MSCs") pursuant to which the hydrocarbons and construction in progress are property of PEMEX. Pursuant to the FPWC, the contractors manage the work in progress, classified as development, infrastructure and maintenance. As of December 31, 2007 and 2006, PEMEX has an outstanding payable amount of Ps. 3,228,735 and Ps. 2,035,618, respectively.
- (4) During 2007, a Floating Production Storage and Offloading ("FPSO") vessel was purchased. The investment in the vessel totaled U.S.\$723,575, of which U.S.\$352,996 were paid in 2007 and the remaining amount of U.S.\$370,579 (Ps.4,026,772) as of December 31, 2007, will be paid over a period of 15 years.

NOTE 11 — FINANCIAL INSTRUMENTS:

PEMEX's cash flows arising from its commercial and financial activities are exposed to the volatility of interest rates, currency exchange rates and hydrocarbon prices in the national and international markets.

In order to supervise and mitigate the potential deviations of its cash flows, PEMEX has adopted a General Risk Management framework, which includes the regulation of derivative financial instruments.

Within this framework, the General Risk Management Policies and Guidelines are proposed by the Risk Management Committee and approved by the Board of Directors.

Functions for the Risk Management Committee (the "Committee") include the authorization of the general strategies of risk management. The committee is comprised of representatives of PEMEX, the Central Bank of Mexico, the SHCP and PMI CIM.

Additionally the Risk Management Deputy Director designs and proposes to the Committee the institutional regulations and risk management strategies for managing financial market risk.

(i) Counterparty risk from the use of derivative financial instruments

PEMEX is exposed to credit risk (or repayment risk) when the market value of these instruments is positive (favorable for PEMEX) since it faces a repayment risk if the counterparty fails to fulfill its performance obligations. When the fair value of a derivative contract is negative, the risk belongs to the counterparty.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

In order to minimize this risk, PEMEX only enters into transactions with high credit quality counterparties based on credit ratings from rating agencies such as Standard & Poors and Moodys.

PEMEX's derivative transactions are generally executed on the basis of standard agreements and in general, collateral for financial derivative transactions is neither provided nor received.

(ii) Interest rate risk management

PEMEX is exposed to fluctuations in the interest rates applicable to different currencies. The predominant exposure is to LIBOR in U.S. dollars, due to the fact that most of its debt is denominated in U.S. dollars or hedged to U.S. dollars through currency swaps. The use of derivative financial instruments allows PEMEX to obtain an acceptable composition of fixed and variable rates in the debt portfolio.

The derivative financial instruments used in PEMEX's hedging transactions consist principally of fixed-floating interest rate swaps, and under these instruments PEMEX has the right to receive payments based on LIBOR or Mexican interest rates (TIIE) and is entitled to pay a fixed rate.

(iii) Exchange rate risk management

Since a significant amount of PEMEX's revenues is denominated in U.S. dollars, PEMEX generally obtains loans in U.S. dollars. However, PEMEX also borrows in currencies other than U.S. dollar in order to take advantage of existing financing conditions of these foreign currencies.

PEMEX has entered into currency swaps transactions as a hedging strategy against exchange fluctuations of debt issued in currencies other than U.S. dollars.

(iv) Commodity price risk management

Natural gas:

PEMEX offers to its customers derivative financial instruments as a value added service and PEMEX provides various hedging contracts to its customers in order to give them the option of protecting themselves against fluctuations in the price of its products. The risk that PEMEX acquires under these contracts is transferred to financial counterparties through its MGI Supply Ltd. Subsidiary.

Crude oil:

Due to its fiscal regime, PEMEX transfers most of its risk related to crude oil prices to the Mexican Government. As a consequence, PEMEX generally does not enter into long-term hedging transactions against fluctuations in crude oil prices. During 2007 and 2006, PEMEX did not enter into any crude oil price hedging transactions.

(v) Fair value of derivative financial instruments

The fair value of derivative financial instruments is sensitive to movements in the underlying market rates and variables. PEMEX monitors the fair value of derivative financial instruments on a periodic basis. Fair values are calculated for each derivative financial instrument, and represent the price at which one party would assume the rights and duties of another party. Fair values of financial derivatives have been calculated using common market valuation methods with reference to available market data as of the balance sheet date.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

- The fair value for interest rate, exchange rate and hydrocarbon derivative instruments is determined by discounting future cash flows as of the balance sheet date, using market quotations for the instrument's remaining life.
- Prices for options are calculated using standard option-pricing models commonly used in the international financial market.
- Exchange-traded energy futures contracts are valued individually at daily settlement prices quoted on the futures markets.

(vi) Embedded derivatives

As of December 31, 2007, PEMEX recognized a net gain of Ps. 5,990,399 recorded in comprehensive financial result, as a result of the foreign currency embedded derivatives detected from contracts denominated in currencies other than the functional currency of PEMEX and its counterparties. These embedded derivatives have been modeled and valued as multiple currency forwards, by using models and inputs commonly used in the market and based on the expected exchange rates between Mexican pesos and the currency of each contract. If expected exchange rates as of the balance sheet date appreciate with respect to those observed at the signing date of each contract, the positive effects will increase.

(vii) Operations with derivative financial instruments

PEMEX enters into derivative financials transactions with the sole purpose of hedging financial risks related to its operations, assets, or liabilities. Nonetheless, some of these transactions do not qualify for hedge accounting and therefore are recorded in the financial statements as non-hedges, despite the fact that their cash flows are offset by the cash flows of the positions to which they relate.

PEMEX seeks to mitigate the impact of market risk in its financials statements, through the establishment of a liability structure consistent with its expected operative cash flows.

As a result, PEMEX seeks to eliminate exchange rate risk of the debt issued in currencies other than pesos or U.S. dollars by entering derivative financial instruments contracts.

Likewise, the applicable accounting rules for derivative financial instruments, establish that a derivative cannot be designated as a hedge of another derivative; therefore, the derivatives offered by PEMEX to its clients, as a value added service, as well as those entered into with the opposite position in order to offset that effect, are treated for accounting purposes as non-hedges.

As of December 31, 2007 and 2006, the fair value of the derivative instruments was (Ps. 6,665,027) and (Ps. 8,982,308), respectively. These amounts include the derivative instruments designated as cash flow hedges and their fair value of (Ps. 977,664) and (Ps. 1,705,290), respectively, that were recorded under other comprehensive loss.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The following table shows the fair value and the notional amount of the over-the-counter derivative instruments, outstanding as of December 31, 2007 and 2006, which are designated as cash flow hedges:

	2007		2006	
	<u>Notional Value</u>	<u>Fair Value</u>	<u>Notional Value</u>	<u>Fair Value</u>
Interest rate swaps:				
Pay fixed/receive variable	<u>Ps. 14,211,489</u>	<u>(Ps. 1,267,432)</u>	<u>Ps. 17,741,995</u>	<u>(Ps. 1,877,925)</u>
Cross-currency swaps:				
Pay Mexican Peso/receive UDI	<u>Ps. 11,901,650</u>	<u>Ps. 221,101</u>	<u>Ps. —</u>	<u>Ps. —</u>

Derivative instruments designated as cash flow hedges that have the same critical characteristics as the item being hedged are considered to be highly effective.

In light of the foregoing, these instruments do not have an impact in earnings due to hedge inefficiency, and their fair value is recognized in its entirety as part of equity through other comprehensive income. The fair value of these instruments is reclassified into earnings at the same time as the hedged item cash flows affect earnings.

If a derivative instrument designated as a cash flow hedge is not effective, the ineffectiveness portion of its fair value has an impact on earnings and the effective portion is recorded as part of equity through other comprehensive income and is reclassified into earnings, while the hedged items cash flows affect earnings.

When a cash flow hedge is no longer effective, the accumulated gains or losses that were recorded in other comprehensive income have to remain in this account and be reclassified into earnings at the same time as the hedge item cash flows affect earnings; however, from that date forward, the derivative instrument will lose the hedge accounting treatment. As of December 31, 2007, only one interest rate swap designated as a cash flow hedge had lost its effectiveness.

As of December 31, 2007, a net loss of Ps. 1,479,284 was reclassified from other comprehensive income into earnings and it is estimated that in 2008 a net loss of Ps. 812,620 will be reclassified from other comprehensive income into earnings.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The following table shows the fair value and the notional amount of over-the-counter derivative instruments as of December 31, 2007 and 2006 that were treated for accounting purposes as non-hedges:

	2007		2006	
	Notional Value	Fair Value	Notional Value	Fair Value
Interest rate swaps pay fixed/receive variable	Ps. 5,000,000	(Ps. 185,719)	Ps. 5,187,950	(Ps. 381,586)
Cross-currency swaps:				
Pay U.S. Dollar/receive Euros	44,730,188	3,549,308	59,713,915	1,796,741
Pay U.S. Dollar/receive Japanese Yen	13,549,835	(355,956)	13,310,235	(968,825)
Pay U.S. Dollar/receive Ponds Sterling	<u>7,417,159</u>	<u>1,120,775</u>	<u>7,706,453</u>	<u>1,294,656</u>
Natural gas swaps:				
Pay fixed/receive variable	Ps. 5,163,787	Ps. 202	Ps. 5,683,033	Ps. 11,916,029
Pay variable/receive fixed	5,185,476	16,882	6,668,063	(11,883,888)
Pay variable/receive variable	<u>472</u>	<u>470</u>	<u>2,493</u>	<u>(3,747)</u>
Natural gas options:				
Put				
Purchase		Ps. 73,261		Ps. 31,953
Sale		(74,064)		384
Call				
Purchase		361,510		117,280
Sale		<u>(361,300)</u>		<u>(116,576)</u>

Note: The exchange rates as of December 31, 2007 and 2006 were Ps. 10.8662 and 10.8810 per U.S. dollar, respectively.

As of December 31, 2007 and 2006, PEMEX recognized a net (loss) and a net profit of (Ps. 514,893) and Ps. 916,790, respectively, in the comprehensive financing cost related to operations with derivative financial instruments treated for accounting purposes as non-hedges.

As of December 31, 2007, PEMEX recognized a net loss of Ps. 702,173, in other revenues related to operations with derivative financial instruments treated for accounting purposes as non-hedges.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The estimated fair value of financial instruments other than derivatives for which it is practicable to estimate their value, as of December 31, 2007 and 2006, in nominal terms, is as follows:

	2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Cash and cash equivalents	Ps. 170,997,240	Ps. 170,997,240	Ps. 195,776,457	Ps. 195,776,457
Accounts receivable, notes and other	151,510,543	151,510,543	137,163,105	137,163,105
Derivative financial instruments	12,909,868	12,909,868	4,389,836	4,389,836
Liabilities:				
Suppliers	35,138,344	35,138,344	37,102,983	37,102,983
Accounts and accumulated expenses payable	18,097,530	18,097,530	14,592,081	14,592,081
Taxes payable	146,593,355	146,593,355	45,006,644	45,006,644
Derivative financial instruments	13,584,495	13,584,495	13,372,143	13,372,143
Current portion of long-term debt	76,050,128	76,050,128	66,240,278	66,240,278
Long-term debt	424,828,472	442,731,344	524,475,242	556,153,282

The fair value of the financial instruments presented in the previous table appears for informative purposes.

The nominal value of financial instruments such as cash equivalents, accounts receivable and payable, taxes payable and current portion of long-term debt approximate their fair value because of their short maturities.

The fair value of long-term debt is determined by reference to market quotes, and, where quotes are not available, is based on discounted cash flow analyses. Because assumptions significantly affect the derived fair value and they are inherently subjective in nature, the estimated fair values may not necessarily be realized in a sale or settlement of the instrument.

NOTE 12 —LABOR OBLIGATIONS:

PEMEX has established employee non-contributory retirement plans in accordance with the *Ley Federal del Trabajo* ("Federal Labor Law") and under collective bargaining agreements. Benefits are determined based on years of service and final salary at retirement. Liabilities and costs of such plans, including those related to the seniority premium benefit, to which every employee is entitled upon termination of employment, are recorded in accordance with actuarial valuations performed by independent actuaries.

PEMEX partially funds its labor obligations through a Mexican trust structure, the resources of which come from the seniority premium item of the Governmental Budget, or any other item that substitutes or could be connected to this item, or that is associated to the same item and the interests, dividends and capital gains obtained from the investments of the trusts.

PEMEX has also established plans for other post-retirement benefit obligations whose actuarial amounts are determined by independent actuaries. Such plans include the following benefits: cash provided to the retired personnel and their dependents for gas consumption, gasoline and other basic necessities, as well as, medical services which are provided using PEMEX's infrastructure.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Cash Flow:

Plan contributions and benefit paid were as follows:

	<u>Retirement remunerations, seniority premiums, pension and indemnity</u>		<u>Other post-retirement Benefits</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Contribution to the pension plan assets	Ps.19,357,177	Ps.13,221,734	Ps.5,750,386	Ps.5,207,690
Payments charged to the plan assets	13,449,831	11,839,880	5,750,386	5,207,690

Payments related to medical services provided to retired personnel were Ps. 2,609,707 and Ps. 2,574,209, during 2007 and 2006, respectively.

The cost, obligations and other elements of the pension plan, seniority premium plan and other post-retirement benefits plans different from restructuring, mentioned in Note 31 of these financial statements, were determined, based on calculations prepared by independent actuaries as of December 31, 2007, 2006 and 2005.

The components of net periodic cost for the years ended December 31, 2007, 2006 and 2005 are as follows:

	<u>Retirement remunerations, seniority premiums, pension and indemnity</u>			<u>Other post-retirement benefits</u>		
	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Net periodic cost:						
Service cost	Ps. 9,167,594	Ps. 7,507,356	Ps. 6,513,609	Ps. 6,405,902	Ps. 5,881,745	Ps. 4,163,849
Financial cost	27,246,555	24,571,208	20,983,951	21,795,906	18,562,492	15,479,140
Return on plan assets	(26,007)	(51,860)	(185,989)	—	—	—
Amortization of prior services cost and plan amendments	677,353	663,036	364,519	4,483,931	4,447,357	4,478,314
Variances in assumptions and experience adjustments	1,319,028	671,355	(168,555)	(1,352,970)	(3,131,317)	(3,811,680)
Amortization of transition liability	6,133,654	6,114,252	6,157,546	6,407,047	6,357,929	6,402,163
Inflation adjustment	1,650,858	1,598,629	1,118,730	1,398,004	1,301,166	889,879
Total periodic cost	46,169,035	41,073,976	34,783,811	39,137,820	33,419,372	27,601,665
Recognition of severance payments	—	—	1,402,142	—	—	—
Net periodic cost	Ps. 46,169,035	Ps. 41,073,976	Ps. 36,185,953	Ps. 39,137,820	Ps. 33,419,372	Ps. 27,601,665

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The actuarial present value of benefit obligations is as follows:

	Retirement remunerations, seniority premiums, pension and indemnity		Other post-retirement benefits	
	2007	2006	2007	2006
Vested benefit obligation value:				
Vested benefit obligation	Ps.206,364,293	Ps.191,557,538	Ps. —	Ps. —
Accumulated benefit obligation (ABO) obligation	Ps.357,768,687	Ps.330,616,544	Ps. —	Ps. —
Projected benefit obligation (PBO)/ Plan assets at fair value	Ps.367,485,744 (7,664,407)	Ps.336,758,891 (2,118,402)	Ps.300,396,198 —	266,481,493 —
Projected benefit obligation over plan assets	359,821,337	334,640,489	300,396,198	266,481,493
Items to be amortized:				
Prior services cost and plan amendments	(6,449,919)	(7,080,185)	(58,102,534)	(62,590,753)
Variances in assumptions and experience adjustments	(54,196,339)	(49,016,755)	743,034	14,811,311
Unamortized transition liability	(66,631,947)	(72,807,858)	(71,146,932)	(77,594,439)
Project liability net	232,543,132	205,735,691	171,889,766	141,107,612
Additional liability	123,768,374	124,821,880	—	—
Total liability	Ps.356,311,506	Ps.330,557,571	Ps.171,889,766	Ps.141,107,612

Significant assumptions used in determining the net periodic cost of plans are as follows:

	Retirement remunerations, seniority premiums, pension and indemnity		Other post-retirement benefits	
	2007	2006	2007	2006
Discount rate	4.25%	4.25%	4.25%	4.25%
Rate of compensation increase	0.50%	0.50%	0.50%	0.50%
Expected long term rate of the return on plan assets	4.25%	4.25%	—	—
Employees' average remaining labor life over which pending amortization items are amortized	11 years	12 years	11 years	12 years

Plan assets

The Plan assets are included into two trusts, *Fondo Laboral Pemex* ("FOLAPE") and *Fideicomiso de Cobertura Laboral y de Vivienda* ("FICOLAVI"), which are managed by BBVA Bancomer, S. A. and a Technical Committee, which is composed of personnel from Petróleos Mexicanos and the trusts.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The weighted-average asset allocation of retirement benefits, for seniority premiums, pensions and other benefits are as follows:

<u>Type of Investment</u>	<u>Retirement remunerations, seniority premiums, pension and indemnity</u>		<u>Other post-retirement benefits</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
	Governmental securities	84.2%	71.0%	84.2%
Fixed rate securities	15.8%	29.0%	15.8%	29.0%
Total	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

NOTE 13 — COMPREHENSIVE (LOSS) INCOME:

Comprehensive (loss) income for the years ended December 31, 2007, 2006 and 2005 was as follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Net (loss) income	(Ps. 18,307,569)	Ps. 46,953,205	(Ps. 82,357,982)
Surplus in restatement of equity	18,638,402	4,064,648	8,184,288
Derivative financial instruments	656,699	5,274,109	(7,036,437)
Effect on equity from labor obligations	(3,432,792)	(18,871,922)	(21,672,659)
Other	—	710,094	—
Comprehensive (loss) income for the year	<u>(Ps. 2,445,260)</u>	<u>Ps. 38,130,134</u>	<u>(Ps. 102,882,790)</u>

NOTE 14 — EQUITY:

On December 31, 1990, certain debt owed by Petróleos Mexicanos to the Mexican Government was capitalized as equity. This capitalization amounted to Ps. 22,334,195 in nominal terms (U.S.\$7,577,000) and was authorized by the Board of Directors. The capitalization agreement between Petróleos Mexicanos and the Mexican Government states that the Certificates of Contribution "A" constitute permanent capital. As a result, the Certificates of Contribution "A" are as follows:

	<u>Amount</u>
Certificates of Contribution "A" (nominal value)	Ps. 10,222,463
Inflation restatement increase	86,735,530
Certificates of Contribution "A" in Mexican pesos of December 31, 2007 purchasing power	<u>Ps. 96,957,993</u>

As a condition of this capitalization, Petróleos Mexicanos agreed to pay a minimum guaranteed dividend to the Mexican Government equal to the debt service for the capitalized debt in December 1990. The minimum guaranteed dividend consisted of the payment of principal and interest on the same terms and conditions as those originally agreed upon with international creditors through 2006, at the exchange rates on the date that such payments are made. Such payments must be approved annually by the Board of Directors. This minimum guaranteed dividend was extended until 2007, by the CA-164/2007 agreement.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

During 2007 and 2006, Petróleos Mexicanos paid Ps. 4,270,225 and Ps. 268,990, (Ps. 263,329 nominal value) respectively, to the Mexican Government in advance for the minimum guaranteed dividend. These payments will be applied to final amount that the Board of Directors approves as the total annual dividend, which usually occurs in the following fiscal year.

In 2006, Board of Directors of Petróleos Mexicanos approved the capitalization (*i.e.*, transfer to equity) of Ps. 621,009 (Ps. 594,987 nominal value) for infrastructure works, corresponding to resources from the Mexican Government in accordance with the Federal Revenue Law for 2004.

During 2006, in compliance with the agreement CA399/2004, the Board of Directors of Petróleos Mexicanos approved the capitalization of Ps. 652,310 (Ps. 608,068 nominal terms) of revenues at December 31, 2005, from the Mexican Government for infrastructure works in accordance with the Federal Income Law for 2004.

In December 2006, the Mexican Government made a payment in the amount of Ps. 47,454,593 (Ps. 45,735,400 nominal value) to Petróleos Mexicanos derived from excess revenues that were paid in accordance with the Federal Expenditure Budget for the 2006 fiscal year. This payment increased the equity of Petróleos Mexicanos and the Subsidiary Entities.

In December 2007, the Mexican Government made payments in the amount of Ps. 11,160,824, to Petróleos Mexicanos, which was capitalized in equity. This total includes two payments in the amount of Ps. 11,131,800 and Ps. 19,700, which were additionally received from the *Fondo sobre Ingresos Excedentes* (“*FIEX*”). PEMEX also capitalized interest in the amount of Ps. 9,324 which was related to these payments. This payment derived from excess revenues that were paid in accordance with the *Ley de Presupuesto y Responsabilidad Hacendaria*, (“Federal Budget and Fiscal Responsibility Law”) article 19, fraction IV, clauses b) and c). Additionally, in February 2008, the Mexican Government made another payment in the amount of Ps. 2,806,200, to Petróleos Mexicanos.

In 2004, Petróleos Mexicanos signed an agency agreement (Funds for Specific Purposes — Trade Commission) with Banco Santander Serfin, S.A. as an agent in order to manage the funds transferred by the Mexican Government to Petróleos Mexicanos and Subsidiary Entities. According to the *Ley de Ingresos de la Federación* (“Federal Revenue Law”), these funds are to be utilized only for infrastructure works related to exploration, refining, gas and petrochemicals. Payments made by the Mexican Government that increase the equity of Petróleos Mexicanos and the Subsidiary Entities are deposited into the Fund for Specific Purposes — Trade Commission. As of December 31, 2007 and 2006, the balance of this account was Ps. 11,858,575 and Ps. 35,589,790, respectively (see Note 6).

NOTE 15 — COMMITMENTS:

a. During 2007, PEMEX purchased a Floating Production Storage and Offloading (“FPSO”) vessel. The basic function of this new vessel is the reception and processing of crude oil from marine wells. The tanker treats and separates oil and gas, in order to meet international API guidelines for exports. Upon completion of this process, the tanker stores the product and distributes it to foreign clients’ ships. The tanker has a storage capacity of 2 million barrels and a distribution capacity of 1.2 million barrels per day.

Total investment in the vessel was U.S.\$723,575, of which U.S.\$352,996 was paid in 2007 and the balance will be due over a period of 15 years.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Future estimated payments are as follows:

2008	U.S. \$	25,267
2009		25,267
2010		25,267
2011		25,267
2012		25,267
2013 and thereafter		244,244
Total	<u>U.S. \$</u>	<u>370,579</u>

- b. PEMEX has entered into a nitrogen supply contract for the pressure maintenance program at the Cantarell field. During 2007, an additional contract was incorporated, also with the purpose of supplying nitrogen to the Ku-Maloob-Zap field, extending the original contract until 2027. At December 31, 2007 and 2006, the value of the nitrogen to be supplied during the term of the contract was approximately Ps. 18,314,382 and Ps. 13,377,497, respectively. In the event of the annulment of the contract and depending on the circumstances, PEMEX has the right and obligation to acquiring the vendor's nitrogen plant, under the terms of the contract.

Future estimated payments are as follows:

2008	Ps.	1,969,805
2009		1,695,836
2010		1,717,418
2011		1,721,866
2012		1,742,658
More than 5 years		9,466,799
Total	<u>Ps.</u>	<u>18,314,382</u>

- c. During 2003, 2004 and 2005, PEMEX entered into Financed Public Work Contracts ("FPWCs") (formerly known as Multiple Services Contracts or "MSCs"). In connection with these contracts, the contractor, at its own cost, has to administer and support the execution of the works in connection with the FPWCs, which are classified into categories of development, infrastructure and maintenance. The estimated value of the FPWCs as of December 31, is as follows:

<u>Date of Contract</u>	<u>Block</u>	<u>2007</u>	<u>2006</u>
February 9, 2004	Olmos	U.S. \$ 343,574	U.S. \$ 343,574
November 21, 2003	Cuervito	260,072	260,072
November 28, 2003	Misión	1,035,580	1,035,580
November 14, 2003	Reynosa-Monterrey	2,437,196	2,437,196
December 8, 2003	Fronterizo	264,977	264,977
December 9, 2004	Pandura-Anáhuac	900,392	900,392
March 23, 2005	Pirineo	645,295	645,295
April 3, 2007	Nejo	911,509	—
April 20, 2007	Monclava	433,501	—
Total		<u>U.S. \$ 7,232,096</u>	<u>U.S. \$ 5,887,086</u>

**PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005**
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

- d. PEMEX, through PMI, enters into sale contracts for crude oil with foreign companies in international markets. The terms and conditions of these contracts are specific to each customer, and the contract durations vary, including evergreen contracts and long term contracts.

NOTE 16 —CONTINGENCIES:

In the ordinary course of business, PEMEX is named in a number of lawsuits of various types. PEMEX evaluates the merit of each claim and assesses the likely outcome, accruing a contingent liability when an unfavorable decision is probable and the amount is reasonably estimable. Such contingent liabilities are discussed below.

- (a) PEMEX is subject to the provisions of the *Ley General del Equilibrio Ecológico y la Protección al Ambiente* (“General Law on Ecological Equilibrium and Environmental Protection”). To comply with this law, environmental audits of PEMEX’s larger operating, storage and transportation facilities have been or are being conducted. Following the completion of such audits, PEMEX has signed various agreements with the *Procuraduría Federal de Protección al Ambiente* (Federal Attorney of Environmental Protection, or “PROFEPA”) to implement environmental remediation and improve environmental plans. Such plans contemplate remediation for environmental damages, as well as related investments for the improvement of equipment, maintenance, labor and materials.
- As of December 31, 2007 and 2006, the reserve for environmental remediation expenses totaled Ps. 2,093,440 and Ps. 2,398,258, respectively. This reserve is included in long-term liabilities in the balance sheet.
- (b) As of December 31, 2007, PEMEX was involved in various civil, commercial, tax, criminal, administrative, labor and arbitration lawsuits. Based on the information available, the amount claimed in connection with these lawsuits totaled approximately Ps. 39,209,855. At December 31, 2007, PEMEX had accrued a reserve of Ps. 10,453,830 for these contingent liabilities. Among these lawsuits, are the following:
- i. Pemex-Refining is a party to an arbitration proceeding (No. 11760/KGA) filed by CONPROCA, S.A. de C.V. (“CONPROCA”) before the International Chamber of Commerce, in which CONPROCA is seeking payment of U.S.\$633,100 related to construction and maintenance services in the Cadereyta refinery. Pemex-Refining filed a counterclaim against CONPROCA in the amount of U.S.\$907,000 (which includes the value added tax).

The arbitration panel notified the parties that it will issue an award on this matter on March 31, 2008. As of the date of these financial statements, such award has not been issued. Once it is issued, a hearing on damages will be held.

 - ii. In April 2004, Construcciones Industriales del Golfo, S.A. de C.V. filed a civil claim against Pemex-Exploration and Production, (exp. 40/2004-VII), for a total amount of Ps. 15,237 plus U.S.\$219,584 for the removal of deposits in the Salamanca refinery. On September 28, 2007, a judgment was issued in favor of Pemex-Exploration and Production. The plaintiff filed an appeal against this judgment, which was denied on January 21, 2008. The plaintiff then filed a constitutional relief known as *amparo*, which is still pending.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

- iii. In December 2003, Unión de Sistemas Industriales, S. A. filed a civil claim against Pemex-Refining (exp. 202/2003), seeking Ps. 393,095. The trial is in the evidentiary stages; expert evidence is still pending.
- iv. In December 2004, Corporación Mexicana de Mantenimiento Integral S. de R. L. de C. V. (“COMMISA”) filed an arbitration claim before the International Court of Arbitration of the International Chamber of Commerce (the “ICA”) against Pemex-Exploration and Production (IPC-01) for breach of a construction agreement in connection with two platforms in the Cantarell complex.

On January 26, 2007, COMMISA filed a claim seeking U.S.\$292,043 and Ps. 37,537; and Pemex-Exploration and Production filed a counterclaim seeking U.S.\$125,897 and Ps. 41,513. On August 10, 2007, each party filed their responses to the claim and counterclaim, respectively. On September 10, 2007, both parties filed their replies, in which COMMISA modified its claim and is, as of the date of these financial statements, seeking U.S.\$319,900 and Ps. 37,200 in damages. On October 10, 2007, the parties filed their rejoinders. A hearing was held during which each party presented its case to the panel and filed its evidence. On February 15, 2008, the parties filed their pleadings.

The final award is expected to be issued before May 31, 2008 in accordance with a resolution issued by the ICA on February 14, 2008.

- v. An arbitration proceeding before the ICA was filed by COMBISA, S. de R. L. de C. V. (“COMBISA”) against Pemex-Exploration and Production (IPC-22) seeking U.S.\$235,770 for the alleged breach of a construction agreement in connection with three platforms in the Cantarell complex. Pemex-Exploration and Production responded to the claim and filed a counterclaim against COMBISA. On July 23, 2007, a final award was granted, pursuant to which COMBISA was ordered to pay U.S.\$4,600 and Pemex-Exploration and Production was ordered to pay U.S.\$61,300 as well as financial expenses and the corresponding value added tax. Both parties requested an additional decision to clarify this final award on November 16, 2007. The FCA modified the award such that total amount owed to COMBISA was corrected and Pemex-Exploration and Production was ordered to pay U.S.\$61,600 as well as financial expenses and the corresponding value added tax. The total amount owed to Pemex-Exploration and Production was ratified.

On January 30, 2008, Pemex-Exploration and Production and COMBISA executed a settlement agreement under which Pemex-Exploration and Production agreed to pay U.S.\$84,579 (plus the value added tax) and COMBISA agreed to pay U.S.\$4,594 plus the value added tax. This claim, which was initially for a total amount of U.S.\$235,770, concluded with a payment of U.S.\$91,983 to COMBISA.

- vi. COMMISA filed a claim before the ICA against Pemex-Exploration and Production (IPC-28) seeking approximately U.S.\$142,400 and Ps. 40,199 for, among other things, the alleged breach of a contract (PEP-O-IT-136/08) related to two vessels, the Bar Protector and Castoro 10, both of which are located in the Cantarell complex. Pemex-Exploration and Production filed a counterclaim. On February 11, 2008, Pemex-Exploration and Production was notified of an award pursuant which Pemex-Exploration and Production was ordered to pay Ps. 10,928 and U.S.\$75,075, plus the value added tax and U.S.\$200 related to arbitration expenses.

**PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005**
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

COMMISA filed a request to execute this award, which was notified to Pemex-Exploration and Production on March 24, 2008. As of the date of these financial statements, an answer to this request will be filed by Pemex-Exploration and Production.

- vii. A civil claim was filed by Asociación de Transportistas al Servicio de Petróleos Mexicanos Clientes o Empresas Sustitutos, A. C. against Pemex-Refining (exp. 262/2005-II) seeking approximately Ps. 1,647,629 for damages in connection with the alleged breach of a tank truck transportation agreement. On March 7, 2008 a final hearing was held in which both parites filed their allegations. A final judgement is still pending.
- viii. A civil claim was filed by Asociación de Transportistas al Servicio de Petróleos Mexicanos, Clientes o Empresas Sustitutos, A. C. against Pemex-Refining (exp. 271/2005-I) asserting that Pemex-Refining should authorize the plaintiff to replace tank trucks older than ten years in accordance with the tank truck transportation agreement mentioned in paragraph vii above. On January 23, 2008, a final hearing was held in which both parites filed their allegations. A final judgement is still pending.
- ix. A civil claim was filed by Asociación de Transportistas al Servicio de Petróleos Mexicanos, Clientes o Empresas Sustitutos, A. C. against Pemex-Refining, (295/2007), seeking a judicial judgment declaring the breach of a services agreement dated March 26, 1993 and damages, among other expenses.

On October 31, 2007, Pemex-Refining was summoned and a precautionary measure was granted to the plaintiff requesting Pemex-Refining to replace tank trucks and grant the appropriate authorizations. On November 5, 2007, Pemex-Refining filed a motion stating that the judge lacked jurisdiction, which was granted and the trial suspended. The resolution of this motion is still pending. A request for constitutional relief known as an *amparo* was filed by Pemex-Refining against the precautionary measure, which was accepted by the *Juzgado Quinto de Distrito en Materia Civil* ("Fifth Civil District Court").

- x. A request for Constitutional relief known as an *amparo* was filed by Minera Carbonífera Río Escondido, S.A. de C.V. and Minerales Monclova, S.A. de C.V. for alleged violation of its mining concessions and for the execution of development, infrastructure and maintenance works in non-associated gas fields under a public works contract (No. 414105826) and a modification of the *Ley Reglamentaria del Artículo 27 Constitucional en el Ramo del Petróleo* ("Regulatory Law to Article 27 of the Political Constitution Concerning Petroleum Affairs"). The purpose of this contract was to explore non-associated gas in the same fields where the plaintiffs have their mining concessions.

The plaintiffs argue they have a right to exploit gas found in the fields located under their mining concessions. As of the date of these financial statements, a final judgment is still pending. A third arbitrator expert's opinion on Geology and a constitutional hearing are still pending.

- xi. An arbitration proceeding before the ICA was filed by Tejas Gas de Toluca, S. de R.L. de C.V. against Gas Natural México S.A. de C.V. ("GNM") and Pemex-Gas and Basic Petrochemicals seeking, among other things, compliance with a transportation agreement and its amendments as agreed in February, 2001 and November, 2001. This agreement was executed for the operation of the Palmillas-Toluca pipeline.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

In February 2008, several hearings were held with the arbitration panel and the part involved, during which a summary of claims and counterclaims were presented. On February 26, 2008, the initial arbitration report was executed and a provisional arbitration calendar was agreed.

- xii. In connection with the claims filed by a group of Congressmen from the LIXth Legislature against Pemex-Exploration and Production related to the Financed Public Works Contracts program ("FPWC"), as of the date of these financial statements only one claim remains open since Pemex-Exploration and Production obtained a favorable judgement in the other similar claims filed by these plaintiffs.

The remaining claim relates to the FPWC entered into between Pemex-Exploration and Production and PTD Servicios Múltiples, S. de R.L. de C.V. ("PTD") for the Cuervito natural gas production block before the *Juzgado Noveno de Distrito en Materia Civil del Distrito Federal* ("Ninth Civil District Court") in Mexico City. On December 12, 2007, Pemex-Exploration and Production was summoned after an appeal filed by PTD was denied. Pemex-Exploration and Production filed a motion arguing the lack of capacity of the plaintiffs due to the termination of their positions as Congressmen. the trial is in the evidenciary stage.

- xiii. In August 2007, a civil claim (12/2007) was filed by Leoba Rueda Nava against Petróleos Mexicanos and Pemex-Refining. This claim was presented to the *Juzgado Decimocuarto de Distrito del Décimo Circuito* ("Fourteenth District Court of the Tenth Circuit") in Coatzacoalcos, Veracruz. Plaintiffs seek, among other things, civil liability and damages resulting from the pollution of land used to store oil waste in accordance with an agreement entered into by and among Leoba Rueda Nava, Petróleos Mexicanos and Pemex-Refining. The trial is in the evidenciary stage. Judicial inspection, confesional and testimonial evidences have been filed. As of the date of these financial statements expert opinions are still pending.
- xiv. Administrative proceedings were initiated by the Federal Competition Commission (the "Commission"). On December 7, 2007, the Commission issued a resolution prohibiting Pemex-Refining from engaging in anti-competitive practices in trading and distributing greases and lubricants in service stations, without specifically requesting a modification or termination of a license agreement. Pemex-Refining filed an *amparo* against this resolution, which is still pending.

In January 2008, the Commission requested Pemex-Refining to provide evidence related to the compliance of a resolution issued by the Commission in 2003 in connection with this same subject. Pemex-Refining informed the Commission that a suspension was granted to Bardahl de México, S. A. de C. V. ("Bardahl") in several *amparos* to maintain the exclusivity right of the Mexlub trademark until a final resolution was issued.

- xv. Several claims have been filed by Impulsora Jalisciense, S. A. de C. V. and Mexicana de Lubricantes, S. A. de C. V.

An *amparo* (1519/2005) was filed by Impulsora Jalisciense, S.A. de C.V., before the *Juzgado Quinto de Distrito en Materia Administrativa* ("Fifth Administrative District Court") in the State of Jalisco. This proceeding has been joined with a pending proceeding

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

filed by Bardahl against the execution of any resolutions lubricants manufactured by Bardahl.

These *amparos* are suspended due to several objections filed by Bardahl. A constitutional hearing is still pending.

- xvi. A civil claim (28/2007) was filed by Mexicana de Lubricantes, S. A. de C. V. against Pemex-Refining seeking, among other things, a judicial judgment declaring null and void any advance termination or cancellation of the following agreements executed between Mexicana de Lubricantes, S. A. de C. V. and Pemex-Refining: 1) License and Trademark contract; 2) Basic greases supply contract; and 3) Manufacture contract of lubricants and greases for Petróleos Mexicanos and the Subsidiary Entities. The claim was summoned and Pemex-Refining was required to file its response in April.

The result of these proceedings is uncertain since their final resolution will be issued by the appropriate authorities.

NOTE 17 —SEGMENT FINANCIAL INFORMATION:

PEMEX's primary business is the exploration and production of crude oil and natural gas and refining and marketing of petroleum products, conducted through four business segments: Pemex-Exploration and Production, Pemex-Refining, Pemex-Gas and Basic Petrochemicals and Pemex-Petrochemicals. Management makes decisions related to the operations of the consolidated business along these four strategic lines.

The primary sources of revenue for the segments are as described below:

- Pemex-Exploration and Production earns revenues from domestic crude oil sales, as well as from the export of crude oil, through PMI Group, to international markets. Export sales are made through PMI Group to approximately 25 major customers in various foreign markets. Less than half of PEMEX crude oil is sold domestically; however, these amounts are in large part sufficient to satisfy Mexican domestic demand.
- Pemex-Refining earns revenues from sales of refined petroleum products and derivatives. Most of Pemex-Refining's sales are to third parties and occur within the domestic market. The entity supplies the *Comisión Federal de Electricidad* ("CFE") with a significant portion of its fuel oil production. Pemex-Refining's most important products are different types of gasoline.
- Pemex-Gas and Basic Petrochemicals earns revenues primarily from domestic sources. Pemex-Gas and Basic Petrochemicals also consumes high levels of its own natural gas production. Most revenues of this entity are obtained from the sale of ethane and butane gas.
- Pemex-Petrochemical is engaged in the sale of petrochemical products to the domestic market. Pemex-Petrochemicals offers a wide range of products that generate large revenues, the majority of which come from methane derivatives, ethane derivatives and aromatics and derivatives.

In making performance analyses for the entities, PEMEX's management focuses on sales volumes and gross revenues as primary indicators of the performance analyses.

Income (loss) and identifiable assets for each segment have been determined before intersegment adjustments. Sales between segments are made at internal transfer prices established by PEMEX, which reflect international market prices.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Following is the condensed financial information of these segments:

	Exploration and Production		Gas and Basic Petrochemicals		Corporate and Subsidiary Companies		Intersegment Eliminations		Total	
Year ended December 31, 2007										
Sales —										
Trade	Ps.	-	Ps.	139,963,302	Ps.	21,701,729	Ps.	542,926,858	Ps.	1,134,974,819
Intersegment		912,295,482		82,940,711		35,942,074		247,993,773		—
Services income		—		—		—		1,880,032	(1,321,401,568)	1,060,609
Total net sales		912,295,482		222,904,013		57,643,803		792,800,663	(1,322,220,991)	1,136,035,428
Gross income		740,811,644		15,816,747		(6,559,693)		41,180,144	(34,854,648)	675,369,686
Operating income (loss)		707,401,828		7,335,910		(14,115,424)		5,850,043	(1,734,890)	590,430,682
Comprehensive financing cost		(25,561,647)		1,071,281		(1,181,167)		10,097,224	1,292,274	(20,046,587)
Net income (loss)		19,966,387		4,958,173		(16,085,945)		(11,473,248)	29,980,683	(18,307,569)
Depreciation and amortization		57,262,960		10,159,674		3,437,370		1,091,848	639,866	72,591,718
Labor cost reserve		29,124,816		6,491,464		8,215,002		12,896,453	—	85,306,866
Taxes and duties		663,549,438		3,846,738		257,203		4,064,958	—	677,255,728
Acquisition of fixed assets		99,252,970		5,871,320		998,725		324,582	—	129,359,898
Total assets		1,237,968,403		133,970,702		79,872,062		2,331,376,672	(2,870,300,731)	1,330,280,606
Current assets		630,760,334		85,311,492		58,650,943		495,164,854	(1,070,863,531)	428,560,787
Investments in shares		342,538		157,094		—		612,696,004	(581,227,948)	33,063,354
Fixed assets		565,433,958		42,005,574		15,569,956		8,250,144	—	793,845,453
Current liabilities		191,867,210		33,463,623		8,896,698		929,478,616	(1,022,952,043)	289,463,852
Labor reserve		180,931,471		40,791,151		49,058,100		79,033,180	—	528,201,272
Total liability		998,713,758		85,452,634		59,275,500		2,262,119,197	(2,502,496,731)	1,280,372,745
Equity		239,254,644		48,518,068		20,596,562		69,257,475	(367,804,000)	49,907,861
Year ended December 31, 2006										
Sales —										
Trade	Ps.	-	Ps.	138,687,862	Ps.	21,638,776	Ps.	535,144,047	Ps.	1,102,433,921
Intersegment		890,012,141		46,242,429		83,058,212		171,981,054	(1,200,948,230)	—
Services income		—		—		—		1,707,386	(631,439)	1,075,947
Total net sales		890,012,141		221,746,074		31,293,170		708,832,487	(1,201,579,669)	1,103,509,868
Gross income		718,463,139		18,030,329		(4,925,440)		31,717,998	(25,840,484)	685,251,658
Operating income (loss)		690,607,335		10,720,768		(11,854,541)		(1,720,065)	(565,837)	604,277,229
Comprehensive financing cost		(24,174,018)		1,134,603		(4,173,330)		12,659,001	(266,662)	(23,846,625)
Net income (loss)		75,888,386		6,311,661		(18,029,704)		54,656,089	(36,547,837)	46,953,205
Depreciation and amortization		51,819,623		3,529,726		902,845		696,602	—	65,672,189
Labor cost reserve		25,562,500		5,637,100		6,972,400		11,546,149	—	74,493,349
Taxes and duties		591,866,238		4,703,707		394,529		4,634,622	—	604,764,509
Acquisition of fixed assets		61,906,641		5,132,529		1,712,598		15,667,903	—	97,650,767
Total assets		1,096,349,650		133,753,202		72,279,723		2,038,713,342	(2,447,984,895)	1,250,020,424
Current assets		533,417,998		84,553,543		50,300,628		457,242,716	(899,414,425)	399,393,196
Investments in shares		330,752		1,967,913		—		491,078,954	(460,773,767)	32,760,946
Fixed assets		514,467,528		41,253,162		15,908,016		8,628,831	—	737,195,457
Current liabilities		84,578,731		38,595,497		11,677,253		787,977,256	(860,383,856)	176,314,129
Labor reserve		162,516,165		36,305,067		43,602,148		68,740,031	—	471,665,183
Total liability		805,563,141		84,445,277		55,768,854		1,984,483,183	(2,043,900,288)	1,208,564,798
Equity		290,786,509		49,307,958		16,510,869		54,230,161	(404,084,641)	41,455,626
Year ended December 31, 2005										
Sales —										
Trade	Ps.	-	Ps.	144,987,328	Ps.	21,826,900	Ps.	454,436,655	Ps.	1,002,606,265
Intersegment		773,336,701		89,170,404		9,518,438		131,997,076	(1,045,330,294)	—
Services income		—		—		—		1,875,001	(650,193)	1,224,808
Total net sales		773,336,701		234,157,732		31,345,338		588,308,732	(1,045,980,487)	1,003,831,073
Gross income		594,226,368		20,740,515		(5,601,679)		7,885,280	(6,451,743)	613,887,174
Operating income (loss)		567,556,903		10,678,648		(9,781,605)		(20,166,208)	20,317,888	539,703,380
Comprehensive financing cost		8,683,177		2,598,710		(3,550,361)		(13,145,650)	4,437,455	(4,836,091)
Net income (loss)		(19,701,797)		7,213,898		(17,851,654)		(76,533,529)	82,024,014	(82,357,982)
Depreciation and amortization		42,648,709		3,857,966		1,075,044		750,720	—	56,995,357
Labor cost reserve		22,739,043		4,782,355		5,742,055		9,336,373	—	63,667,038
Taxes and duties		595,838,203		2,412,419		262,157		3,917,966	—	626,874,462
Acquisition of fixed assets		29,498,613		1,936,748		2,511,707		43,829,686	—	84,314,567
Total assets		910,762,474		104,721,683		55,842,991		1,624,736,468	(1,890,886,536)	1,125,596,261
Current assets		379,304,272		56,041,394		33,282,845		429,691,461	(721,191,173)	316,080,435
Investments in shares		227,313		1,276,801		—		231,359,791	(204,339,923)	28,681,076
Fixed assets		475,493,308		40,924,037		15,850,726		9,340,494	—	694,467,196
Current liabilities		123,657,961		21,971,433		53,748,694		554,475,788	(690,761,619)	177,582,783
Labor reserve		142,000,010		30,508,286		36,672,374		58,796,102	—	405,583,808
Total liability		747,717,710		59,003,711		90,957,975		1,639,794,045	(1,686,540,129)	1,154,606,227
Equity		163,044,885		45,717,987		(35,114,975)		(15,057,361)	(204,346,661)	(29,009,817)

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 18 — FISCAL REGIME:

On December 21, 2005, the Mexican Congress approved a new fiscal regime for PEMEX, which was published in the Official Gazette of the Federation, effective January 1, 2006.

Under this new fiscal regime, PEMEX's contributions remain established by the *Ley Federal de Derechos* ("Federal Duties Law"), except for the Excess Gain Duties (Crude Oil Gain Tax), which is established by the Federal Income Law. The fiscal regime for PEMEX applicable for 2006 and 2007 contemplated the following duties:

a. The Ordinary Hydrocarbons Duty — In 2006 and 2007, this duty applied a variable rate that depended on the price of Mexican crude oil for export. In 2006 and 2007, the rate ranged from 78.68% to 87.81% (depending on the price of Mexican crude oil).

The method of calculating this duty is the value of the extracted total production of crude oil and natural gas during the year minus certain permitted deductions (including investments, plus some costs, expenses and duties). During 2007, PEMEX made daily and weekly advance payments to the account of this duty, in the amount of Ps. 464,837,848 (Ps. 231,326,765 daily and Ps. 233,511,083 weekly). During 2006, PEMEX made daily and weekly advance payments to the account of this duty, in the amount of Ps. 541,916,001 (Ps. 269,596,338 daily and Ps. 272,319,663 weekly).

b. Hydrocarbon Duty for the Oil Revenues Stabilization Fund — This duty was applied at a rate between 1% and 10% of the value of the extracted crude oil production where the yearly weighted average crude oil export price for a certain year exceeds between U.S.\$22.00 and U.S.\$30.00 per barrel.

c. Extraordinary Duty on Crude Oil Exports — This duty was applied at a rate of 13.1% on the difference between the value realized for crude oil exports and the budgeted crude oil price of U.S.\$42.80, times the annual export volume. This duty is to be credited against the Hydrocarbon Duty for the Oil Revenues Stabilization Fund. The income from this duty is designated to the states of Mexico via the Income of the Federative Entities Stabilization Fund.

d. Excess Gains Revenue Duty — This duty was derogated in 2007, however during 2006, applied a rate of 6.5% to the difference between the realized value and the budgeted value of crude oil exports of U.S.\$36.50. This duty is to be credited against the Hydrocarbon Duty to Fund Stabilization and, where necessary, against the Ordinary Hydrocarbon Duty.

e. Duty for the Fund for Scientific and Technological Research on Energy — This duty was applied at a rate of 0.05% to the value of the extracted production of crude oil and natural gas for the year. The revenues from this tax are designated for the *Instituto Mexicano del Petróleo* ("Mexican Petroleum Institute") in accordance with the *Presupuesto de Egresos de la Federación* ("Federal Expenditure Budget").

f. Duty for the Fiscal Monitoring of Oil Activities — This duty was applied at a rate of 0.003% to the value of extracted production of crude oil and natural gas for the year. The revenues from this tax are designated for the *Auditoria Superior de la Federación* ("Supreme Federal Audit") in accordance with the Federal Expenditure Budget.

g. Additional Duty — This duty is applied if the actual production of crude oil in the years 2006, 2007 and 2008 is less than the target production, but only when the shortfall is not by reason of force majeure, act of god or energy policy.

h. Special Tax on Production and Services — In accordance with the regulations in effect, PEMEX is subject to the Special Tax on Production and Services ("IEPS"), which applies to the import and sale of

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

gasoline and diesel. The IEPS is paid to SHCP monthly, after deducting the daily advance payments. The rates applicable to this tax depend on factors such as the type of product, price of reference, the region where one sells, additional freight and applicable commissions.

In 2005, increase in international prices of hydrocarbons and petroleum products caused the rate of the IEPS tax to be negative, which was absorbed by PEMEX. On January 1, 2006, the Federal Revenue Law was amended, allowing to PEMEX to credit the negative IEPS against other taxes and payments to which PEMEX is also subject. As a result of this PEMEX recognized in 2007 and 2006 revenue of approximately Ps. 72,137,000 and Ps. 57,330,998 (Ps. 55,256,000 nominal value), respectively, presented in the consolidated statement of operations within "Other revenues". As of December 31, 2007, there was a negative balance of IEPS tax credit of Ps. 32,943,613 (see Note 6).

i. Hydrocarbon Income Tax ("IRP") — This tax is calculated by applying a 30% rate on the excess of the total revenues minus the authorized deductions pursuant to the specific rules expressed by the SHCP.

For the years ended December 31, 2007 and 2006 PEMEX generated an IRP as follows:

	<u>2007</u>	<u>2006</u>
Current IRP	Ps. 4,070,364	Ps. 3,705,184
Deferred IRP	1,867,292	1,031,619
	5,937,656	4,736,803
Inflation effect	92,711	178,056
Total IRP	<u>Ps. 6,030,367</u>	<u>Ps. 4,914,859</u>

In accordance with Article 7 of the Federal Revenue Law from January 1, 2007, Petróleos Mexicanos and the Subsidiary Entities, except Pemex-Exploration and Production, were required to make daily payments (including non-working days) of Ps. 3,314 to the account of the IRP during the fiscal year. On the first working day of every week of the fiscal year, PEMEX would have to pay Ps. 23,262. Through December 31, 2007, the daily and weekly payments made to the Federal Treasury totaled Ps. 2,442,496. As of December 31, 2007, Pemex has caused Ps. 3,431,142 of IRP.

The principal concepts that cause the deferred IRP are the following:

	<u>2007</u>	<u>2006</u>
Deferred asset IRP:		
Advance from customers	Ps. 491,424	Ps. 518,388
Provision for insurance	94,892	115,176
Provision for contingencies	19,918	11,831
Environmental reserve	63,508	85,255
Allowance for uncollectible	8,899	9,870
	678,641	740,520
Deferred liability IRP:		
Advance insurance	(2,692)	(7,314)
Properties, plants and properties	(5,552,588)	(3,855,675)
	(5,555,280)	(3,862,989)
Long term liability	<u>(Ps. 4,876,639)</u>	<u>(Ps. 3,122,469)</u>

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

j. Value Added Tax — For purposes of determining the Value Added Tax (“VAT”), PEMEX follows the criterion for excluding only the interests paid for institutions of credit and credit unions in accordance with the fraction V of the article 15 of the Regulation of Value Added Tax.

k. Income and Assets Taxes — Certain Subsidiary Companies are subject to the income tax law and the assets tax law.

For the years ended December 31, 2007, 2006 and 2005, the Subsidiary Companies incurred the following income tax:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Current income tax	Ps. 3,253,655	Ps. 4,771,281	Ps. 3,487,273
Deferred income tax	(27,414)	(166,237)	494,405
	<u>Ps. 3,226,241</u>	<u>Ps. 4,605,044</u>	<u>Ps. 3,981,678</u>

The principal concepts that cause the Deferred Income Taxes are the following:

	<u>2007</u>	<u>2006</u>
Deferred asset income taxes:		
Losses of prior years	Ps. 653	Ps. 8,359
Deferred liability income taxes:		
Properties, plants and equipment	(1,535,911)	(1,483,062)
Long term liability	<u>(Ps. 1,535,258)</u>	<u>(Ps. 1,474,703)</u>

On October 1, 2007, a modification to the Federal Duties Law was published in the Official Gazette of the Federation. Effective January 1, 2008, the fiscal regime applicable to Pemex-Exploration and Production was modified.

NOTE 19 —NEW ACCOUNTING PRONOUNCEMENTS

The CINIF has issued the following FRS, effective for years beginning after December 31, 2007, and which do not provide for earlier application:

- (a) **FRS B-10 “Effects of inflation”** — FRS B-10 supersedes Bulletin B-10 and its five amendments, as well as the related circulars and INIF. The principal guidelines established by this FRS are:
- (i) The use of *unidades de inversión* (“UDIs”) to determine the inflation for a given period;
 - (ii) the elimination of inventory replacement costs as well as specific indexation for fixed assets,
 - (iii) the requirement to recognize the effects of inflation only when operating in an inflationary economic environment (accumulated inflation equal to or higher than 26% in the most recent three-year period); and
 - (iv) reclassification of the accounts of gain or loss from holding non-monetary assets (“RETANM”), monetary position gains or losses (“REPOMO”), and deficit/excess in equity restatement, to retained earnings, when the unrealized portion is not identified.

Management estimates that the initial effects of this new FRS will be a charge to retained earnings and a credit to surplus in the restatement of equity in the amount of Ps. 178,171,999, and will have no effect on assets, liabilities, equity or net income.

- (b) **FRS D-3 “Employee benefits”** — FRS supersedes Bulletin D-3, the portion applicable to Employee Statutory Profit Sharing (“ESPS”) of Bulletin D-4 and INIF. The principal guidelines

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

established by this FRS are: (i) a maximum of five years for amortizing unrecognized/unamortized items, with the option to recognize immediately actuarial gains or losses in results of operations; (ii) the elimination of the recognition of an additional liability and related intangible asset and any related item as a separate element of equity; (iii) the inclusion severance benefits in results of operations; and (iv) the presentation of ESPS, including deferred ESPS, in the statement of income as ordinary operations. Additionally, FRS D-3 establishes that the asset and liability method required by FRS D-4 should be used for determining deferred ESPS, and that any effects arising from the change are to be recognized in retained earnings, with no restatement of prior years' financial statements.

As of date of these financial statements, management is still in the process of determining the initial effects of this new FRS.

- (c) **FRS D-4 "Tax on earnings"** — FRS supersedes Bulletin D-4 and Circulars 53 and 54. The principal guidelines established by this FRS are: (i) the reclassification of the cumulative income taxes effects resulting from the initial adoption of Bulletin D-4 in 2000 to retained earnings; (ii) the recognition of the *Impuesto al Activo* ("IMPAC") as a tax credit (benefit), rather than as a tax prepayment; and (iii) the transfer of accounting treatment of ESPS incurred and deferred to FRS D-3, as discussed in paragraph (b) above.

Management estimates that the initial effects of this new FRS will not be material.

- (d) **FRS B-2 "Statement of cash flows"** — FRS supersedes Bulletin B-12 and paragraph 33 of Bulletin B-16. The principal guidelines established by this FRS are: (i) the replacement of the statement of changes in financial position with the statement of cash flows; (ii) the reporting of cash inflows and cash outflows in nominal currency units *i.e.* the effects of inflation are not included; (iii) the establishment of two alternative preparation methods (direct and indirect), without stating preference for either method. In addition, cash flows from operating activities are to be reported first, followed by cash flows from investing activities and finally, cash flows from financing activities; (iv) the reporting of captions of principal items as gross; and (v) the requirement of disclosure of the composition of those items considered cash equivalents.
- (e) **FRS B-15 "Translation of foreign currencies"** — FRS B-15 supersedes Bulletin B-15. The principal guidelines established by this FRS are: (i) the substitution of the integrated foreign operation and foreign entity concepts for determining recording currency, functional currency and reporting currency, requiring that translation be made based on the economic environment in which the entity operates, regardless of its dependency on the holding company; and (ii) the inclusion of translation procedures for those instances where the reporting currency is different from the functional currency.

NOTE 20 —SUBSEQUENT EVENTS:

On April 11, 2008, the average price of the crude oil for exportation was of U.S.\$91.84 per barrel; this price increased by approximately 11.4% as compared to the average price as of December 28, 2007 which was U.S.\$82.44 per barrel.

On April 11, 2008, the exchange rate was Ps. 10.5503 per dollar, which is 2.1% less than the exchange rate as of December 31, 2007, which was Ps.10.8662.

On April 8, 2008, the Mexican President sent to the Mexican Congress an Energy Reform Initiative.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The Energy Reform includes five fundamental initiatives:

- A new Organic Law for Petróleos Mexicanos.
- Modifications to the Organic Law of the Public Federal Administration.
- Creation of an oil commission, which would be decentralized entity under the *Secretaría de Energía* (Energy Ministry or “SENER”), with technical and operative autonomy.
- Extensive modifications to the *Ley Reglamentaria*, (“Regulatory Law”).
- Extensive modifications to the *Ley de la Comisión Reguladora de Energía* (“Law of the Regulatory Commission of Energy”).

NOTE 21—DIFFERENCES BETWEEN MEXICAN FRS AND U.S. GAAP

PEMEX’s consolidated financial statements are prepared in accordance with Mexican FRS, which differs in certain significant respects from accounting principles generally accepted in the United States (“U.S. GAAP”). In accordance with Bulletin B-10, as discussed in Note 3a. to the financial statements, all of the related U.S. GAAP adjustments have also been restated to reflect the effects of inflation. The application of Bulletin B-10 represents a comprehensive measure of the effects of price level changes and is considered to result in a more meaningful presentation than historical cost-based financial reporting in an environment such as Mexico. None of the adjustments to the financial statements for the effects of inflation required under Mexican FRS have been eliminated in the U.S. GAAP reconciliation.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The differences between Mexican FRS and U.S. GAAP, as they relate to PEMEX, are presented below together with explanations of certain adjustments that affect net income and shareholders' equity as of and for the years ended December 31, 2007, 2006 and 2005:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Net (loss) income for the year under Mexican FRS	(Ps. 18,307,569)	Ps. 46,953,205	(Ps. 82,357,982)
U.S. GAAP adjustments:			
Exploration and drilling costs, net (a)	(1,370,873)	(1,498,801)	(1,549,819)
Pensions and seniority premiums (b)	2,328,436	1,939,725	1,012,457
Post-retirement benefits (c)	4,025,557	5,042,554	3,375,220
Accrued vacation (d)	(45,809)	(20,549)	(16,712)
Fixed asset adjustments:			
Capitalized gains (losses) of derivative financial instruments, net (e)	(177,334)	3,928,429	(8,445,996)
Capitalization of interest, net (f)	3,509,960	2,794,394	1,928,272
Impairment, net (g)	3,344,517	3,978,566	6,246,987
Depreciation convention (h)	783,144	783,144	783,144
Derivative financial instruments (i)	(8,149,706)	74,673	1,030,873
Profit in inventory (j)	(18,919,219)	(4,156,613)	(2,776,119)
Available-for-sale investment securities (l)	246,258	(2,995,342)	(830,179)
Effects of inflation accounting on U.S. GAAP adjustments (m)	159,139	28,627	206,880
Deferred income taxes (n)	(62,488)	(74,777)	442,668
Reclassification of Pemex Finance net income to minority interest (o)	(6,089)	(54,789)	1,159,233
Total U.S. GAAP adjustments, net	(14,334,507)	9,769,241	2,566,909
Net (loss) income for the year under U.S. GAAP	(Ps. 32,642,076)	Ps. 56,722,446	(Ps. 79,791,073)
Comprehensive (loss) income under U.S. GAAP:			
Net (loss) income for the year under U.S. GAAP	(Ps. 32,642,076)	Ps. 56,722,446	(Ps. 79,791,073)
Other comprehensive (loss) income:			
Additional minimum pension liability(b) ⁽¹⁾	(3,793,689)	(20,311,938)	(19,692,549)
Derivative financial instruments (i)	656,699	5,274,109	(4,930,806)
Unrealized gains on available-for-sale investment securities (l)	(246,258)	2,995,342	830,179
Surplus in restatement of equity	18,539,917	4,108,268	5,571,542
Other	—	710,094	—
Comprehensive (loss) income	(Ps. 17,485,407)	Ps. 49,498,321	(Ps. 98,012,707)

(1) This line item previously reported the amount of (Ps. 168,399,229), which included the amount related to recognition of the initial effect of SFAS 158 in 2007 of Ps. 164,605,540. PEMEX corrected this amount by removing it from Other comprehensive (loss) income—Additional minimum pension liability and presenting it as a direct entry to Accumulated other comprehensive loss.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

	2007	2006
Components of accumulated other comprehensive (loss) income at December 31:		
Derivative financial instruments (i)	(Ps. 1,105,629)	(Ps. 1,762,328)
Additional minimum pension liability (b) ⁽¹⁾	(46,693,813)	(42,900,124)
Recognition of initial effect of SFAS 158 (b) ⁽¹⁾	(164,605,540)	—
Unrealized gains on available-for-sale investment securities (l)	12,716,759	12,963,017
Surplus in restatement of equity	175,864,184	157,324,267
Other	710,094	710,094
Accumulated other comprehensive (loss) income	(Ps. 23,113,945)	Ps. 126,334,926
	2007	2006
Equity is reconciled as follows:		
Equity under Mexican FRS	Ps. 49,907,861	Ps. 41,455,626
U.S. GAAP adjustments:		
Exploration and drilling costs (a)	12,518,420	13,889,293
Pensions and seniority premiums:		
Pensions and seniority premiums (b)	(5,546,942)	(7,875,378)
Additional minimum pension liability (b)	(67,715,653)	5,426,624
Post-retirement benefits:		
Post-retirement benefits (c)	(34,187,352)	(38,212,908)
Effect in equity of labor obligation (c)	(91,824,161)	—
Accrued vacation (d)	(636,092)	(590,283)
Fixed asset adjustments:		
Capitalized gains of hedging financial instruments, net (e)	2,883,974	3,061,308
Capitalization of interest, net (f)	(4,782,607)	(8,292,567)
Impairment, net (g)	(26,564,246)	(29,908,763)
Depreciation convention (h)	—	(783,144)
Derivative financial instruments (i)	—	8,149,706
Profit in inventory (j)	(26,755,771)	(7,836,552)
Advanced payments on minimum guaranteed dividend (k)	(4,270,225)	(268,990)
Deferred income taxes (n)	305,403	367,891
Reclassification of Pemex Finance equity to minority interest (o)	(1,415,775)	(1,464,681)
Total U.S. GAAP adjustments, net	(247,991,027)	(64,338,444)
Deficit under U.S. GAAP	(Ps. 198,083,166)	(Ps. 22,882,818)

(1) Additional minimum pension liability, which was previously reported in the amount of Ps. 211,299,353, was corrected to separately disclose the Recognition of the initial effect of SFAS 158 in the amount of Ps. 164,605,540 and the Additional minimum pension liability in the amount of Ps. 46,693,813.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

	2007	2006
Changes in U.S. GAAP equity for the year ended December 31:		
Deficit at January 1	(Ps. 22,882,818)	(Ps. 120,942,611)
Net (loss) income for the period	(32,642,076)	56,722,446
Mexican Government increase in equity of Subsidiary Entities	11,160,824	48,727,913
Minimum guaranteed dividends	(4,270,225)	(166,440)
Accumulated other comprehensive loss: ⁽¹⁾		
Recognition of initial effect of SFAS 158	(164,605,540)	—
Other comprehensive (loss) income:		
Additional minimum pension liability (b) ⁽¹⁾	(3,793,689)	(20,311,936)
Derivative financial instruments (i)	656,699	5,274,109
Unrealized gains on available-for-sale investment securities (l)	(246,258)	2,995,342
Surplus in restatement of equity	18,539,917	4,108,265
Other	—	710,094
Deficit at December 31	(Ps. 198,083,166)	(Ps. 22,882,818)

(1) Other comprehensive (loss) income—Additional minimum pension liability, previously reported in the amount of Ps. 168,399,299, included the Recognition of initial effect of SFAS 158 in the amount of Ps. 164,605,540. PEMEX corrected the presentation of the Recognition of the initial effect of SFAS 158 as a direct entry to Accumulated other comprehensive loss.

I. Explanation of reconciling items:

(a) Exploration and drilling costs

Effective January 1, 2004, for Mexican FRS purposes, PEMEX changed its accounting policy for the recognition of well exploration and drilling costs to the successful-efforts method of accounting. The change in accounting policy for recording well exploration and drilling expenses had no effect on our consolidated financial statements.

Under U.S. GAAP, PEMEX follows the successful-efforts method of accounting by which costs of drilling exploratory wells and exploratory-type stratigraphic test wells are initially capitalized and are later charged to expenses if proved reserves are not discovered. Development costs, including the costs of drilling development wells and development-type stratigraphic test wells, are capitalized. The capitalized costs of wells and related equipment are amortized on a UOP basis over proved developed reserves, as the related oil and gas reserves are extracted.

Consequently, at December 31, 2007 and 2006, the U.S. GAAP equity adjustment represented the cumulative costs of capitalized unsuccessful wells in proven areas under U.S. GAAP, not capitalized under Mexican FRS through December 31, 2003, net of the amortization of such capitalized amounts. The 2007, 2006 and 2005 U.S. GAAP net income adjustment reflects the amortization of such capitalized costs on a UOP basis.

In April 2005, the Financial Accounting Standards Board (“FASB”) issued a FASB Staff Position No. SFAS 19-1 “Accounting for Suspended Well Costs” (“FSP 19-1”). FSP 19-1 addresses the circumstances that would permit the continued capitalization of exploratory well costs beyond one year, other than when additional exploration wells are necessary to justify major capital expenditures and drilling of those wells is

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

under way or firmly planned for the near future. Under the provisions of FSP 19-1, exploration costs would continue to be capitalized after the completion of drilling when (a) the well has found a sufficient quantity of reserves to justify completion as a producing well and (b) the enterprise is making sufficient progress assessing the reserves and the economic and operating viability of the project. If either condition is not met, or if an enterprise obtains information that raises substantial doubt about the economic or operational viability of the project, the exploratory well would be assumed to be impaired, and its costs, net of any salvage value, would be charged to expenses. FSP 19-1 provides a number of indicators that need to be present to demonstrate that sufficient progress has been made in assessing the reserves and the economic viability of the project.

PEMEX's policy is to determine whether or not exploratory well costs are capitalized or expensed shortly after completion of drilling. As such, PEMEX does not have significant suspended well costs for the three years ended December 31, 2007. No capitalized exploratory well costs have been charged to expenses since the adoption of FSP 19-1.

(b) Pensions and seniority premiums

Under Mexican FRS, PEMEX follows Bulletin D-3, which establishes the procedures for measuring the expenses and liabilities for pension plans, seniority premiums and severance payments. The main differences between PEMEX's application of Bulletin D-3 and the U.S. GAAP guidance provided in Statement of Financial Accounting Standards ("SFAS") No. 87, "Employers' Accounting for Pensions" ("SFAS No. 87"), are the implementation dates (including the measurement date for benefit obligations, amortization of past liabilities and recognition of gain and losses).

On September 30, 2006, the FASB approved substantial amendments to SFAS 87, 88, 106 and 132, through the issuance of SFAS 158—"Employers' Accounting for Defined Benefit Pension and other Post-retirement Plans and Amendment of FASB Statements 87, 88, 106 and 132(R)," which proposed a new methodology for the recognition of labor liabilities in companies' financial statements.

The principal changes included in SFAS 158 do not affect the methodology for determining the charge to income during the year (net periodic pension cost), but only their recognition in the balance sheet. Changes in SFAS 158 include: (i) a shift in the minimum amount to be recognized as a liability in the balance sheet, from Accumulated Benefit Obligation (ABO) to Projected Benefit Obligation (PBO); (ii) recognition of the total outstanding items to write off as a direct impact on the affected property (Accumulated Other Comprehensive Income Loss or "AOCI"); (iii) recognition of asset effect; and (iv) disclosure in the balance sheet of noncurrent assets, current liabilities and noncurrent liabilities.

PEMEX recognized SFAS No. 158, effective January 1, 2007, and included its effects in the results of the actuarial valuation of its labor obligations.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The differences between Bulletin D-3 and SFAS 158 are summarized as follows:

<u>Item</u>	<u>Bulletin D-3</u>	<u>SFAS 158</u>
Net Periodic Cost	No difference	No difference
Minimum liability to be recognized	Accumulated Benefit Obligations (ABO)	Projected Benefit Obligations (PBO) Recognize the total outstanding items as a component of the Accumulated other comprehensive loss/income (AOCI); for retirement and post-retirement benefits, as an adjustment to equity
Items not amortized unrecognized (actuarial gains/losses, prior service, plan amendments and transition obligation).	Recognized as components of net periodic cost based on the employees' average working lifetime. Difference between ABO and plan assets	N/A
Unfunded ABO	Difference between unfunded ABO and net projected liability	N/A
Recognition of additional minimum liability		In the year of recognition of actuarial gain/losses and past service costs/credits, there is also a write off of an equivalent amount in other comprehensive income (OCI) SFAS 158, paragraph 4(d)
Recognition of intangible asset and other comprehensive income	Offsetting account of additional liability	
Disclosure in the balance sheet of noncurrent assets, current liabilities and noncurrent liabilities	N/A	Required (for retirement and post-retirement benefits)

(c) Post-retirement benefits

Under U.S. GAAP, PEMEX follows the guidelines of SFAS No. 106, "Employers' Accounting for Post-retirement Benefits Other than Pensions" ("SFAS No. 106") in accounting for health service and other supplemental payments provided to retirees and other eligible family members. SFAS No. 106 requires the accrual of the expected cost of providing such benefits during retirement.

Effective January 1, 2007, PEMEX recognized SFAS No. 158, "Employer's Accounting for Defined Benefit Pension and Other Post-retirement Plans." This statement requires an employer to recognize the funded status of a defined benefit post-retirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income of a business entity. This statement also requires an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions.

The recognition of SFAS 158 for post-retirement benefit plans results in the same differences between Bulletin D-3 and SFAS 158 as those related to pensions and seniority premiums (see Note 21I.(b)).

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(d) Accrued vacation

Under Mexican FRS, vacation expense is recognized when the vacation is utilized by the employee. Under U.S. GAAP, vacation expense is accrued based on when it is earned by the employee.

(e) Fixed assets—Capitalized gains and losses of derivative financial instruments

Under Mexican FRS, finance costs related to loans allocated to construction projects are capitalized as part of capitalized interest, and are included net of gains and losses arising from derivative financial instruments designated as hedges.

Under U.S. GAAP, gains and losses arising from financial instruments designated as cash flow hedges cannot be capitalized as part of qualifying assets. These amounts are accumulated in other comprehensive income and are reclassified into earnings over the life of the assets the hedged transaction relates to. For the years ended December 31, 2007, 2006 and 2005, the capitalized (loss) gain adjustments in the reconciliation were Ps. (19,439), Ps. 3,929,158 and Ps. (8,120,773), respectively, arising from hedging instruments.

The 2007, 2006 and 2005 net income adjustments also include a reversal of depreciation of Ps. (157,895), Ps. (729) and Ps. (325,223), respectively, related to amounts previously capitalized.

(f) Fixed assets—Capitalization of interest

Effective January 1, 2007, Pemex adopted FRS D-6 “Capitalization of Comprehensive Financing Result,” which establishes the rules that must be observed in the capitalization of the Comprehensive Financing Result attributable to certain assets whose acquisition required a substantial period (prolonged) before their intended use.

The capitalized comprehensive financing result is composed of the cost of interest, the foreign exchange effect, the result in monetary position and other costs associated with obtaining financing identified with qualifying assets, which directly affect the investment cost during the acquisition period.

Under U.S. GAAP, interest is capitalized by applying an average interest rate to the average amount of accumulated expenditures for the qualifying asset during the period. PEMEX has accordingly adjusted its results of operations and equity to reflect the U.S. GAAP requirements for capitalizing interest.

Interest costs for the years ended December 31, 2007, 2006 and 2005, for Mexican FRS and U.S. GAAP purposes were allocated as follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Under Mexican FRS:			
Interest capitalized	Ps. 5,350,849	Ps. 6,996,305	Ps. 5,540,983
Interest expense	57,847,569	46,099,472	57,146,232
Total interest cost	<u>Ps. 63,198,418</u>	<u>Ps. 53,095,777</u>	<u>Ps. 62,687,215</u>
Under U.S. GAAP:			
Interest capitalized	Ps. 7,797,815	Ps. 8,659,013	Ps. 6,321,963
Interest expense	55,400,603	44,436,764	56,365,252
Total interest cost	<u>Ps. 63,198,418</u>	<u>Ps. 53,095,777</u>	<u>Ps. 62,687,215</u>

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

In addition, the net income adjustment for capitalized interest presented herein also includes the reversal of depreciation of Ps. 1,062,994, Ps. 1,131,686, and Ps. 1,147,292 for the years ended December 31, 2007, 2006 and 2005, respectively, related to the cumulative difference in amounts previously capitalized for such assets because the cumulative amounts capitalized under Mexican FRS have exceeded those amounts under U.S. GAAP.

(g) Fixed assets—Impairment

For Mexican FRS purposes, as described in Note 3j, PEMEX evaluates the impairment of long-lived assets whenever there are events or circumstances indicating that the book value of a given asset may not be recoverable under Bulletin C-15.

For each of the cash-generating units, if the book value of the long-lived assets exceeds the estimated future value (discounted) of cash flows recoverable by such long-lived assets, a charge is made to income for the period for an impairment loss. PEMEX performs this calculation at least annually. In accordance with Bulletin C-15, the impairment recorded can be reversed in subsequent periods if the subsequent impairment analysis does not indicate a loss in such future periods.

For U.S. GAAP purposes, an evaluation of impairment is undertaken whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable, as is the case under Mexican FRS. However, under U.S. GAAP, the impairment criteria are met when the carrying value of assets exceeds the sum of expected future cash flows (undiscounted and without financing charges) of the related assets. The asset is written down to fair value as determined by using the present value of expected future cash flows. U.S. GAAP does not allow for reversal of losses; PEMEX measures impairment of its oil and gas producing assets based on the undiscounted estimated future cash flows associated with estimated proved reserves on a field-by-field basis.

In determining the estimated future cash flows for impairment purposes for all periods presented, hydrocarbon duties based on sales to third parties have not been included in the net cash flow calculation for both Mexican FRS and U.S. GAAP. Management believes that the hydrocarbon duties paid are similar in nature to income taxes or dividend distributions payable to its parent, and therefore are properly excluded from the net cash flow calculation.

In 2007, 2006 and 2005, under U.S. GAAP, PEMEX did not record an impairment charge. During 2007, there was no impairment for the year under Mexican FRS; however, during 2006 and 2005, PEMEX recognized an impairment charge under Mexican FRS of Ps. 703,247 and Ps. 3,719,165, respectively, relating to Pemex-Petrochemicals and Pemex-Exploration and Production assets. Because these assets had already been impaired under U.S. GAAP, these charges have been reversed for U.S. GAAP purposes. The 2007, 2006 and 2005 U.S. GAAP net income reconciliation also includes a credit of Ps. 3,344,517, Ps. 3,275,319 and Ps. 4,134,166, respectively, for depreciation due to the difference in carrying values of long-lived assets between Mexican FRS and U.S. GAAP.

In addition, the 2005 U.S. GAAP net income reconciliation includes a debit of Ps. 1,606,344 to adjust for the impairment reversal accounted for under Mexican FRS during 2005.

(h) Fixed assets—Depreciation convention

Until 2002, under PEMEX's accounting policies, assets would begin to depreciate in the year after which they were placed in service. Under U.S. GAAP, however, assets are depreciated from the date they were placed in service. Beginning in 2003, PEMEX prospectively changed its accounting policies requiring

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

depreciation from the month after the asset was placed into service, therefore eliminating any differences between Mexican FRS and U.S. GAAP for assets placed in service in 2003 and later years. The 2007, 2006 and 2005 U.S. GAAP adjustments reflect a credit to income of Ps. 783,144 for the reversal of the depreciation expense previously recorded under U.S. GAAP for assets placed in service before 2003.

(i) Accounting for derivative financial instruments

For U.S. GAAP purposes, PEMEX applies SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (as amended, "SFAS No. 133"), which requires that all derivative instruments (including certain derivative instruments embedded in other contracts) be recognized in the balance sheet as assets or liabilities at their fair values and that changes to fair values be recognized immediately in earnings, unless the derivative qualifies as a "hedge" (as defined in SFAS No. 133), for which certain special accounting treatment is permitted.

In accordance with U.S. GAAP, hedge effectiveness is assessed consistently with the method and risk management strategy documented for each hedging relationship. PEMEX assesses the effectiveness of each hedging relationship retrospectively and prospectively to ensure that hedge accounting was appropriate for the prior period and continues to be appropriate for future periods. PEMEX considers hedge accounting to be appropriate if the assessment of hedge effectiveness indicates that the change in fair value of the designated hedging instrument is highly effective at offsetting the change in fair value or cash flow variability due to the hedged risk of the hedged item or transaction.

If a derivative instrument qualifies as a fair value hedge, the change in the fair value of the derivative and the change in the fair value of the hedged item that is due to the hedged risks is recorded in earnings based on the income classification of the item being hedged. These hedges also adjust the book values of the derivatives and hedged item. If a derivative instrument qualifies as a cash flow hedge, the effective portion of the hedging instrument's gain or loss is reported as stockholders' equity (as a component of accumulated other comprehensive income) and is reclassified into earnings in the period during which the transaction being hedged affects earnings. Gains or losses reclassified from stockholders' equity to earnings are classified in accordance with the earnings treatment of the hedged transaction. The ineffective portion of a hedging derivative's fair value change, where that derivative is used in a cash flow hedge, is recorded as current earnings in the comprehensive financing result. Classification in the statement of operations of the ineffective portion of the hedging instrument's gain or loss is based on the income statement classification of the transaction being hedged. If a derivative instrument does not qualify as a hedge under the applicable guidance, the change in the fair value of the derivative is immediately recognized in the statement of operations in the comprehensive financing result.

PEMEX also evaluates contracts for "embedded" derivatives, and considers whether any embedded derivatives have to be bifurcated, or separated, from the host contracts in accordance with SFAS No. 133 requirements. Embedded derivatives may have terms that are not clearly and closely related to the terms of the host contract in which they are included. If embedded derivatives exist that are not clearly and closely related to the host contract or either include leverage features or exposure to the substantial loss of the principal in the case of structured products, they are accounted for separately from the host contract as freestanding derivatives, with changes in their fair value recorded in current earnings in the comprehensive financing result to the extent that the hybrid instrument is not already recorded at fair value with changes in fair value recorded in earnings.

When hedge accounting is discontinued due to PEMEX's determination that the derivative no longer qualifies as an effective fair value hedge, PEMEX will continue to carry the derivative on the balance sheet at

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

its fair value with changes in fair value recorded in earnings under the comprehensive financing result. The related hedged asset, liability or firm commitment will cease to be adjusted for changes in fair value that are due to the previously hedged risk and subsequent interests accrual will be recognized based on the new effective interest yield or funding cost, taking into account the fair value hedge adjustment amount as of the termination date of the hedge. When PEMEX discontinues hedge accounting in a cash flow hedge relationship because it is no longer probable that the forecasted transaction will occur in the originally expected period or within two months, the effective gain or loss on the derivative remaining in accumulated other comprehensive income is reclassified immediately into earnings; if a derivative instrument ceases to meet the criteria for hedge accounting, any subsequent gains or losses are recognized in current earnings and the effective portion, as of the date the cash flow hedge relationship ceased to exist, is recorded in earnings based on where the hedged item had an effect, in the amount needed to achieve the effective yield or funding cost provided by the derivative while the hedged item still impacts earnings.

The remaining adjustment of the carrying amount of a fair value hedged asset, liability or firm commitment will remain part of the carrying amount of that asset or liability or firm commitment until the asset is sold or written off, the liability expires, is paid or transferred or the firm commitment ceases to exist. In fair value hedges, an adjustment of the carrying amount of a hedged interest-bearing financial instrument will be amortized to earnings as part of the new effective yield; amortization will begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

For Mexican FRS purposes, effective January 1, 2005, PEMEX adopted the provisions of Bulletin C-10, "Derivative Financial Instruments and Hedging Operations," issued by the MIPA, which contains provisions similar to those of SFAS 133, and provides expanded guidance for the recognition, valuation, accounting treatment and disclosure applicable to derivative financial instruments including hedges and embedded derivatives, included hedge documentation and effectiveness testing.

Similar to the requirements under U.S. GAAP, contracts need to be evaluated for embedded derivatives with such derivatives needing to be bifurcated from the host contracts under certain conditions and recognized at fair value with fluctuations recognized in earnings. For Mexican FRS purposes and U.S. GAAP, foreign currency embedded derivatives in either recognized financial instruments or in non-recognized contractual agreements, are bifurcated from host contracts when such contracts are not denominated in one of the functional currencies of either one of the counterparties.

As of December 31, 2007, PEMEX did recognize an impact in earnings in the comprehensive financing result, due to the foreign currency embedded derivatives effects. The foreign currency embedded derivatives were bifurcated from host contracts when such contracts were not denominated in the functional currency of either one of the contractual counterparties; therefore as of December 31, 2007 there are no differences between Mexican FRS and U.S. GAAP related to accounting for derivative instruments and hedging activities (including embedded derivatives attributable to the embedded non-functional currency component), except that U.S. GAAP allows for non-effectiveness testing associated with the use of interest rate swaps, when they meet certain general and particular conditions in designated hedging relationships (known as the "short-cut method criteria").

As a result of the above, PEMEX has recognized a U.S. GAAP adjustment for the years ended December 31, 2007, 2006 and 2005, representing a net (loss) gain of Ps. (8,149,706) Ps. 74,673 and Ps. 1,030,873, respectively, reported in the comprehensive financing result in the consolidated statements of operations.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

For the years ended December 31, 2007, 2006 and 2005, PEMEX recognized a net gain (loss) of Ps. 656,699, Ps. 5,274,109 and Ps. (4,930,806), respectively, reported as “derivative financial instruments” in the consolidated other comprehensive income (loss) statement under U.S. GAAP.

As to permissible exclusions under both Mexican FRS and U.S. GAAP, for hedge effectiveness testing on formalized hedge relationships, PEMEX uses all components of each derivative’s gain or loss that were included in the assessment and measurement of hedge effectiveness, except for the time value (extrinsic value changes) of option contracts. The time value exclusion on options based hedges is reflected in the comprehensive financing result within earnings.

For cash flow hedges, effective gains and losses on derivative contracts that are reclassified from accumulated other comprehensive income to current-period earnings are included in the line item in which the hedged item is recorded in the period during which the forecasted transaction (including recognized assets or liabilities where applicable as hedged items) affects earnings. In 2007, a net loss of Ps. 1,479,284 was reclassified from other comprehensive income (loss) into earnings and as of December 31, 2007, a net loss of Ps. 812,620 of the balance related to derivative instruments accumulated in other comprehensive income (loss) is expected to be reclassified during the next twelve months to the consolidated statement of operations. In 2006, a net loss of Ps. 727,706 was reclassified from other comprehensive income (loss) into earnings.

(j) Profit in inventory

Under Mexican FRS, PEMEX values crude oil and derivatives for export at realizable value with the difference between the realizable value and cost recorded in earnings. In contrast, U.S. GAAP requires that inventories be recorded at the lower of cost or market value. For U.S. GAAP equity reconciliation purposes, PEMEX has eliminated the effect of recognizing a profit within its ending inventory balance at each period end. For net income reconciliation purposes, the adjustment reflects the reversal of the prior year’s equity adjustment as inventory is sold, as well as profit in inventory at the balance sheet date.

(k) Advance payments on minimum guaranteed dividend

Under Mexican FRS, advance payments on the minimum guaranteed dividend owed to the Mexican Government derived from the capitalization of debt as described in Note 14 are recorded as an account receivable prior to approval of the total annual dividend amount by the Board of Directors, which usually takes place in the following fiscal year.

Under U.S. GAAP, such receivable balances are reflected as a reduction in equity. PEMEX has accordingly adjusted equity to reflect the advance minimum guaranteed dividend payment as a reduction in equity.

The effective rate used to calculate the minimum guaranteed dividend is LIBOR plus 6.175% (in 2007, was 6.3165% and from 4.5206% to 6.4530% in 2006).

The final payment of capitalized debt amounted to U.S. \$392,310, and was made in January 2007.

(l) Accounting for available-for-sale securities (Repsol)

Pursuant to SFAS No. 115, PEMEX classifies its investment securities as “available-for-sale” and, accordingly, they are recorded at fair value with unrealized gains and losses excluded from the statement of operations and reported in other comprehensive (loss) income. The fair value of the securities is determined by quoted market prices at December 31, 2007, 2006 and 2005. An impairment loss is recognized when the loss is considered other than temporary.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Under Mexican FRS, these investment securities are also recorded at fair value but the unrealized gains and losses are reflected in earnings. The income adjustments for the years ended December 31, 2005, 2006 and 2007 reflect the reversal of the fair value adjustment to earnings as reflected under Mexican FRS whereas U.S. GAAP would require such adjustment to be reflected in other comprehensive (loss) income.

The U.S. GAAP cost and fair value of PEMEX's investments at December 31, 2007, 2006 and 2005, are as follows:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain</u>
2007	Ps. 10,429,499	Ps. 23,146,258	Ps. 12,716,759
2006	Ps. 10,229,803	Ps. 23,192,820	Ps. 12,963,017
2005	Ps. 10,078,636	Ps. 20,046,310	Ps. 9,967,675

(m) Effects of inflation on the U.S. GAAP adjustments

Various U.S. GAAP adjustments included herein are adjustments to monetary assets and liabilities recorded under Mexican FRS pursuant to Bulletin B-10 as described in Note 3a. and, therefore, the adjustments to the respective balance would also result in an adjustment to the monetary gain or loss as reported under Mexican FRS for each of the three years presented.

(n) Deferred income taxes

As described in Note 18, during 2005, a new fiscal regime was enacted that was applicable to Petróleos Mexicanos and its subsidiary entities effective January 1, 2006. Due to the change in tax regime, Petróleos Mexicanos and its subsidiary entities began recognizing deferred income taxes during 2005. The U.S. GAAP equity adjustment represents the cumulative impact of deferred income taxes relating to the other U.S. GAAP adjustments applicable to Petróleos Mexicanos and its subsidiary entities.

(o) Reclassification of Pemex Finance equity to minority interest

Effective July 1, 2005, PEMEX entered into an option agreement with BNP Paribas Private Bank and Trust Cayman Limited to acquire 100% of the shares of Pemex Finance. As a result, since 2005, the financial results of Pemex Finance have been consolidated into the financial statements of PEMEX for Mexican FRS purposes. Historically, Pemex Finance has been consolidated in the accompanying condensed consolidated U.S. GAAP information included herein for all periods presented. However, under U.S. GAAP, net income and retained earnings from Pemex Finance are reclassified as minority interest due to the fact that PEMEX is not currently owner of any of the shares of Pemex Finance. The U.S. GAAP adjustment related to Pemex Finance represents the reclassification of net income and equity recognized under Mexican FRS to minority interest.

II. Additional disclosure requirements:

(a) Consolidation of Pemex Finance

PEMEX and certain subsidiaries have entered into several agreements with Pemex Finance under which Pemex Finance purchases existing accounts receivable and rights to future receivables from certain customers. Pemex Finance obtains resources for such purchases through the placement of debt instruments in the international markets as well as the recurring returns on its investments. Through December 31, 2004, Pemex Finance was not consolidated into PEMEX's condensed consolidated financial statements for Mexican FRS purposes. Beginning in 2005, Pemex Finance is consolidated under Mexican FRS.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Under U.S. GAAP SFAS No. 140, "Accounting for the Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" ("SFAS No. 140"), PEMEX has evaluated the Pemex Finance structure in light of the permitted and non-permitted activities of a Qualified Special Purpose Entity ("QSPE") and has determined that Pemex Finance does not qualify as a QSPE and should therefore be consolidated for U.S. GAAP purposes. Consequently, Pemex Finance has been consolidated in the accompanying condensed consolidated U.S. GAAP information included herein for all periods presented; subsequently is reclassified as minority interest as described in note 21 Ip.

(b) Special Tax on Production and Services ("IEPS Tax")

Under Mexican FRS, the IEPS Tax is reflected as part of "Net domestic sales" when charged to customers and the amounts payable to the Mexican Government are then deducted from "Income before hydrocarbon extraction duties and other, special tax on production and services, and cumulative effect of adoption of new accounting standards."

Under U.S. GAAP, this tax would have no net effect on revenues nor would it be deducted from "Income before hydrocarbon extraction duties and other, special tax on production and services, and cumulative effect of adoption of new accounting standards," as both the amount charged to customers and the amount accrued as payable to the tax authorities would be excluded from revenues (*i.e.*, there is no gross-up).

(c) Environmental, dismantlement and abandonment liabilities

PEMEX estimates its environmental liabilities on a site-by-site basis based on the best available information. PEMEX establishes accruals for its environmental liabilities using estimates based on costs of similar remediation works most recently contracted and in progress at that time.

PEMEX has internal guidelines for estimating and recording environmental liabilities, the *Guía para la Determinación de las Provisiones y Revelaciones de Carácter Ambiental* (Guidelines for the Determination of Environmental Liabilities and their Disclosure). The guidelines' purpose is to standardize and improve PEMEX's internal procedures for identifying necessary remediation works and estimating and monitoring environmental liabilities.

These guidelines establish that an environmental liability exists when:

- i) As a result of the activities of PEMEX, an affected area is identified in a particular site, and PEMEX undertakes a formal commitment to correct the environmental deficiency, in accordance with the criteria, guidelines, standards and legal framework in force; and
- ii) A reasonable estimate of the costs of remediation or clean-up of the identified affected area has been made, including the costs of the assessment studies.

As stated above, in accordance with past and present internal guidelines, PEMEX conducts site-by-site studies to identify environmental liabilities and develop a reasonable estimate of such liabilities. These guidelines consider many factors but are tailored to specific Mexican requirements. Each contaminated site must be characterized, quantified and assessed through a specific study. The contamination of the affected sites may extend to the soil, subsoil and bodies of water, including water deposits, lagoons, swamps and others. These sites may be located inside PEMEX's facilities, in surrounding areas, in abandoned areas where PEMEX had activity in the past or along the pipelines.

Once the corresponding contaminated site has been identified and evaluated, expenses for the cleanup of (i) hydrocarbon seepage and other spills that may cause pollution and that cannot be corrected in a short

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

timeframe, (ii) water deposits and (iii) the concentration of hazardous residuals, will be included in the remediation or restoration of affected areas. Estimates are kept current based on the best available information.

Based on reports from field managers and other available information, management prepares reports for identified affected areas on a periodic basis. When the contamination relates to a new incident, PEMEX informs the *Procuraduría Federal de Protección al Ambiente* (Federal Environmental Protection Agency, or “PROFEPA”) and responds immediately to eliminate the cause of the incident or to minimize its impact. Subsequently, PEMEX and PROFEPA jointly determine whether the contamination has been eliminated or if additional actions are necessary for the remediation of the site.

PEMEX believes its environmental liabilities are probable when its initial studies reveal the existence of contamination in the inspected areas at levels above those permitted by Mexican law, indicating that PEMEX will have to perform remediation works necessary to bring the site into compliance. PEMEX believes the liability is reasonably estimable when (i) an assessment of the size of the affected area has been made, (ii) it has compared the affected area to other affected areas identified and addressed in the past, and (iii) based on PEMEX’s experience with current or recent activities on similar sites, PEMEX can assess the estimated remediation costs in order to be able to calculate the corresponding environmental liability. Thus, PEMEX accrues for these environmental liabilities when it identifies affected areas with contamination levels above those permitted by Mexican law and PEMEX is able to make a reasonable estimate of the size of the affected area and the remediation cost. In addition, PEMEX periodically revises its estimates of environmental liabilities as it obtains new information during the course of the remediation works in order to ensure its estimates are based on the most accurate and updated information.

PROFEPA administers the Mexican environmental regulatory rubric and establishes acceptable standards of environmental remediation. Although PROFEPA has the authority to review and inspect remediation works performed by PEMEX and compliance with permitted contamination levels established by laws and regulations, it does not determine PEMEX’s environmental liabilities. PEMEX maintains proper records of all of the studies, estimations, performed works and any other information that PROFEPA may request from time to time.

During 2007, 2006 and 2005, PEMEX spent Ps. 4,120,000, Ps. 4,175,000 and Ps. 3,019,000, respectively, on various environmental projects and related expenditures. The most important projects have included the modernization of installations, the implementation of systems and control mechanisms to monitor atmospheric pollution, the acquisition of equipment to clean hydrocarbon spills, the expansion of aquatic effluent systems, the restoration and reforestation of affected areas, environmental investigative studies and the conducting of environmental audits. In addition, PEMEX has engaged in extensive research and development efforts to develop capacity for increased production of unleaded gasoline, diesel and fuel oil with lower sulfur content and alternative fuels, such as industrial oil gas and natural gas. Currently, PEMEX is developing a procedure, *Procedimiento para la Determinación de Gastos Asociados a las Actividades de Seguridad Industrial y Protección Ambiental* (Procedure for the Determination of Costs Associated with Industrial Safety and Environmental Protection) to determine the costs and expenses related to activities associated with industrial safety and environmental management.

PEMEX’s management believes that its operations are in substantial compliance with the *Ley General del Equilibrio Ecológico y Protección al Ambiente* (General Law of Ecological Equilibrium and Environmental Protection, or the “Environmental Law”) as such law has been historically interpreted and enforced.

Environmental expenditures are expensed or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

benefit are expensed. Liabilities for expenditures of a non-capital nature are recorded on a discounted basis when expenses include payments during periods longer than one year, when environmental assessment and/or remediation is probable and the costs can be reasonably estimated.

As PEMEX has exclusive rights to production and processing of crude oil, natural gas, and refined products within Mexico, there are no instances of joint liability; PEMEX is the sole responsible party in the event of environmental damage. PEMEX obtains insurance policies to cover the cost of certain environmental contingencies. The liability accruals are not reflected net of any amounts forthcoming under such policies.

Environmental liabilities accrued in the consolidated financial statements, for both Mexican FRS and U.S. GAAP purposes, as of December 31, are divided among the operating units as follows:

	<u>2007</u>	<u>2006</u>
Pemex—Exploration and Production	Ps. 371,639	Ps. 716,572
Pemex—Refining ⁽¹⁾	1,507,709	1,341,520
Pemex—Gas and Basic Petrochemicals	211,692	284,183
Pemex—Petrochemicals	2,400	55,983
Total Environmental Liability Accrual	<u>Ps. 2,093,440</u>	<u>Ps. 2,398,258</u>

(1) The increase primarily resulted from revisions to estimates and new reserves established for additional remediation plans.

(d) Dismantlement and abandonment costs

Under current Mexican law, PEMEX's legal obligation related to dismantlement and abandonment activities is governed by the following two federal laws: the Petroleum Works Law and the Environmental Law described in this note. Although PEMEX is subject to other laws and regulations established at a local level in areas where PEMEX undertakes petroleum extraction activities, these local laws and regulations do not contain any specific guidance on abandonment, restoration and removal of oil and gas facilities or otherwise impose a higher standard on PEMEX in this regard. Mexico is not a party to any international treaty or convention that would affect PEMEX's understanding of its obligation with regard to dismantlement and abandonment activities. Thus, the only relevant law for PEMEX as to abandonment and removal of facilities related to oil- and gas-producing activities is Mexican federal law.

The Petroleum Works Law provides that wells must be plugged, or in certain cases, capped, to ensure the maintenance of sanitary and safe conditions and to prevent the seepage of hydrocarbons to the surface. The Petroleum Works Law requires that PEMEX plug a well when it turns out to be dry, invaded with salt water or abandoned due to a mechanical accident, or once a well's production has been depleted such that abandonment is necessary due to economic unfeasibility of production. All activities required for plugging a well are undertaken with the purpose of isolating, in a definitive and convenient manner, the cross formations in the perforation that contains oil, gas or water in order to ensure that hydrocarbons do not seep to the surface.

PEMEX must obtain authorization from the Ministry of Energy before performing any plugging activities. The Petroleum Works Law also states that the Ministry of Energy may authorize temporary plugging of exploratory wells where production of hydrocarbons is commercially feasible but for which there are no adequate means for their exploitation.

PEMEX monitors and reviews its own internal estimates of costs to undertake dismantlement and abandonment at levels consistent with Mexican legal requirements and guidelines for oil and gas industry

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

extraction activities. Estimates as to aggregate costs include PEMEX's operational specifics such as the number of onshore and offshore wells, depth of wells, the varying nature of offshore platforms, expected production lives, current expectations as to when the costs will be incurred based on present production rates and other operational specifics. The actual costs incurred in the dismantlement and retirement of wells are considered where practicable, as described above. The average cost for plugging and dismantlement varies from producing region to producing region and from platform to platform. For the offshore regions, to the extent that actual costs are not available due to limited plugging and dismantlement activity historically, PEMEX relies on estimates based on services costs. The estimated costs are both peso- and U.S. dollar-denominated.

(e) Pensions and seniority premiums

The components of seniority premiums and pension plan cost, calculated in accordance with SFAS No. 87 and 158, using December 31 as a measurement date, consist of the following:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Service cost	Ps. 9,088,563	Ps. 7,110,082	Ps. 6,513,611
Interest cost	27,204,694	23,954,649	20,983,953
Return on plan assets	(11,149)	(32,821)	(185,989)
Net amortization of gain and losses	431,153	349,640	815,762
Amortization of net transition obligation	5,733,629	5,708,786	5,749,251
Adjustment to net periodic pension cost due to inflation	866,361	1,521,663	1,098,702
Plan amendments	527,348	522,253	198,205
Net cost under U.S. GAAP	<u>43,840,599</u>	<u>39,134,252</u>	<u>35,173,495</u>
Net cost under Mexican FRS	<u>(46,169,035)</u>	<u>(41,073,977)</u>	<u>(36,185,952)</u>
Additional (benefit) expense recognized under U.S. GAAP	<u>(Ps. 2,328,436)</u>	<u>(Ps. 1,939,725)</u>	<u>(Ps. 1,012,457)</u>

Actuarial assumptions (net of inflation) used in the calculation of benefit obligations, net seniority premiums and pension plan cost under U.S. GAAP as of December 31 are:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Discount rate	4.25%	4.25%	4.50%
Rates of increase in compensation levels	0.50%	0.50%	0.50%
Expected long-term rate of return on assets	4.25%	4.25%	5.00%

The calculation of pension cost and benefit obligations under SFAS No. 87 and 158 requires considerable judgment with respect to choosing actuarial assumptions. Each significant assumption reflects PEMEX's best estimate of the plan's future performance solely with respect to that assumption. Assumed discount rates and compensation levels often have the greatest effect on pension cost and benefit obligations, and are related because both are affected by some of the same economic factors. The discount rate is based upon the current prices for settling the pension obligation, referred to as the "settlement rate" and the current yield on high quality corporate bonds (AA or better) of term and currency consistent with the benefit obligation as of the measurement date. According to the external actuary, assumed compensation levels reflect PEMEX's estimate of actual future compensation levels for the individuals involved and is consistent with

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

assumed discount rates to the extent that both incorporate expectations of the same future economic conditions, such as inflation.

The combined seniority premium and pension plan liability as of December 31 under SFAS No. 87 and 158 is as follows:

	<u>2007</u>	<u>2006</u>
Accumulated benefit obligation	Ps. 354,120,653	Ps. 329,198,933
Projected benefit obligation	364,687,896	336,758,893
Plan assets at fair value	(7,122,630)	(2,118,402)
Projected benefit obligation in excess of plan assets	357,565,266	334,640,491
Unrecognized net loss	—	(45,560,129)
Unrecognized transition obligation	—	(69,564,015)
Unrecognized prior service costs	—	(5,905,290)
Accrued liability under U.S. GAAP	357,565,266	213,611,057
Accrued liability recognized under Mexican FRS	(232,543,132)	(205,735,690)
U.S. GAAP adjustment to seniority premium and pension plan liability after recognition of SFAS 158	Ps. 125,022,134	Ps. 7,875,367
Accumulated other comprehensive income	119,475,192	—
Net U.S. GAAP adjustment to seniority premium and pension plan liability	5,546,942	7,875,367
Additional minimum liability	Ps. —	Ps. 115,122,678

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The changes recognized in “accumulated other comprehensive income” before and after the recognition of SFAS 158, as of December 31 is as follows:

	<u>2007</u>	<u>2006</u>
<i>Before recognition of the funded status provisions of SFAS 158</i>		
Additional liability	Ps.114,921,322	Ps. 115,122,678
Actual intangible assets	68,227,509	<u>72,222,554</u>
Accumulated other comprehensive (Income)	46,693,813	<u>42,900,124</u>
<i>After recognition of the funded status provision of SFAS 158</i>		
Transition (assets) obligation	Ps. 63,402,660	Ps. —
Prior service cost (income)	5,208,308	—
Net (gain)/loss	50,864,224	—
Accumulated other comprehensive (Income)	119,475,192	—
Increase in accumulated other comprehensive loss (income) to reflect the recognition of SFAS 158	Ps. 72,781,379	Ps. —
Non current assets	(7,122,630)	—
Current liabilities	10,719,970	—
Non current liabilities	346,845,296	—
Net amount recognized in statement of financial position as of December 31, 2007	Ps.357,565,266	<u>Ps. 328,733,735</u>

The scheduled maturities on the benefits expected to be paid according to the plans in each of the next ten years through 2017, are as follows:

<u>Year</u>	<u>Expected Benefit</u> <u>Payments</u>
2008	Ps. 17,842,600
2009	17,923,433
2010	19,624,667
2011	21,467,404
2012	23,259,417
2013	25,232,630
2014	26,954,721
2015	28,900,722
2016	30,446,622
2017	32,066,949
Total	<u>Ps. 243,719,165</u>

The 2007 and 2006 U.S. GAAP equity adjustments of Ps. 67,715,653 and Ps. 5,426,624 reflect the difference in the amounts recognized in accumulated other comprehensive loss under Mexican FRS of Ps. 51,759,539 and Ps. 48,326,747, respectively, and the amounts recognized under U.S. GAAP of Ps. 119,475,192 and Ps. 42,900,124, respectively, and including the adoption of SFAS 158.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The objective of PEMEX's investment guidelines with respect to its plan assets is to grant the highest security together with an adequate rate of return, maintaining the purchasing power of the investments. The comparative benchmark used by PEMEX is the monthly average of primary interest rates of Mexican Government 28-day Treasury-bills ("Cetes 28").

The investment guidelines list certain prohibited investments, such as securities of companies that are subject to intervention by a regulatory authority, subordinated securities, convertible securities, certain foreign exchange securities, derivatives such as futures, forwards, swaps, options, exotic options, swaptions, etc., except structured notes in pesos with protected initial investment, securities having terms with certain characteristics such as liquidity, risk, return, or maturity that do not comply with certain requirements set by PEMEX's Financial Resources Committee and securities not listed on the Mexican Stock Exchange.

The expected long-term rate of return is based on the guidelines of the Mexican Society of Consulting Actuaries, which annually issues recommendations for selecting financial assumptions based on a historical analysis conducted using economic variables such as inflation, risk-free interest rates and increases to the legal minimum wage and salaries in general.

At December 31, 2007 and 2006, all of PEMEX's plan assets were invested in Mexican Government bonds and bonds issued by financial institutions listed on the Mexican Stock Exchange. The following table shows PEMEX's actual investment allocation at December 31 of each year.

<u>Securities</u>	<u>2007</u>	<u>2006</u>
Mexican Government Bonds	84.%	71%
Bonds issued by financial institutions listed on the Mexican Stock Exchange	16%	29%
Total	<u>100%</u>	<u>100%</u>

(f) Other post-retirement benefits

PEMEX implemented SFAS No. 106, effective January 1, 1995, using the transitional recognition method and December 31 as a measurement date.

PEMEX makes supplemental payments in respect of its obligations for gas, gasoline and basic food supplies and provides healthcare benefits, in each case to retired employees and immediate family members. PEMEX regularly adjusts the level of its supplemental payments based on inflationary conditions. Healthcare is provided through a regional network of PEMEX hospitals and medical centers, which also provide care to active PEMEX employees. No commitments have been made regarding the level of such contributions in the future.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The scheduled amounts of the benefits expected to be paid according to the plans in each of the next ten years, through 2017, are as follows:

<u>Year</u>	<u>Expected Benefit</u> <u>Payments</u>
2008	Ps. 13,257,829
2009	14,117,305
2010	15,172,410
2011	16,350,695
2012	17,605,214
2013	18,965,386
2014	20,307,814
2015	21,715,469
2016	22,562,957
2017	23,634,012
Total	<u>Ps. 183,689,091</u>

F-65

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The components of other post-retirement benefits expense consist of the following for the years ended December 31, 2007, 2006 and 2005:

	2007			2006			2005		
	Supplemental Payments	Health Services	Total	Supplemental Payments	Health Services	Total	Supplemental Payments	Health Services	Total
Service cost	Ps. 4,103,096	Ps. 2,298,180	Ps. 6,401,276	Ps. 4,687,869	Ps. 1,210,546	Ps. 5,898,415	Ps. 2,715,518	Ps. 1,448,328	Ps. 4,163,846
Interest cost	14,283,753	7,508,894	21,792,647	12,170,005	5,543,442	17,713,447	9,689,454	5,572,995	15,262,449
Amortization of actuarial (gains) and losses	812,365	(562,453)	249,912	421,135	(2,697,498)	(2,276,363)	(177,395)	(1,690,144)	(1,867,539)
Amortization of prior service cost and plan amendments	21,545	55,841	77,386	21,369	58,797	80,166	(15,598)	—	(15,598)
Amortization of transition obligation	3,112,566	2,791,828	5,904,394	3,087,178	2,769,056	5,856,234	3,108,667	2,791,742	5,900,409
Adjustment to net periodic post-retirement benefit cost due to inflation	444,765	241,883	686,648	826,344	278,575	1,104,919	512,410	270,467	782,877
Net expense under U.S. GAAP	22,778,090	12,334,173	35,112,263	21,213,900	7,162,918	28,376,818	15,833,056	8,393,386	24,226,444
Expense under Mexican FRS	(22,925,973)	(16,211,847)	(39,137,820)	(21,560,040)	(11,859,332)	(33,419,372)	(15,890,329)	(11,711,335)	(27,601,664)
Additional expense (benefit) under U.S. GAAP	(Ps. 147,883)	(Ps. 3,877,674)	(Ps. 4,025,557)	(Ps. 346,140)	(Ps. 4,696,414)	(Ps. 5,042,554)	(Ps. 57,273)	(Ps. 3,317,949)	(Ps. 3,375,220)

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Actuarial assumptions used in the calculation of other post-retirement benefits and costs under U.S. GAAP as of December 31 were:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Discount rate	4.25%	4.25%	4.50%
Health care cost trend rate	1.50%	1.50%	1.50%

Since the other post-retirement benefits are not based on levels of compensation, it is not necessary to use salary increase assumptions to determine expenses. The effect of a 1% increase in the healthcare cost trend rate was to increase net expense for other post-retirement benefits by Ps. 9,686,783 for 2007, Ps. 1,748,864 for 2006 and Ps. 2,288,044 for 2005, and to increase the accumulated post-retirement benefit obligation by Ps. 14,698,361 for 2007, Ps. 13,928,396 for 2006 and Ps. 21,373,088 for 2005. The effect of a 1% decrease in the health care cost trend rate was to decrease net expense for other post-retirement benefits by Ps. 6,386,544 for 2007, Ps. 1,403,883 for 2006 and Ps. 2,519,736 for 2005, and decrease the accumulated post-retirement benefit obligation by Ps. 12,007,042 for 2007, Ps. 11,383,680 for 2006 and Ps. 26,676,555 for 2005.

F-67

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The other post-retirement benefits liability as of December 31, 2007 and 2006 was as follows:

	2007			2006		
	Supplemental Payments	Health Services	Total	Supplemental Payments	Health Services	Total
Accumulated unfunded post retirement benefit obligation:						
Retirees	Ps. 97,348,838	Ps. 53,911,935	Ps. 151,260,773	Ps. 83,090,461	Ps. 52,182,612	Ps. 135,273,073
Fully eligible active participants	16,897,125	1,633,991	18,531,116	15,356,194	1,388,752	16,744,946
Other active plan participants	84,421,650	43,687,740	128,109,390	75,012,521	39,450,953	114,463,474
Total	198,667,613	99,233,666	297,901,279	173,459,176	93,022,317	266,481,493
Unrecognized actuarial gains (losses)	—	—	—	(26,829,950)	11,130,345	(15,699,605)
Prior service cost and plan amendments	—	—	—	(473,680)	(503,366)	(977,046)
Unamortized transition obligation	—	—	—	(37,623,004)	(32,861,317)	(70,484,321)
Net post-retirement benefit liability:						
U.S. GAAP	198,667,613	99,233,666	297,901,279	108,532,542	70,787,979	179,320,521
Mexican FRS	(132,243,775)	(39,645,991)	(171,889,766)	(115,068,180)	(26,039,433)	(141,107,613)
U.S. GAAP adjustment after recognition of SFAS 158	66,423,838	59,587,675	126,011,513	(6,535,638)	44,748,546	38,212,908
Accumulated other comprehensive income	73,107,425	18,716,736	91,824,161	—	—	—
Net U.S. GAAP adjustment	<u>(Ps. 6,683,587)</u>	<u>Ps. 40,870,939</u>	<u>Ps. 34,187,352</u>	<u>(Ps. 6,535,638)</u>	<u>Ps. 44,748,546</u>	<u>Ps. 38,212,908</u>

F-68

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The changes recognized in “other comprehensive income” as of December 31, 2007 were as follows:

	2007		
	<u>Supplemental Payments</u>	<u>Health Services</u>	<u>Total</u>
<i>After recognition of the funded status provision of SFAS 158</i>			
Transition (assets) obligation	Ps. 34,490,623	Ps. 29,986,702	Ps. 64,477,325
Prior service cost (income)	452,493	446,770	899,263
Net (gain)/loss	<u>38,164,309</u>	<u>(11,716,736)</u>	<u>26,447,573</u>
Accumulated other comprehensive (Income)	<u>Ps. 73,107,425</u>	<u>Ps. 18,716,736</u>	<u>Ps. 91,824,161</u>
Increase in accumulated other comprehensive loss (income) to reflect the adoption of SFAS 158	<u>Ps. 73,107,425</u>	<u>Ps. 18,716,736</u>	<u>Ps. 91,824,161</u>
Current liabilities	Ps. 8,810,348	Ps. 4,447,481	Ps. 13,257,829
Noncurrent liabilities	<u>189,857,265</u>	<u>94,786,185</u>	<u>284,643,450</u>
Net amount recognized in statement of financial position as of December 31, 2007	<u>Ps.198,667,613</u>	<u>Ps. 99,233,666</u>	<u>Ps.297,901,279</u>

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

PEMEX recognized SFAS No. 158, and included its effects in the results of the actuarial valuation of its labor obligations effective January 1, 2007. Pursuant to the requirements of SFAS No. 132, the following tables present a reconciliation of the beginning and ending balances of plan assets' fair value and the accumulated post-retirement benefit obligation:

	Seniority Premiums and Pension Benefits		Supplemental Payments		Health Services	
	2007	2006	2007	2006	2007	2006
Change in projected benefit obligation (PBO)						
Projected benefit obligation at beginning of year	Ps.324,558,730	Ps.281,522,669	Ps.167,175,066	Ps.142,717,327	Ps.89,652,288	Ps.65,811,024
Effect of inflation on beginning balance	12,200,163	11,410,961	6,284,111	5,784,761	3,370,030	2,667,518
Service cost	9,088,563	7,110,078	4,103,096	4,687,869	2,298,180	1,210,546
Interest cost	27,204,694	23,954,649	14,283,753	12,170,005	7,508,894	5,543,442
Prior service costs and plan amendments	(3,817)	1,421,199	677,354	683,104	131,165	278,782
Actuarial (gains)/losses	5,079,228	23,305,400	11,894,618	12,676,122	(1,121,669)	19,901,488
Benefits paid	(13,439,665)	(11,966,065)	(5,750,385)	(5,260,012)	(2,605,222)	(2,390,482)
Projected benefit obligation at end of year	<u>Ps.364,687,896</u>	<u>Ps.336,758,891</u>	<u>Ps.198,667,613</u>	<u>Ps.173,459,176</u>	<u>Ps.99,233,666</u>	<u>Ps.93,022,318</u>
Change in plan assets						
Fair value of plan assets at beginning of year	Ps. 2,041,656	Ps. 1,467,227	—	Ps. —	Ps. —	Ps. —
Effect of inflation on beginning balance	76,746	59,472	—	—	—	—
Actual return on plan assets	(758,787)	(804,844)	—	—	—	—
Company contributions	24,953,065	18,304,118	—	—	—	—
Transfer of funds	(5,750,385)	(5,207,690)	5,750,385	5,207,690	—	—
Benefits paid	(13,439,665)	(11,699,880)	(5,750,385)	(5,207,690)	—	—
Fair value of plan assets at end of year	<u>Ps. 7,122,630</u>	<u>Ps. 2,118,403</u>	<u>Ps. —</u>	<u>Ps. —</u>	<u>Ps. —</u>	<u>Ps. —</u>

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(g) Leases

As of December 31, 2007, PEMEX did not have any significant operating lease arrangements or capital leases.

(h) Supplemental geographical information

The majority of PEMEX's operations are in Mexico. The following shows PEMEX's domestic and export sales for the years ended December 31 (on a Mexican FRS basis):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Domestic sales	Ps. 592,047,961	Ps. 567,289,873	Ps. 545,339,433
Export sales:			
United States	441,431,866	450,196,550	376,680,788
Canada, Central and South America	36,547,306	35,426,621	34,475,634
Europe	52,691,863	41,273,059	39,640,832
Far East	12,255,823	8,247,818	6,469,578
Total export sales	Ps. 542,926,858	Ps. 535,144,048	Ps. 457,266,832
Total sales	Ps.1,134,974,819	Ps.1,102,433,921	Ps.1,002,606,265

PEMEX does not have significant long-lived assets outside of Mexico.

For the years ended December 31, 2006 and 2005, under Mexican FRS, PEMEX recognized non-cash fixed asset impairment charges and reversals per segment as discussed in Note 21Ig.

(i) Valuation and qualifying accounts

The valuation and qualifying accounts for PEMEX are as follows:

<u>Description</u>	<u>Balance at beginning of period</u>	<u>Additions charged to costs and expenses</u>	<u>Deductions</u>	<u>Balance at end of period</u>
For the year ended December 31, 2007:				
Reserves deducted in the balance sheet from the assets to which they apply:				
Allowance for doubtful accounts	Ps. 2,674,170	Ps. 12,242,359	(Ps. 13,425,595)	Ps. 1,490,934
For the year ended December 31, 2006:				
Reserves deducted in the balance sheet from the assets to which they apply:				
Allowance for doubtful accounts	Ps. 2,709,459	Ps. 153,181	(Ps. 188,470)	Ps. 2,674,170
For the year ended December 31, 2005:				
Reserves deducted in the balance sheet from the assets to which they apply:				
Allowance for doubtful accounts	Ps. 2,141,949	Ps. 1,670,690	(Ps. 1,103,180)	Ps. 2,709,459

Note: The above valuation and qualifying accounts are presented in accordance with U.S. GAAP. The Mexican FRS accounts titled "reserve for dismantlement and abandonment activities, sundry creditors and others" and "reserve for retirement payments, pensions, and seniority premiums" are accrued liability accounts, and not valuation and qualifying accounts and have not been included in the table above.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(j) Significant risks and uncertainties

Environmental

The ultimate costs to be incurred in relation to PEMEX's environmental contingencies may exceed the total amounts reserved. Additional liabilities may be accrued as the assessment work is completed and formal remediation plans are formulated. Numerous factors affect the reliability and precision of clean-up cost estimates, including the individual characteristics of the site, the lack of specific guidance as to permissible levels of pollution and type of technology available for remediation as well as general economic factors, such as inflation.

As discussed in this note, PEMEX accrues an environmental liability when a reasonable estimate of the costs for remediation or clean-up of the identified affected area has been made. In some cases, investigations are not yet at a stage where PEMEX is able to quantify the liability or estimate a range of possible exposure. In such cases, the amounts of PEMEX's liabilities are indeterminate due to the unknown magnitude of possible contamination, the imprecise and conflicting engineering evaluations and estimates of proper cleanup methods and costs, the unknown timing and extent of the corrective actions that may be required, and the ambiguities in Mexican environmental laws and regulations.

PEMEX is not aware of any unasserted claims or assessments, which may give rise to an environmental liability, and therefore, no amounts related to such items have been reflected in the environmental accrual.

Mexican Government

The operations and earnings of PEMEX have been, and may in the future be, affected from time to time in varying degree by political developments and laws and regulations, such as forced divestiture of assets, budgetary adjustments, restrictions on production levels and capital expenditures, price controls, tax increases, cancellation of contract rights, refined product specifications, and environmental, health and safety regulations. Both the likelihood of such occurrences and their overall effect upon PEMEX are not estimable.

Labor

PEMEX employees belonging to the Petroleum Workers' Union of the Mexican Republic represent approximately 80% of the workforce. They have a collective bargaining agreement which is renegotiated every two years. On July 17, 2007, Petróleos Mexicanos and the Union executed a new collective bargaining agreement that became effective on August 1, 2007. The terms of the new agreement provide for a 4.25% increase in wages and a 1.6% increase in other benefits. By its terms, the new collective bargaining agreement is scheduled to expire on July 31, 2009.

Product prices

Because PEMEX's major products are energy-related commodities, significant changes in the international prices of crude oil, natural gas, refined products and petrochemical products could have a significant impact on PEMEX's results of operations in any particular year. In 2007, crude oil represented approximately 37% of PEMEX's sales revenues net of the IEPS Tax, and prices of the products PEMEX produces can be influenced by changes in crude oil prices, which makes it reasonably possible that PEMEX is vulnerable to near-term severe impacts from fluctuations in prices.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(k) Capitalized software costs

Direct internal and external costs related to the development of internal use software are deferred and included in other assets. Capitalized software costs, net of amortization, as of December 31, 2007 and 2006 amounted to Ps. 162,404 and Ps. 167,953, respectively. Amortization expense for the years ended December 31, 2007, 2006 and 2005 amounted to Ps. 112,310, Ps. 145,810 and Ps. 278,359, respectively.

(l) Supplemental condensed information on a U.S. GAAP basis

The following condensed consolidating information reflects the U.S. GAAP adjustments disclosed in this note.

CONDENSED CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2007 AND 2006

	2007	2006
ASSETS		
Total current assets	Ps. 397,534,791	Ps. 399,950,872
Properties and equipment, net	777,900,994	715,161,586
Intangible asset derived from the actuarial computation of labor obligations and other assets	35,865,531	109,159,182
Total assets	<u>Ps.1,211,301,316</u>	<u>Ps.1,224,271,640</u>
LIABILITIES		
Other current liabilities	Ps. 290,099,944	Ps. 176,904,411
Reserve for retirement payments, pensions and seniority premiums	23,977,799	—
Total current liabilities	314,077,743	176,904,411
Long-term debt	424,828,472	524,475,242
Reserve for dismantlement and abandonment activities, sundry creditors and others	31,467,252	31,513,074
Reserve for retirement payments, pensions and seniority premiums	631,488,746	508,054,258
Non current deferred income tax liabilities	6,106,494	4,742,792
Total liabilities	1,407,968,707	1,245,689,777
Minority interest	1,415,775	1,464,681
TOTAL EQUITY (DEFICIT)	<u>(198,083,166)</u>	<u>(22,882,818)</u>
Total liabilities and equity	<u>Ps.1,211,301,316</u>	<u>Ps.1,224,271,640</u>

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED
DECEMBER 31, 2007, 2006 AND 2005

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Total revenues, net of IEPS tax	Ps. 1,136,035,428	Ps.1,103,509,868	Ps. 982,007,013
Cost of sales	469,614,890	413,280,469	382,868,741
Gross income	666,420,538	690,229,399	599,138,272
General expenses	84,939,004	78,753,185	74,183,794
Operating income	581,481,534	611,476,214	524,954,478
Other revenues	83,019,010	61,213,533	2,896,394
Comprehensive financing result (cost)	(25,609,627)	(18,151,461)	(10,116,062)
Profit sharing in non-consolidated subsidiaries and affiliates	5,791,312	7,078,236	7,828,486
Income before taxes, duties and other and minority interest	644,682,229	661,616,522	525,563,296
Taxes and duties, net of IEPS tax	(677,318,216)	(604,839,287)	(604,607,734)
Cumulative effect of adoption of new accounting standards	—	—	(1,905,868)
Minority interest	(6,089)	(54,789)	1,159,233
Net income (loss)	<u>(Ps. 32,642,076)</u>	<u>Ps. 56,722,446</u>	<u>(Ps. 79,791,073)</u>

F-74

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	2007	2006	2005
Operating Activities			
Net (loss) income for the year	(Ps. 32,642,076)	Ps. 56,722,446	(Ps. 79,791,073)
Adjustments to reconcile net (loss) income to cash provided by (used in) operating activities:			
Depreciation and amortization	68,929,829	61,981,571	52,806,137
Reserve for retirement payments, pensions and seniority premiums	78,952,867	67,511,070	59,399,939
Loss on disposal of fixed assets	10,051,439	3,240,015	5,382,303
Allowance for uncollectible trade accounts	(1,086,357)	70,256	636,594
Minority interest	4,157	67,788	(1,159,233)
Foreign exchange loss (gain)	4,318,464	13,966,773	(30,220,724)
Accrued interest	4,607,397	—	—
Profits sharing in subsidiaries	(5,533,058)	(4,157,818)	(1,660,060)
Deferred income taxes	1,881,378	(1,861,265)	1,692,580
Dismantlement and abandonment costs in fixed assets	—	(1,992,048)	(1,761,581)
Unrealized gains on financial instruments	(8,149,706)	(74,672)	(733,513)
Gain from monetary position	(13,413,563)	(14,819,222)	(17,633,272)
	107,920,771	180,654,894	(13,041,903)
Changes in operating assets and liabilities:			
Accounts and notes receivable	(10,237,517)	(19,845,331)	(55,976,205)
Inventories	3,643,578	(8,630,955)	(7,263,527)
Other assets	1,219,546	(3,249,700)	3,675,065
Accounts payable and accrued liabilities ⁽¹⁾	106,582,975	(9,738,736)	47,316,130
Retirement, seniority premiums and other post-retirement benefit contributions and payments ⁽¹⁾	(27,717,544)	(21,003,633)	(22,897,096)
Cash flow provided by (used in) operating activities	181,411,809	118,186,539	(48,187,536)
Investing Activities			
Acquisition of fixed assets	(134,133,678)	(106,659,605)	(78,426,949)
Investments in Subsidiaries	1,508,668	—	—
Specific funds accounts-trade commission	—	(6,599,909)	7,497,438
Cash flows used in investing activities	(132,625,010)	(113,259,514)	(70,929,511)
Financing Activities⁽¹⁾			
Proceeds from new long term financing	117,557,830	168,709,813	263,049,489
Financing payments	(194,928,716)	(148,281,185)	(140,741,177)
Increase in Equity of Subsidiary Entities	11,160,824	48,702,873	48,142,543
Dividends paid to the Mexican Government	(263,329)	(268,990)	(16,500,691)
Cash flows (used in) provided by financing activities	(66,473,391)	68,862,511	153,950,164
Effects of inflation on cash and cash equivalents	(7,092,625)	(8,463,098)	(2,017,874)
(Decrease) increase in cash and equivalents	(24,779,217)	65,326,438	32,815,244
Cash and cash equivalents, beginning of period	195,776,457	130,450,019	97,634,776
Cash and cash equivalents, end of period	Ps. 170,997,240	Ps. 195,776,457	Ps. 130,450,019
Supplemental cash disclosures:			
Interest paid (net of amounts capitalized)	Ps. 42,784,228	Ps. 53,161,244	Ps. 59,154,710
Taxes paid	623,886,506	635,331,409	541,262,289
Supplemental non-cash disclosures:			
Unrealized gains on available for sale securities	(Ps. 240,723)	Ps. 2,995,342	Ps. 830,179
Additional minimum pension liability	(168,399,229)	(20,311,938)	(19,692,549)
Derivative financial instruments	656,699	5,274,109	(4,930,806)

(1) PEMEX previously reported 2007 Retirement, seniority premiums and other post-retirement benefit contributions and payments under Financing activities in the amount of Ps. (27,717,544). PEMEX has corrected such amount under Operating activities. PEMEX has also, within Operating activities, broken out the line item Accounts payable and accrued liabilities to separately disclose the amounts of its retirement, seniority premiums and other post-retirement benefit contributions and payments during 2006 and 2005.

These changes to the previously reported amounts are summarized in the table below:

	2007	
	As Previously Reported	As Corrected
Cash flow provided by (used in) operating activities	Ps. 209,129,353	Ps. 181,411,809
Cash flow (used in) provided by financing activities	(Ps. 94,190,935)	(Ps. 66,473,391)

F-75

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(m) Recently issued accounting standards

In September 2006, the FASB issued SFAS 157, “Fair Value Measurement”. SFAS 157 defines fair value, establishes a framework for the measurement of fair value, and enhances disclosure about fair value measurements. SFAS does not require any new fair value measurements. SFAS 157 is effective for fair value measurements already required or permitted by other standards for fiscal years beginning after November 15, 2007. PEMEX is required to adopt SFAS 157 beginning on January 1, 2008. SFAS 157 is required to be applied prospectively, except for certain financial instruments. Any transition adjustment will be recognized as an adjustment to opening retained earnings in the year of adoption. In November 2007, the FASB proposed a one-year deferral of SFAS 157’s fair-value measurement requirements for nonfinancial assets and liabilities that are not required or permitted to be measured at fair value on a recurring basis. PEMEX is currently evaluating the impact of its adoption of SFAS 157 on its results of operations and financial position.

In December 2007, the FASB issued FASB Statement No. 141R, “Business Combinations” (“SFAS 141R”) and FASB Statement No. 160, “Noncontrolling Interests in Consolidated Financial Statements—an amendment to ARB No. 51” (“SFAS 160”). SFAS 141R and SFAS 160 require most identifiable assets, liabilities, noncontrolling interests, and goodwill acquired in a business combination to be recorded at “full fair value” and require noncontrolling interests (previously referred to as minority interests) to be reported as a component of equity, which changes the accounting for transactions with noncontrolling interest holders. Both statements are effective for periods beginning on or after December 15, 2008, and earlier adoption is prohibited. SFAS 141R will be applied to business combinations occurring after the effective date. SFAS 160 will be applied prospectively to all noncontrolling interests, including any that arose before the effective date. PEMEX is currently evaluating the impact of adopting SFAS 141R and SFAS 160 on its results of operations and financial position.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities — including an amendment of FASB Statement No. 115” (“SFAS 159”). SFAS 159 gives PEMEX the irrevocable option to carry most financial statements assets and liabilities at fair value that are not currently required to be measured at fair value. If the fair value option is selected, changes in fair value would be recorded in earnings at each subsequent reporting date. SFAS 159 is effective for PEMEX’s 2008 fiscal year. PEMEX is currently evaluating the impact that the adoption of this statement could have on its financial condition, results of operations and cash flows.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB SFAS No. 133” (“SFAS 133”). SFAS 133 changes the disclosure requirements for derivative instruments and hedging activities by requiring the entities to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance and cash flows. This statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Early adoption is permitted. PEMEX is currently evaluating the impact of adopting SFAS 161 on its financial condition and results of operations.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

(n) Accounting for Buy/Sell Contracts

In the first quarter of 2005, the United States Securities and Exchange Commission (“SEC”) issued comment letters to companies in the oil and gas industry requesting disclosure of information related to the accounting for buy/sell contracts. Under a buy/sell contract, a company agrees to buy a specific quantity and quality of a commodity to be delivered at a specific location while simultaneously agreeing to sell a specified quantity and quality of a commodity at a different location to the same counterparty. Physical delivery occurs for each side of the transaction, and the risk and reward of ownership are evidenced by title transfer, assumption of environmental risk, transportation scheduling, credit risk and risk of nonperformance by the counterparty. Both parties settle each side of the buy/sell contract through separate invoicing.

The SEC raised the issue as to whether the accounting for buy/sell contracts should be shown net on the income statement and accounted for under the provisions of Accounting Principles Board (“APB”) Opinion No. 29, “Accounting for Nonmonetary Transactions” (“APB 29”). PEMEX understands that others in the oil and gas industry may report buy/sell transactions on a net basis in the income statement rather than gross.

The EITF considered this topic in Issue No. 04-13, “Accounting for Purchases and Sales of Inventory with the Same Counterparty” (“EITF 04-13”). At its September 2005 meeting, the EITF decided that two or more legally separate exchange transactions with the same counterparty, including buy/sell transactions, should be combined and considered as a single arrangement for purposes of applying APB 29 when the transactions were entered into “in contemplation” of one another. EITF 04-13 was ratified by the FASB in September 2005, and is effective for new arrangements, or modifications or renewals of existing arrangements, entered into as of April 1, 2006, which was the effective date for PEMEX’s adoption of this standard. During the years ended in December 31, 2007, 2006 and 2005, PEMEX did not enter into any arrangement that would be considered a buy/sell contract under EITF 04-13.

(o) Deferred income taxes

PEMEX follows the provisions of the revised Statement D-4, “Accounting Treatment of Income Tax, Asset Tax and Employee Profit Sharing,” for Mexican FRS purposes. Accounting for income taxes in accordance with this statement is similar to accounting for income taxes in accordance with U.S. GAAP SFAS 109, “Accounting for Income Taxes” (“SFAS 109”).

As described in Note 18, during 2005, a new fiscal regime applicable to PEMEX and its subsidiaries was enacted. Beginning January 1, 2006, certain subsidiary companies of PEMEX will be subject to the tax regime applicable to all other Mexican corporations. In general, Mexican companies are taxed based on pre-tax income at a statutory rate. The statutory rate for Mexico for 2006 was 29% and for 2007 was 28%. As a result of the change in fiscal regime in 2005, PEMEX began generating deferred income taxes.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

At December 31, 2007 and 2006, the primary components of the net deferred tax liability under U.S. GAAP consist of the following:

	<u>2007</u>	<u>2006</u>
Current deferred tax asset:		
Accounts and other receivables	Ps. 947,346	Ps. 1,364,303
Inventories	3,979,258	1,887,170
Accrued liabilities	245,505	383,263
Prepays and other current assets	45,405	218,420
Total current deferred tax asset	<u>5,217,514</u>	<u>3,853,156</u>
Less: current valuation allowance	<u>(4,799,664)</u>	<u>(3,339,648)</u>
Net current deferred tax asset	<u>Ps. 417,850</u>	<u>Ps. 513,508</u>
Current deferred tax liability:		
Prepays and other current assets	—	—
Total current deferred tax liability	<u>Ps. —</u>	<u>Ps. —</u>
Noncurrent deferred tax asset:		
Contingencies	Ps. 1,304,574	Ps. 1,466,308
Derivative financial instruments	—	—
Reserve for environmental costs	516,493	503,387
Property taxes	—	—
Tax loss carryforwards	653	8,370
Other assets	182,115	—
Fixed assets	5,189,973	7,951,927
Total noncurrent deferred tax asset	<u>7,193,808</u>	<u>9,929,992</u>
Less: noncurrent valuation allowance	<u>(6,617,685)</u>	<u>(8,606,622)</u>
Net noncurrent deferred tax asset	<u>Ps. 576,123</u>	<u>Ps. 1,323,370</u>
Noncurrent deferred tax liability:		
Derivative financial instruments	—	(649,728)
Fixed assets	(7,100,465)	(5,416,431)
Net noncurrent deferred tax liability	<u>(7,100,465)</u>	<u>(6,066,159)</u>
Total noncurrent deferred tax liability	<u>(6,524,342)</u>	<u>(4,742,789)</u>
Net deferred tax liability	<u>(Ps. 6,106,493)</u>	<u>(Ps. 4,229,281)</u>
Net deferred tax liability under U.S. GAAP	(Ps. 6,106,493)	(Ps. 4,229,281)
Net deferred tax liability under Mexican FRS	6,411,896	4,597,172
Net U.S. GAAP adjustments to the net deferred tax liability	<u>Ps. 305,403</u>	<u>Ps. 367,891</u>

(p) Asset retirement obligations

PEMEX's liability provisions recognized in the balance sheet represent obligations whose settlement will probably require the future use of estimated economic resources. These provisions have been recorded based on the present value of management's best estimate of future payments necessary to settle the liability. However, actual results could differ from the provisions recognized. No assets or trust funds have been established to satisfy these obligations.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

In March 2005, the FASB issued FASB Interpretation No. 47, “Accounting for Conditional Asset Retirement Obligations — An Interpretation of FASB Statement No. 143,” (“FIN 47”), which was adopted by PEMEX on December 31, 2005. FIN 47 clarifies that the phrase “conditional asset retirement obligation,” as used in SFAS 143, refers to a legal obligation to perform an asset retirement activity for which the timing and/or method of settlement are conditioned on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists as to the timing and/or method of settlement. Uncertainty about the timing and/or method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists. SFAS 143 acknowledges that, in some cases, sufficient information may not be available to reasonably estimate the fair value of an asset retirement obligation. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. The adoption of FIN 47 has not had a material impact on PEMEX’s financial position and results of operations.

The following table indicates the changes to PEMEX’s pre-tax asset retirement obligations in 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Balance at January 1	Ps. 16,027,309	Ps. 14,787,131
Liabilities incurred	1,338,248	1,789,002
Liabilities settled	—	—
Accretion expense	118,204	(36,911)
Inflation	(580,643)	(302,725)
Currency exchange gain	245,272	(72,542)
Revisions in estimated cash flows	—	(136,646)
Balance at December 31	<u>Ps. 17,148,390</u>	<u>Ps. 16,027,309</u>

NOTE 22—SUBSIDIARY GUARANTOR INFORMATION, PIDIREGAS LIABILITIES AND THE PEMEX PROJECT FUNDING MASTER TRUST (THE “MASTER TRUST”)

The following consolidating information presents condensed consolidating balance sheets at December 31, 2007 and 2006 and condensed consolidating statements of operations and cash flow for the years ended December 31, 2007, 2006 and 2005 of Petróleos Mexicanos, the Master Trust, Pemex-Exploration and Production, Pemex-Refining, Pemex-Gas and Basic Petrochemicals and the Non-Guarantor Subsidiaries (excluding the Master Trust).

These statements are prepared in conformity with Mexican FRS, including the recognition of inflation in accordance with Bulletin B-10, with one exception: for the purposes of the presentation of the subsidiary guarantor information, the Subsidiary Entities and Subsidiary Companies have been accounted for as investments under the equity method by Petróleos Mexicanos. Earnings of subsidiaries are therefore reflected in Petróleos Mexicanos’ investment account and earnings. The principal elimination entries eliminate Petróleos Mexicanos’ investment in subsidiaries and intercompany balances and transactions. Pemex-Exploration and Production, Pemex-Refining and Pemex-Gas and Basic Petrochemicals (collectively, the “Subsidiary Guarantors”) and Pemex-Petrochemicals are 100%-owned subsidiaries of Petróleos Mexicanos. Pemex-Petrochemicals, Pemex Finance and the Subsidiary Companies collectively comprise the non-guarantor subsidiaries (“Non-Guarantor Subsidiaries”). Petróleos Mexicanos’ guaranty of the indebtedness of the Master Trust is full

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

and unconditional. The guaranties by the Subsidiary Guarantors of Petróleos Mexicanos' guaranty of the Master Trust's payment obligations are full and unconditional and joint and several.

The Master Trust, a consolidated entity which is a Delaware statutory trust, was organized under the laws of Delaware on November 10, 1998. On December 31, 1998, PEMEX transferred all assets and liabilities related to PIDIREGAS for an amount equaling Ps. 12,471,156 (in nominal terms) to the Master Trust. The main objective of the Master Trust is to administer financial resources related to PIDIREGAS, such financial resources being designated by PEMEX for that purpose, by assuming payment obligations under contracts relating to PIDIREGAS and acting as the borrower under financing arrangements for PIDIREGAS.

Under an Assignment and Indemnity Agreement dated November 10, 1998, among Petróleos Mexicanos, the Master Trust and the Subsidiary Guarantors, Petróleos Mexicanos and the Subsidiary Guarantors have certain obligations to the Master Trust with respect to the liabilities incurred by the Master Trust in connection with PIDIREGAS. These obligations include:

- (i) the obligation of Petróleos Mexicanos to guarantee the repayment of the debt obligations undertaken by the Master Trust to finance PIDIREGAS;
- (ii) the obligation of Petróleos Mexicanos and the Subsidiary Guarantor which is sponsoring the relevant PIDIREGAS to make such payments to the Master Trust as may be necessary for the Master Trust to fulfill its payment obligations in respect of any financing the Master Trust has entered into in connection with such project; and
- (iii) the joint and several obligation of Petróleos Mexicanos and each of the aforementioned Subsidiary Guarantors to indemnify the Master Trust with respect to any liability incurred by the Master Trust in connection with PIDIREGAS.

The Master Trust is consolidated in the financial statements of PEMEX for each of the periods presented in accordance with consolidation principles detailed in Mexican FRS Bulletin B-8 "Consolidated and Combined Financial Statements and Valuation of Permanent Investments in Stocks." In accordance with U.S. accounting principles, the Master Trust is a special purpose entity requiring consolidation in the financial statements as it does not meet non-consolidation criteria as specified in U.S. accounting literature.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

The following table sets forth, as of the date of this report, the principal amount outstanding of the registered debt securities issued by Master Trust, for which Petróleos Mexicanos is the Guarantor and Pemex—Exploration and Production, Pemex—Refining and Pemex—Gas and Basic Petrochemicals are the Subsidiary Guarantors:

Table 1: Registered Debt Securities of the Master Trust

Security	Issuer	Guarantor	Principal Amount Outstanding
5.75% Notes due 2015	Master Trust	Petróleos Mexicanos	U.S.\$ 234,372
6.125% Notes due 2008	Master Trust	Petróleos Mexicanos	281,400
6.625% Guaranteed Bonds due 2035	Master Trust	Petróleos Mexicanos	1,249,000
7.375% Notes due 2014	Master Trust	Petróleos Mexicanos	362,995
7.875% Notes due 2009	Master Trust	Petróleos Mexicanos	797,727
8.00% Notes due 2011	Master Trust	Petróleos Mexicanos	182,174
8.625% Bonds due 2022	Master Trust	Petróleos Mexicanos	160,245
8.625% Bonds due 2023	Master Trust	Petróleos Mexicanos	106,507
9.125% Notes due 2010	Master Trust	Petróleos Mexicanos	552,855
9.25% Guaranteed Bonds due 2018	Master Trust	Petróleos Mexicanos	107,109
9.375% Guaranteed Notes due 2008	Master Trust	Petróleos Mexicanos	294,775
9.50% Guaranteed Bonds due 2027	Master Trust	Petróleos Mexicanos	219,217

The following table sets forth, as of the date of this report, the principal amount outstanding of the registered debt securities issued by Petróleos Mexicanos, and guaranteed by Pemex Exploration and Production, Pemex Refining and Pemex Gas and Basic Petrochemicals:

Table 2: Registered Debt Securities of Petróleos Mexicanos

Security	Issuer	Guarantor	Principal Amount Outstanding
9.25% Global Guaranteed Bonds due 2018	Petróleos Mexicanos	Pemex Exploration and Production, Pemex Refining and Pemex Gas and Basic Petrochemicals	U.S.\$ 9,296
9.375% Guaranteed Notes due 2008	Petróleos Mexicanos	Pemex Exploration and Production, Pemex Refining and Pemex Gas and Basic Petrochemicals	99,859
9.50% Global Guaranteed Bonds due 2027	Petróleos Mexicanos	Pemex Exploration and Production, Pemex Refining and Pemex Gas and Basic Petrochemicals	102,149

The Master Trust does not guaranty debt securities issued by Petróleos Mexicanos.

The significant differences between Mexican and U.S. GAAP as they affect PEMEX are described in Note 21. The following also presents the reconciliation of equity to U.S. GAAP as of December 31, 2007 and

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

2006 and the reconciliation of income to U.S. GAAP for the three years ended December 31, 2007 for each of Petróleos Mexicanos, the Master Trust, the Subsidiary Guarantors and the Non-Guarantor Subsidiaries. The following reconciliation to U.S. GAAP does not include the reversal of Mexican FRS inflation accounting adjustments, as these adjustments represent a comprehensive measure of the effects of price level changes in the inflationary Mexican economy, which is considered a more meaningful presentation than historical cost-based financial reporting for both Mexican and U.S. accounting purposes.

As of December 31, 2007, Petróleos Mexicanos, the Master Trust, Fideicomiso F/163 and RepCon Lux are the only entities of PEMEX authorized to contract debt with debt outstanding as of that date, and thus all guaranteed debt is issued by these entities. The guarantees of the Subsidiary Guarantors are full and unconditional and joint and several. PEMEX's management has not presented separate financial statements for the Subsidiary Guarantors because it has determined that such information is not material to investors.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

BALANCE SHEET

As of December 31, 2007

	Petróleos Mexicanos ⁽¹⁾	Master Trust ⁽¹⁾	Subsidiary Guarantors ⁽¹⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
ASSETS						
Current assets:						
Cash and cash equivalents	Ps. 121,386,348	Ps. 19,201,904	Ps. 3,672,809	Ps. 26,736,179	Ps. —	Ps. 170,997,240
Accounts, notes receivable and other, net and derivative financial instruments	18,262,729	3,883,155	86,304,727	55,969,800	—	164,420,411
Accounts receivable-intercompany	123,671,752	73,310,725	778,048,681	95,832,373	(1,070,863,531)	—
Inventories, net	313,283	—	77,582,304	15,247,549	—	93,143,136
Total current assets	263,634,112	96,395,784	945,608,521	193,785,901	(1,070,863,531)	428,560,787
Long-term receivables — intercompany	633,228,579	470,050,109	16,380,552	98,550,013	(1,218,209,253)	—
Investments in shares	368,950,383	—	1,595,297	30,312,679	(367,795,005)	33,063,354
Other investments	213,432,941	—	—	—	(213,432,941)	—
Properties and equipment, net	8,070,672	—	770,025,355	15,749,426	—	793,845,453
Intangible asset derived from the actuarial computation of labor obligations	11,124,683	—	54,913,164	5,970,988	—	72,008,835
Other assets	954,213	—	809,713	1,038,251	—	2,802,177
Total assets	Ps.1,499,395,583	Ps. 566,445,893	Ps.1,789,332,602	Ps. 345,407,258	(Ps. 2,870,300,730)	Ps.1,330,280,606
LIABILITIES						
Current liabilities:						
Current portion of long-term debt	Ps. 6,603,093	Ps. 62,355,642	Ps. 2,337,399	Ps. 4,753,994	Ps. —	Ps. 76,050,128
Accounts payable — intercompany	728,424,666	6,605,943	219,812,679	68,108,752	(1,022,952,040)	—
Other current liabilities	3,816,030	13,457,162	151,890,502	44,250,030	—	213,413,724
Total current liabilities	738,843,789	82,418,747	374,040,580	117,112,776	(1,022,952,040)	289,463,852
Long-term debt	8,676,110	289,721,950	5,160,995	121,269,417	—	424,828,472
Long-term payables-intercompany	623,510,449	194,105,101	648,882,879	13,046,260	(1,479,544,689)	—
Reserve for retirement payments, pensions, seniority premiums, dismantlement and abandonment activities, sundry creditors, and others	79,229,875	200,095	433,390,324	53,260,127	—	566,080,421
Total Liabilities	1,450,260,223	566,445,893	1,461,474,778	304,688,580	(2,502,496,729)	1,280,372,745
EQUITY						
EQUITY	49,135,360	—	327,857,824	40,718,678	(367,804,001)	49,907,861
Total liabilities and equity	Ps.1,499,395,583	Ps. 566,445,893	Ps.1,789,332,602	Ps. 345,407,258	(Ps. 2,870,300,730)	Ps.1,330,280,606

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PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

U.S. GAAP RECONCILIATION OF EQUITY

For the year ended December 31, 2007

	Petróleos Mexicanos ⁽¹⁾	Master Trust ⁽¹⁾	Subsidiary Guarantors ⁽¹⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
	Ps.	Ps.	Ps.	Ps.	(Ps.)	Ps.
Equity under Mexican FRS	49,135,360	—	327,857,824	40,718,678	(367,804,001)	49,907,861
U.S. GAAP adjustments:						
Exploration and drilling costs	—	—	12,518,420	—	—	12,518,420
Pensions and seniority premiums	(215,898)	—	(4,721,584)	(609,460)	—	(5,546,942)
Additional Pension liability	(9,035,148)	—	(52,271,893)	(6,408,612)	—	(67,715,653)
Post-retirement benefits	(4,792,303)	—	(25,951,048)	(3,444,001)	—	(34,187,352)
Effect in equity of labor obligation	(13,666,071)	—	(69,621,670)	(8,536,420)	—	(91,824,161)
Accrued vacation	(88,199)	—	(483,805)	(64,088)	—	(636,092)
Fixed asset adjustments:						
Capitalized gains (losses) of hedging financial instruments, net	—	—	2,883,974	—	—	2,883,974
Capitalization of interest, net	39,891	—	(5,233,589)	411,091	—	(4,782,607)
Impairment, net	—	—	(22,615,830)	(3,948,416)	—	(26,564,246)
Profit in inventory	—	—	(26,755,771)	—	—	(26,755,771)
Deferred income taxes	—	—	305,403	—	—	305,403
Advance payment of minimum guaranteed dividends (APMGD)	(4,270,225)	—	—	—	—	(4,270,225)
Reclassification of Pemex Finance net income to minority interest	—	—	—	(1,415,775)	—	(1,415,775)
Investments in subsidiaries ⁽²⁾	(215,963,074)	—	—	—	215,963,074	—
Total U.S. GAAP adjustments, net	(247,991,027)	—	(191,947,393)	(24,015,681)	215,963,074	(247,991,027)
Equity (Deficit) under U.S. GAAP	<u>Ps. (198,855,667)</u>	<u>Ps. —</u>	<u>Ps. 135,910,431</u>	<u>Ps. 16,702,997</u>	<u>(Ps. 151,840,927)</u>	<u>(Ps. 198,083,166)</u>

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(2) Reflects adjustment to investment balances of subsidiaries as a result of applying U.S. GAAP adjustments of such subsidiaries.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION
BALANCE SHEET
As of December 31, 2006

	<u>Petróleos Mexicanos⁽¹⁾</u>	<u>Master Trust⁽¹⁾</u>	<u>Subsidiary Guarantors⁽¹⁾</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX Consolidated</u>
ASSETS						
Current assets:						
Cash and cash equivalents	Ps. 133,079,873	Ps. 22,681,704	Ps. 2,977,334	Ps. 37,037,546	Ps. —	Ps. 195,776,457
Accounts, notes receivable and other, net and derivative financial instruments	41,568,203	5,393,950	51,748,849	42,841,939	—	141,552,941
Accounts receivable-intercompany	51,127,882	40,622,344	685,098,180	68,332,370	(845,180,776)	—
Inventories, net	437,851	7,942	51,439,914	10,178,091	—	62,063,798
Total current assets	226,213,809	68,705,940	791,264,277	158,389,946	(845,180,776)	399,393,196
Long-term receivables — intercompany	615,065,974	405,184,550	21,331,177	100,448,654	(1,142,030,355)	—
Investments in shares	405,264,102	—	2,455,759	29,117,822	(404,076,737)	32,760,946
Other investments	56,697,030	—	—	—	(56,697,030)	—
Properties and equipment, net	8,423,458	—	712,658,610	16,113,389	—	737,195,457
Intangible asset derived from the actuarial computation of labor obligations	11,931,936	—	58,163,091	6,400,106	—	76,495,133
Other assets	1,282,491	—	1,139,339	1,753,862	—	4,175,692
Total assets	<u>Ps. 1,324,878,800</u>	<u>Ps. 473,890,490</u>	<u>Ps. 1,587,012,253</u>	<u>Ps. 312,223,779</u>	<u>(Ps. 2,447,984,898)</u>	<u>Ps. 1,250,020,424</u>
LIABILITIES						
Current liabilities:						
Current portion of long-term debt	Ps. 12,844,824	Ps. 32,662,476	Ps. 1,365,763	Ps. 19,367,215	—	Ps. 66,240,278
Accounts payable — intercompany	634,537,523	4,565,436	180,187,172	25,882,770	(845,172,901)	—
Other current liabilities	4,389,487	12,814,454	55,490,541	37,379,369	—	110,073,851
Total current liabilities	651,771,834	50,042,366	237,043,476	82,629,354	(845,172,901)	176,314,129
Long-term debt	15,805,453	373,149,214	1,201,152	134,319,423	—	524,475,242
Long-term payables-intercompany	545,477,446	50,698,910	582,599,564	19,951,468	(1,198,727,388)	—
Reserve for retirement payments, pensions, seniority premiums, dismantlement and abandonment activities, sundry creditors, and others	69,199,554	—	391,368,856	47,207,017	—	507,775,427
Total Liabilities	1,282,254,287	473,890,490	1,212,213,048	284,107,262	(2,043,900,289)	1,208,564,798
EQUITY	42,624,513	—	374,799,205	28,116,517	(404,084,609)	41,455,626
Total liabilities and equity	<u>Ps. 1,324,878,800</u>	<u>Ps. 473,890,490</u>	<u>Ps. 1,587,012,253</u>	<u>Ps. 312,223,779</u>	<u>(Ps. 2,447,984,898)</u>	<u>Ps. 1,250,020,424</u>

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION
U.S. GAAP RECONCILIATION OF EQUITY
For the year ended December 31, 2006

	<u>Petróleos Mexicanos⁽¹⁾</u>	<u>Master Trust⁽¹⁾</u>	<u>Subsidiary Guarantors⁽¹⁾</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX Consolidated</u>
Equity under Mexican FRS	Ps. 42,624,513	Ps. —	Ps.374,799,205	Ps. 28,116,517	(Ps.404,084,609)	Ps. 41,455,626
U.S. GAAP adjustments:						
Exploration and drilling costs	—	—	13,889,293	—	—	13,889,293
Pensions and seniority premiums	(526,576)	—	(6,518,979)	(829,823)	—	(7,875,378)
Additional Pension liability	722,398	—	4,215,207	489,019	—	5,426,624
Post-retirement benefits	(5,391,421)	—	(29,003,251)	(3,818,236)	—	(38,212,908)
Accrued vacation	(81,540)	—	(449,182)	(59,561)	—	(590,283)
Fixed asset adjustments:						
Capitalized gains (losses) or derivative financial instruments, net	—	—	3,061,308	—	—	3,061,308
Capitalization of interests, net	27,020	—	(8,493,416)	173,829	—	(8,292,567)
Impairment, net	—	—	(25,765,627)	(4,143,136)	—	(29,908,763)
Depreciation convention	(17,692)	—	(736,698)	(28,754)	—	(783,144)
Derivative financial instruments	613	—	8,146,456	2,637	—	8,149,706
Profit in inventory	—	—	(7,836,552)	—	—	(7,836,552)
Deferred income taxes	—	—	367,891	—	—	367,891
Advance payment of minimum guaranteed dividends	(268,990)	—	—	—	—	(268,990)
Reclassification of Pemex Finance net income to minority interest	—	—	—	(1,464,681)	—	(1,464,681)
Investments in subsidiaries ⁽²⁾	(58,802,256)	—	—	—	58,802,256	—
Total U.S. GAAP adjustments, net	<u>(64,338,444)</u>	<u>—</u>	<u>(49,123,550)</u>	<u>(9,678,706)</u>	<u>58,802,256</u>	<u>(64,338,444)</u>
Equity (Deficit) under U.S. GAAP	<u>(Ps. 21,713,931)</u>	<u>Ps. —</u>	<u>Ps.325,675,655</u>	<u>Ps. 18,437,811</u>	<u>(Ps.345,282,353)</u>	<u>(Ps. 22,882,818)</u>

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(2) Reflects adjustment to investment balances of subsidiaries as a result of applying U.S. GAAP adjustments of such subsidiaries

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION
STATEMENT OF INCOME

For the year ended December 31, 2007

	Petróleos Mexicanos ⁽¹⁾	Master Trust ⁽¹⁾	Subsidiary Guarantors ⁽¹⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
Net sales	Ps. 34,453,424	Ps. —	Ps. 1,607,811,952	Ps. 814,111,011	(Ps. 1,321,401,568)	Ps. 1,134,974,819
Services income	27,491	—	—	1,852,541	(819,423)	1,060,609
Total sales revenues	34,480,915	—	1,607,811,952	815,963,552	(1,322,220,991)	1,136,035,428
Costs of sales	235,627	—	932,208,069	815,588,389	(1,287,366,343)	460,665,742
Gross income	34,245,288	—	675,603,883	375,163	(34,854,648)	675,369,686
General expenses:						
Transportation and distribution expenses	—	—	23,561,036	1,237,503	—	24,798,539
Administrative expenses	32,982,205	25,934	51,611,895	8,684,722	(33,164,291)	60,140,465
Total general expenses	32,982,205	25,934	75,172,931	9,922,225	(33,164,291)	84,939,004
Operating income	1,263,083	(25,934)	600,430,952	(9,547,062)	(1,690,357)	590,430,682
Other (expenses) revenues, net	(321,083)	—	82,028,474	(6,439,786)	7,751,405	83,019,010
Comprehensive financing result (cost) income	10,119,811	(25,786,670)	(30,254,918)	(4,995,428)	30,870,618	(20,046,587)
Equity participation in subsidiaries	(29,969,811)	—	—	12,842,972	22,671,893	5,545,054
Capitalization of Master Trust operations and others	—	25,812,604	—	3,810,272	(29,622,876)	—
(Loss) Income before taxes and duties	(18,908,000)	—	652,204,508	(4,329,032)	29,980,683	658,948,159
Taxes and duties	662,486	—	672,933,568	3,659,674	—	677,255,728
Net (loss) income for the year	(Ps. 19,570,486)	Ps. —	(Ps. 20,729,060)	(Ps. 7,988,706)	Ps. 29,980,683	(Ps. 18,307,569)

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

U.S. GAAP RECONCILIATION OF INCOME

For the year ended December 31, 2007

	<u>Petróleos Mexicanos⁽¹⁾</u>	<u>Master Trust⁽¹⁾</u>	<u>Subsidiary Guarantors⁽¹⁾</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX Consolidated</u>
Net (loss) income under Mexican FRS	(Ps. 19,570,486)	Ps. —	(Ps. 20,729,060)	(Ps. 7,988,706)	Ps.29,980,683	(Ps. 18,307,569)
U.S. GAAP adjustments:						
Exploration and drilling costs	—	—	(1,370,873)	—	—	(1,370,873)
Pension and seniority premiums	310,678	—	1,797,395	220,363	—	2,328,436
Post-retirement benefits	599,118	—	3,052,203	374,236	—	4,025,557
Accrued vacation	(6,659)	—	(34,623)	(4,527)	—	(45,809)
Fixed asset adjustments:						
Capitalized gains of hedging financial instruments, net	—	—	(177,334)	—	—	(177,334)
Capitalization of interest, net	12,871	—	3,259,826	237,263	—	3,509,960
Impairment, net	—	—	3,149,798	194,719	—	3,344,517
Depreciation convention	17,692	—	736,700	28,752	—	783,144
Derivative financial instruments	(613)	—	(8,146,456)	(2,637)	—	(8,149,706)
Profit in inventory	—	—	(18,919,219)	—	—	(18,919,219)
Available-for-sale securities	246,258	—	—	—	—	246,258
Deferred income taxes	—	—	(62,488)	—	—	(62,488)
Effect of inflation accounting on U.S. GAAP adjustment	140,863	—	16,163	2,113	—	159,139
Reclassification of Pemex Finance net income to minority interest	—	—	—	(6,089)	—	(6,089)
Investments in Subsidiaries	(15,654,715)	—	—	—	15,654,715	—
Total U.S. GAAP adjustments	<u>(14,334,507)</u>	<u>—</u>	<u>(16,698,908)</u>	<u>1,044,193</u>	<u>15,654,715</u>	<u>(14,334,507)</u>
Net (loss) income for the year	<u>(Ps. 33,904,993)</u>	<u>Ps. —</u>	<u>(Ps. 37,427,968)</u>	<u>(Ps. 6,944,513)</u>	<u>Ps.45,635,398</u>	<u>(Ps. 32,642,076)</u>

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

STATEMENT OF INCOME

For the year ended December 31, 2006

	Petróleos Mexicanos ⁽¹⁾	Master Trust ⁽¹⁾	Subsidiary Guarantors ⁽¹⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
Net sales	Ps.26,436,747	Ps. —	Ps.1,564,963,881	Ps.711,981,523	Ps.(1,200,948,230)	Ps.1,102,433,921
Services income	—	—	—	1,707,386	(631,439)	1,075,947
Total revenues	26,436,747	—	1,564,963,881	713,688,909	(1,201,579,669)	1,103,509,868
Costs of sales	209,910	—	880,664,298	713,123,190	(1,175,739,188)	418,258,210
Gross income	26,226,837	—	684,299,583	565,719	(25,840,481)	685,251,658
Transportation and distribution expenses	—	—	23,785,565	1,136,091	—	24,921,656
Administrative expenses	31,117,062	31,114	42,096,348	8,135,270	(25,327,021)	56,052,773
Total costs and operating expenses	31,117,062	31,114	65,881,913	9,271,361	(25,327,021)	80,974,429
Operating income	(4,890,225)	(31,114)	618,417,670	(8,705,642)	(513,460)	604,277,229
Other (expenses) revenues net	(671,689)	—	60,257,979	795,886	831,357	61,213,533
Comprehensive financing result (cost) income	17,621,942	(10,567,511)	(32,065,634)	(7,121,106)	8,285,684	(23,846,625)
Equity participation in subsidiaries	36,579,228	—	—	10,041,050	(36,546,701)	10,073,577
Capitalization of Master Trust operations and others	—	10,598,625	—	(1,993,908)	(8,604,717)	—
Income (loss) before taxes and duties	48,639,256	—	646,610,015	(6,983,720)	(36,547,837)	651,717,714
Taxes and duties	360,447	—	599,735,358	4,668,704	—	604,764,509
Net income (loss) for the year	<u>Ps.48,278,809</u>	<u>Ps. —</u>	<u>Ps. 46,874,657</u>	<u>Ps. (11,652,424)</u>	<u>Ps. (36,547,837)</u>	<u>Ps. 46,953,205</u>

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

U.S. GAAP RECONCILIATION OF INCOME

For the year ended December 31, 2006

	<u>Petróleos Mexicanos⁽¹⁾</u>	<u>Master Trust⁽¹⁾</u>	<u>Subsidiary Guarantors⁽¹⁾</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX Consolidated</u>
Net income (loss) under Mexican FRS	Ps.48,278,809	Ps. —	Ps.46,874,657	(Ps. 11,652,424)	(Ps. 36,547,837)	Ps.46,953,205
U.S. GAAP adjustments:						
Exploration and drilling costs	—	—	(1,498,801)	—	—	(1,498,801)
Pension and seniority premiums	258,219	—	1,506,708	174,798	—	1,939,725
Post-retirement benefits	730,119	—	3,845,768	466,667	—	5,042,554
Accrued vacation	(2,987)	—	(15,532)	(2,030)	—	(20,549)
Fixed asset adjustments:						
Capitalized gains of hedging financial instruments, net	—	—	3,928,429	—	—	3,928,429
Capitalization of interest, net	14,470	—	2,439,576	340,348	—	2,794,394
Impairment, net	—	—	3,546,475	432,091	—	3,978,566
Depreciation convention	17,692	—	736,700	28,752	—	783,144
Derivative financial instruments	(209,153)	—	287,164	—3,338	—	74,673
Profit in inventory	—	—	(4,156,613)	—	—	(4,156,613)
Available-for-sale securities	(2,995,342)	—	—	—	—	(2,995,342)
Deferred income taxes	—	—	(74,777)	—	—	(74,777)
Effect of inflation accounting on U.S. GAAP Adjustment	8,891	—	17,453	2,283	—	28,627
Reclassification of Pemex Finance net income to minority interest	—	—	—	(54,789)	—	(54,789)
Investments in Subsidiaries	<u>11,947,332</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>(11,947,332)</u>	<u>—</u>
Total U.S. GAAP adjustments	<u>9,769,241</u>	<u>—</u>	<u>10,562,550</u>	<u>1,384,782</u>	<u>(11,947,332)</u>	<u>9,769,241</u>
Net income (loss) for the year	<u>Ps.58,048,050</u>	<u>Ps. —</u>	<u>Ps.57,437,207</u>	<u>(Ps. 10,267,642)</u>	<u>(Ps. 48,495,169)</u>	<u>Ps.56,722,446</u>

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

STATEMENT OF INCOME

For the year ended December 31, 2005

	Petróleos Mexicanos ⁽¹⁾	Master Trust ⁽¹⁾	Subsidiary Guarantors ⁽¹⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
Net sales	Ps. 24,061,252	Ps. —	Ps. 1,430,157,491	Ps. 593,717,816	Ps. (1,045,330,294)	Ps. 1,002,606,265
Services income		—		1,875,001	(650,193)	1,224,808
Total sales revenues	24,061,252	—	1,430,157,491	595,592,817	(1,045,980,487)	1,003,831,073
Costs of sales	144,345	—	812,102,068	617,226,094	(1,039,528,608)	389,943,899
Gross income	23,916,907		618,055,423	(21,633,277)	(6,451,879)	613,887,174
General expenses:						
Transportation and distribution expenses	—	—	22,490,759	1,165,151	—	23,655,910
Administrative expenses	25,656,966	27,590	46,231,359	5,381,815	(26,769,846)	50,527,884
Total costs and operating expenses	25,656,966	27,590	68,722,118	6,546,966	(26,769,846)	74,183,794
Operating income	(1,740,059)	(27,590)	549,333,305	(28,180,243)	20,317,967	539,703,380
Other (expenses) revenues, net	(1,096,609)	—	(2,816,900)	21,144,400	(14,334,497)	2,896,394
Comprehensive financing result (cost) income	141,280	(4,114,555)	7,422,464	(12,722,733)	4,437,453	(4,836,091)
Equity participation in subsidiaries	(79,370,808)	—	—	6,004,200	82,025,273	8,658,665
Capitalization of Master Trust operations and others	—	4,142,145	—	6,280,036	(10,422,181)	—
(Loss) income before taxes and duties, special tax on production and services (IEPS tax) and cumulative effect of adoption of new accounting standards	(82,066,196)	—	553,938,869	(7,474,340)	82,024,015	546,422,348
Taxes and duties	—	—	622,694,255	4,180,207	—	626,874,462
Cumulative effect of adoption of new accounting standards	(481,068)	—	(1,241,427)	(183,373)	—	(1,905,868)
Net (loss) income for the year	Ps. (82,547,264)	Ps. —	Ps. (69,996,813)	Ps. (11,837,920)	Ps. 82,024,015	Ps. (82,357,982)

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

U.S. GAAP RECONCILIATION OF INCOME

For the year ended December 31, 2005

	<u>Petróleos Mexicanos⁽¹⁾</u>	<u>Master Trust⁽¹⁾</u>	<u>Subsidiary Guarantors⁽¹⁾</u>	<u>Non-Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX Consolidated</u>
Net (loss) income under Mexican FRS	(Ps.82,547,264)	Ps. —	(Ps. 69,996,813)	(Ps. 11,837,920)	Ps. 82,024,015	(Ps. 82,357,982)
U.S. GAAP adjustments:						
Exploration and drilling costs	—	—	(1,549,819)	—	—	(1,549,819)
Pension and seniority premiums	161,589	—	757,723	93,145	—	1,012,457
Post-retirement benefits	437,766	—	2,641,111	296,343	—	3,375,220
Accrued vacation	(2,343)	—	(12,697)	(1,672)	—	(16,712)
Fixed asset adjustments:						
Capitalized gains (losses) of hedging financial instruments, net	—	—	(8,445,996)	—	—	(8,445,996)
Capitalization of interests, net	12,550	—	1,660,006	255,716	—	1,928,272
Impairment, net	—	—	2,381,679	3,865,308	—	6,246,987
Depreciation convention	9,848	—	758,517	14,779	—	783,144
Derivative financial instruments	(833,939)	(4,214,796)	5,333,327	746,281	—	1,030,873
Profit in inventory	—	—	(2,776,119)	—	—	(2,776,119)
Available-for-sale securities	(830,179)	—	—	—	—	(830,179)
Deferred income taxes	—	—	442,668	—	—	442,668
Effect of inflation accounting on U.S. GAAP adjustment	190,371	—	14,586	1,923	—	206,880
Reclassification of Pemex Finance net income to minority interest	—	—	—	1,159,233	—	1,159,233
Investments in subsidiaries	3,421,246	—	—	—	(3,421,246)	—
Total U.S. GAAP adjustments	<u>2,566,909</u>	<u>(4,214,796)</u>	<u>1,204,986</u>	<u>6,431,056</u>	<u>(3,421,246)</u>	<u>2,566,909</u>
Net (loss) income for the year	<u>(Ps.79,980,355)</u>	<u>(Ps. 4,214,796)</u>	<u>(Ps. 68,791,827)</u>	<u>Ps. (5,406,864)</u>	<u>Ps. 78,602,769</u>	<u>(Ps. 79,791,073)</u>

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PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION
STATEMENT OF CASH FLOW⁽¹⁾

For the year ended December 31, 2007

	Petróleos Mexicanos ⁽²⁾	Master Trust ⁽²⁾	Subsidiary Guarantors ⁽²⁾	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
Operating activities						
Net income (loss) for the year	(Ps. 19,570,485) Ps.	—	(Ps. 20,729,059)	(Ps. 7,988,708)	(Ps. 29,980,683)	(Ps. 18,307,569)
Adjustments to reconcile net income (loss) to cash provided by operating activities						
Depreciation and amortization	639,866	—	70,860,006	1,091,846	—	72,591,718
Reserve for retirement payments, pensions and seniority premiums	12,742,593	—	64,195,411	8,368,862	—	85,306,866
Loss on disposal of fixed assets	33,101	—	9,752,826	265,512	—	10,051,439
Allowance for uncollectible trade accounts	(111)	—	(1,039,524)	(46,722)	—	(1,086,357)
Allowance for decline in the value of inventory	(46,625)	—	(94,928)	(45,151)	—	(186,704)
Conversion effect	—	—	—	—	—	—
Foreign exchange loss (gain)	658,970	3,668,150	—	(8,656)	—	4,318,464
Accrued interest	(338,113)	4,193,183	24,426	727,893	—	4,607,389
Equity in earning in investees less dividend received and other	29,980,683	—	—	(5,533,058)	(29,980,683)	(5,533,058)
Gain from monetary position	(11,040,864)	—	(3,469,158)	1,643,735	—	(12,866,287)
Deferred income taxes	—	—	1,867,292	27,414	—	1,894,706
Changes in operating assets and liabilities						
Accounts and notes receivable	21,799,646	1,315,383	(35,391,122)	(13,975,332)	—	(26,251,425)
Inter-company changes and deductions	372,417,508	2,375,374	(230,977,862)	17,875,996	(161,691,016)	—
Inventories	155,330	7,654	(10,154,825)	(4,659,156)	—	(14,650,997)
Other assets	281,816	—	288,350	649,381	—	1,219,547
Accounts payable and accrued liabilities ⁽³⁾	(668,839)	1,307,046	96,944,710	8,870,377	—	106,453,294
Retirement, seniority premiums and other post-retirement benefits contributions and payments ⁽³⁾	(4,951,499)	—	(21,412,162)	(1,353,883)	—	(27,717,544)
Cash flows provided by (used in) operating activities	402,092,977	12,866,790	(79,335,619)	5,910,350	(161,691,016)	179,843,482
Investing activities:						
Increase in fixed assets, net	(331,786)	—	(131,384,646)	(986,862)	—	(132,703,294)
Inter-company (increase) decrease in investments	(187,467,741)	(113,704,714)	161,051,930	(5,397,631)	145,518,156	—
Investments in Subsidiaries	(3,297,964)	—	771,494	3,283,315	889,766	1,646,611
Cash flows (used in) provided by investing activities	(191,097,491)	(113,704,714)	30,438,778	(3,101,178)	146,407,922	(131,056,683)
Financing Activities⁽¹⁾						
Proceeds from long term financing	51,509,770	59,731,700	6,316,360	—	—	117,557,830
Financing payments	(64,163,753)	(106,625,310)	(1,316,313)	(22,823,340)	—	(194,928,716)
Inter-company (decrease) increase in financing	(216,111,281)	145,073,451	44,700,132	10,163,426	16,174,272	—
Increase in equity of subsidiary entities	11,160,824	—	—	—	—	11,160,824
Minimum guaranteed dividends paid to the Mexican Government	(263,329)	—	—	891,178	(891,178)	(263,329)
Cash flows (used in) provided by financing activities	(217,867,769)	98,179,841	49,700,179	(11,768,736)	15,283,094	(66,473,391)
Effects of inflation on cash and cash equivalents	(4,821,242)	(821,717)	(107,863)	(1,341,803)	—	(7,092,625)
Increase (decrease) in cash and cash equivalents	(11,693,525)	(3,479,800)	695,475	(10,301,367)	—	(24,779,217)
Cash and cash equivalents, beginning of period	133,079,873	22,681,704	2,977,334	37,037,546	—	195,776,457
Cash and cash equivalents, end of period	Ps. 121,386,348	Ps. 19,201,904	Ps. 3,672,809	Ps. 26,736,179	Ps. —	Ps. 170,997,240

(1) The accompanying cash flow is prepared in accordance with Mexican FRS.

(2) Petróleos Mexicanos is the issuer of the registered debt securities shown in Table 2 above and a full and unconditional guarantor of the registered debt securities shown in Table 1 above. The Master Trust is the issuer of the registered debt securities shown in Table 1 above, but is not an obligor on the registered debt securities shown in Table 2 above. The Subsidiary Guarantors are full and unconditional guarantors of the registered debt securities listed in both Table 1 and Table 2 above.

(3) PEMEX previously reported 2007 Retirement, seniority premiums and other post-retirement benefit contributions and payments under Financing activities in the amount of (Ps. 27,717,544). PEMEX has corrected such amount under Operating activities.

These changes to the previously reported amounts are summarized in the table below:

	As Previously Reported					
	Petróleos Mexicanos	Master Trust	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations	PEMEX Consolidated
Cash flow provided by (used in) operating activities	Ps. 407,044,476	Ps. 12,866,790	(Ps. 57,923,457)	Ps. 7,264,233	(Ps. 161,691,016)	Ps. 207,561,026
Cash flow (used in) provided by financing activities	(222,819,268)	98,179,841	28,288,017	(13,122,619)	15,283,094	(94,190,935)
	As Corrected					
Cash flow provided by (used in) operating activities	402,092,977	12,866,790	(79,335,619)	5,910,350	(161,691,016)	179,843,482
Cash flow (used in) provided by financing activities	(Ps. 217,867,769)	Ps. 98,179,841	Ps. 49,700,179	(Ps. 11,768,736)	Ps. 15,283,094	(Ps. 66,473,391)

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION
STATEMENT OF CASH FLOW⁽¹⁾

For the year ended December 31, 2006

	<u>Petróleos</u> <u>Mexicanos⁽²⁾</u>	<u>Master Trust⁽²⁾</u>	<u>Subsidiary</u> <u>Guarantors⁽²⁾</u>	<u>Non-Guarantor</u> <u>Subsidiaries</u>	<u>Eliminations</u>	<u>PEMEX</u> <u>Consolidated</u>
Operating activities						
Net income (loss) for the year	Ps. 48,278,809	Ps. —	Ps. 46,874,657	(Ps. 11,652,424)	(Ps. 36,547,837)	Ps. 46,953,205
Adjustments to reconcile net income (loss) to cash provided by operating activities						
Depreciation and amortization	696,602	—	64,072,741	902,846	—	65,672,189
Reserve for retirement payments, pensions and seniority premiums	11,441,909	—	55,940,799	7,110,641	—	74,493,349
Impairment of fixed assets	0	—	—	703,247	—	703,247
Loss on disposal of fixed assets	25,566	—	2,948,752	265,697	—	3,240,015
Allowance for uncollectible trade accounts	803	—	(53,755)	123,209	—	70,257
Allowance for decline in the value of inventory	(19,045)	—	(73,872)	(57,485)	—	(150,402)
Foreign exchange loss (gain)	19,881	12,892,035	646,451	408,406	—	13,966,773
Equity in earning in investees less dividend received and other	(30,613,224)	—	0	(10,041,051)	36,547,837	(4,106,438)
Gain from monetary position	(12,419,713)	—	(4,208,196)	1,808,687	—	(14,819,222)
Deferred income taxes	—	—	1,070,397	(166,236)	—	904,161
Dismantlement and abandonment costs in fixed assets	—	—	(1,992,048)	—	—	(1,992,048)
Changes in operating assets and liabilities						
Accounts and notes receivable	6,012,026	(5,414,268)	(25,452,316)	5,042,409	—	(19,812,149)
Inter-company changes and deductions	(99,515,994)	(1,027,173)	116,167,851	(80,576,615)	64,951,931	—
Inventories	(34,567)	(8,965)	(8,335,597)	(2,413,642)	—	(10,792,771)
Other assets	(1,106,629)	—	(101,576)	420,273	—	(787,932)
Accounts payable and accrued liabilities ⁽³⁾	3,629,240	(3,286,970)	(17,983,763)	3,653,082	—	(13,988,411)
Retirement, seniority premiums and other post-retirement benefits contributions and payments ⁽³⁾	(4,414,348)	—	(14,777,052)	(1,812,233)	—	(21,003,633)
Cash flows provided by (used in) operating activities	(78,018,684)	3,154,659	214,743,473	(86,281,189)	64,951,931	118,550,190
Investing activities						
Increase in fixed assets, net	(264,788)	—	(100,423,287)	(1,913,683)	—	(102,601,758)
Specific funds account-trade commission	(6,599,909)	—	—	—	—	(6,599,909)
Inter-company (increase) decrease in investments	(336,307,451)	(87,159,615)	(293,707,153)	59,224,025	657,950,194	—
Investments in Subsidiaries	(2,896,579)	—	(859,254)	10,386,194	(11,051,854)	(4,421,493)
Cash flows provided by (used in) investing activities	(346,068,727)	(87,159,615)	(394,989,694)	67,696,536	646,898,340	(113,623,160)
Financing Activities ⁽¹⁾						
Proceeds from long term financing	40,748,298	117,116,030	—	10,845,485	—	168,709,813
Financing payments	(47,051,324)	(96,041,579)	—	(5,188,282)	—	(148,281,185)
Inter-company (decrease) increase in financing	518,061,228	29,899,016	143,116,680	33,180,854	(724,257,778)	—
Increase in equity of subsidiary entities	13,708,017	—	34,737,021	257,834	—	48,702,872
Minimum guaranteed dividends paid to the Mexican Government	(268,990)	—	—	(12,407,507)	12,407,507	(268,990)
Cash flows provided by financing activities	525,197,229	50,973,467	177,853,701	26,688,384	(711,850,271)	68,862,510
Effects of inflation on cash and cash equivalents	(8,955,456)	(2,689,606)	2,714,894	467,066	—	(8,463,102)
Increase (decrease) in cash and cash equivalents	92,154,362	(35,721,095)	322,374	8,570,797	—	65,326,438
Cash and cash equivalents, beginning of period	40,925,511	58,402,799	2,654,960	28,466,749	—	130,450,019
Cash and cash equivalents, end of period	<u>Ps. 133,079,873</u>	<u>Ps. 22,681,704</u>	<u>Ps. 2,977,334</u>	<u>Ps. 37,037,546</u>	<u>Ps. —</u>	<u>Ps. 195,776,457</u>

(1) The accompanying cash flow is prepared in accordance with Mexican FRS.

(2) Petróleos Mexicanos is the issuer of the registered debt securities shown in Table 2 above and a full and unconditional guarantor of the registered debt securities shown in Table 1 above. The Master Trust is the issuer of the registered debt securities shown in Table 1 above, but is not an obligor on the registered debt securities shown in Table 2 above. The Subsidiary Guarantors are full and unconditional guarantors of the registered debt securities listed in both Table 1 and Table 2 above.

(3) PEMEX has broken out the line item Accounts payable and accrued liabilities within Operating activities to separately disclose the amounts of its retirement, seniority premiums and other post-retirement benefit contributions and payments during 2006.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

NOTE 23 — SUPPLEMENTARY INFORMATION ON OIL AND GAS EXPLORATION AND PRODUCTION ACTIVITIES (UNAUDITED)

The following tables provide supplementary information on the oil and gas exploration, development and production activities of Pemex-Exploration and Production in compliance with SFAS No. 69, "Disclosures about Oil and Gas Producing Activities" ("SFAS No. 69"). All exploration and production activities of Pemex-Exploration and Production are located in Mexico.

The supplemental data presented herein reflects information for all of Pemex-Exploration and Production's oil and gas producing activities. Capitalized costs and results of operations presented herein have been prepared in accordance with U.S. GAAP. Unless otherwise indicated, all information is presented in constant pesos as of December 31, 2007.

Capitalized costs for oil and gas producing activities (unaudited):

	As of December 31,		
	<u>2007</u>	<u>2006</u>	<u>2005</u>
Proved properties	Ps. 954,798,041	Ps. 844,858,923	Ps. 739,325,338
Construction in progress	50,804,000	56,714,624	56,736,361
Accumulated depreciation and amortization	(405,777,786)	(383,800,878)	(330,177,167)
Net capitalized costs	<u>Ps. 599,824,255</u>	<u>Ps. 517,772,669</u>	<u>Ps. 465,884,532</u>

Costs incurred for oil and gas property exploration and development activities (unaudited):

	Year Ended December 31,		
	<u>2007</u>	<u>2006</u>	<u>2005</u>
Exploration	Ps. 15,133,406	Ps. 12,572,748	Ps. 15,742,112
Development	100,790,721	88,196,418	80,924,293
Total costs incurred	<u>Ps. 115,924,127</u>	<u>Ps. 100,769,166</u>	<u>Ps. 96,666,405</u>

There are no property acquisition costs because PEMEX exploits oil reserves owned by the Mexican nation.

Exploration costs include costs of geological and geophysical studies of fields amounting to Ps. 4,975,089, Ps. 5,248,601 and Ps. 5,612,993 for 2007, 2006 and 2005, respectively that, in accordance with the successful efforts methods of accounting, are accounted for as geological and geophysical exploration expenses.

Development costs include those costs incurred in obtaining access to proved reserves and providing facilities for extracting, treating, gathering and storing oil and gas.

PETROLÉOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Results of operations for oil and gas producing activities (unaudited):

	Year Ended December 31,		
	2007	2006	2005
Revenues from sale of oil and gas	Ps.912,229,890	Ps.889,945,219	Ps.773,336,700
Hydrocarbon duties	663,069,892	583,210,826	534,532,678
Excess-gains taxes	—	8,223,820	60,869,738
Production costs (excluding taxes)	82,715,955	75,665,272	76,855,383
Other costs and expenses	24,200,433	38,066,615	52,545,754
Exploration expenses	4,975,089	5,248,601	5,612,993
Depreciation, depletion, amortization and accretion	56,843,298	49,430,936	40,460,252
	831,804,667	759,846,070	770,876,798
Results of operations for oil and gas producing activities	Ps. 80,425,223	Ps.130,099,149	Ps. 2,459,902

Crude oil and natural gas reserves:

Sales prices and production costs (unaudited)

The following table summarizes average sales prices as of December 31 of each year presented (excluding production taxes) in U.S. dollars:

	2007	2006	2005
Weighted average sales price per barrel of oil equivalent ⁽¹⁾	U.S.\$ 69.49	U.S.\$ 43.39	U.S.\$ 43.75
Crude oil, per barrel	U.S.\$ 83.43	U.S.\$ 47.97	U.S.\$ 47.04
Natural gas, per thousand cubic feet	U.S.\$ 6.59	U.S.\$ 6.04	U.S.\$ 6.85

(1) To convert dry gas to barrel of oil equivalent, a factor is used of 5.201 thousand cubic feet of dry gas per barrel of oil.

Crude oil and natural gas reserves (unaudited)

Under the Political Constitution of the United Mexican States and Mexican statutory law, all oil and other hydrocarbon reserves within Mexico are owned by the Mexican nation and not by PEMEX. Under its Organic Law, PEMEX has the exclusive right to produce these reserves and owns the extracted production, not the reserves, subject to a federal production tax. As discussed in Note 18, during 2007, a new fiscal regime, applicable to PEMEX effective as of January 1, 2008, by means of a decree, modifying several provisions of the Federal Law of Duties related to hydrocarbons. PEMEX's activities are limited to reserves located in Mexico.

Taxes for 2006 and 2007 were calculated pursuant to the Federal Duties Law effective as of October 1, 2007, which includes the following duties:

Ordinary Hydrocarbon Duty—A variable rate of 74.0% in 2008, 73.5% in 2009, 73.0% in 2010, 72.5% in 2011 and 71.5% in 2012-2032 is applied as a function of crude oil and gas prices considered as of December 31. The base for calculating this duty is the value of total crude oil and natural gas production during the year minus the allowed deductions (depreciated investments, costs, expenses and applicable rights). The deductions allowed may not exceed the value obtained by multiplying the produced volume for a

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

particular year times the price of U.S. \$6.5 per barrel of oil equivalent for crude oil and associated natural gas, and U.S. \$2.7 per thousand of cubic feet of non-associated natural gas, respectively.

Duty on hydrocarbons for the stabilization fund of the petroleum incomes—A rate of 10 percent is applied, based on the price of crude oil for export over the value of crude oil production during the year, which always exceeds U.S.\$ 31 per barrel.

Duty for the scientific and technological research fund on matter of energy—A rate of 0.15% in 2008, 0.30% in 2009, 0.40% in 2010, 0.50% in 2011 and 0.65% in 2012-2032 is applied over the value of the crude oil and natural gas production during the year.

Duty for the petroleum fiscalization—A rate of 0.003% is applied over the value of the total crude oil and natural gas production during the year.

Proved oil and natural gas reserves are those estimated quantities of crude oil, natural gas and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions — *i.e.*, prices and costs at the date of estimation. Mexico's proved reserves are estimated by Pemex-Exploration and Production's technical staff, using the year-end crude oil and natural gas prices to calculate its reserves estimates, and reviewed by an independent group inside Pemex-Exploration and Production to ensure consistency.

Pemex-Exploration and Production estimates Mexico's reserves using standard geological and engineering methods generally accepted by the petroleum industry. The choice of method or combinations of methods employed in the analysis of each reservoir is determined by experience in the area, stage of development, quality and completeness of basic data and production and pressure histories.

Reserves data sets forth herein represent estimates only. Reserves valuation is a subjective process of estimating underground accumulations of crude oil and natural gas that cannot be measured in an exact manner. The accuracy of any reserves estimate depends on the quality of available data, engineering and geological interpretation and professional judgment. As a result, estimates of different engineers may vary. In addition, the results of drilling, testing and producing subsequent to the date of an estimate may lead to the revision of an estimate.

Mexico's total proved developed and undeveloped reserves of crude oil, condensates and liquefiable hydrocarbons recoverable from processing plants decreased by 5% in 2007, from 12,849 million barrels of oil equivalent at December 31, 2006 to 12,187 million barrels of oil equivalent at December 31, 2007.

Mexico's proved developed reserves of crude oil, condensates and liquid hydrocarbons recoverable from processing plants, decreased by 6% in 2007, from 8,978 million barrels of oil at December 31, 2006 to 8,436 million barrels of oil at December 31, 2007.

Mexico's total proved developed and undeveloped dry gas reserves decreased by 5% in 2007, from 13,856 billion cubic feet at December 31, 2006 to 13,162 billion cubic feet at December 31, 2007. Mexico's proved developed dry gas reserves decreased by 6% in 2007, from 8,688 billion cubic feet at December 31, 2006 to 8,163 billion cubic feet at December 31, 2007.

The following two tables of crude oil and dry gas reserves set forth PEMEX's estimates of Mexico's proved reserves determined in accordance with Rule 4-10(a) of Regulation S-X of the Securities Act.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Crude Oil and Condensate Reserves (including natural gas liquids)⁽¹⁾

	(In millions of barrels)		
	2007	2006	2005
<i>Proved developed and undeveloped reserves</i>			
At January 1	12,849	13,671	14,803
Revisions ⁽²⁾	455	425	165
Extensions and discoveries	150	86	57
Production	(1,268)	(1,332)	(1,354)
At December 31	<u>12,187</u>	<u>12,849</u>	<u>13,671</u>
<i>Proved developed reserves at December 31</i>	8,436	8,978	9,617

Note: Numbers may not total due to rounding.

(1) Crude oil and condensate reserves include the fraction of liquefiable hydrocarbons recoverable in natural gas processing plants.

(2) Revisions include positive and negative changes due to new data gathered through drilling of wells and reservoir performance

Source: Pemex-Exploration and Production.

Dry Gas Reserves⁽¹⁾

	(In billions of cubic feet)		
	2007	2006	2005
<i>Proved developed and undeveloped reserves</i>			
At January 1	13,856	14,557	14,807
Revisions ⁽²⁾	879	280	640
Extensions and discoveries	171	505	415
Production ⁽³⁾	(1,744)	(1,487)	(1,305)
At December 31	<u>13,162</u>	<u>13,856</u>	<u>14,557</u>
<i>Proved developed reserves at December 31</i>	8,163	8,688	8,888

Note: Numbers may not total due to rounding.

(1) To convert dry gas to barrel of oil equivalent, a factor is used of 5.201 thousand cubic feet dry gas per barrel of oil

(2) Revisions include positive and negative changes due to new data gathered through drilling of wells and reservoir performance.

(3) Production refers to dry gas, although natural gas production reported in other tables refers to sour wet gas. There is shrinkage in volume when natural gas liquids and impurities are extracted to obtain dry gas. Therefore, reported natural gas volumes are greater than dry gas volumes.

Source: Pemex-Exploration and Production.

Based on reservoir performance, new information, and discoveries and production during 2007, proved reserves of crude oil, natural gas, condensates and liquid hydrocarbons for all regions as of December 31, 2007, were estimated to be 14,717.2 million barrels of oil equivalent as compared to 15,514.2 million barrels of oil equivalent at December 31, 2006.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

Standardized measure of discounted future net cash flows related to proved oil and gas reserves (unaudited)

The standardized measure tables presented below relate to proved oil and gas reserves excluding proved reserves scheduled to be produced after the year 2032.

Estimated future cash inflows from production are computed by applying prices of oil and gas on December 31 to the year-end quantities. Future development and production costs are those estimated future expenditures needed to develop and produce the year-end estimated proved reserves, assuming constant year-end economic conditions.

Future tax expenses are computed by applying the appropriate year-end statutory tax rates—with consideration of the tax rates of the new fiscal regime for Pemex-Exploration and Production already legislated for 2008—to the future pre-tax net cash flows related to Mexico's proved oil and gas reserves.

The estimated future payment of taxes was made based on the new fiscal regime applicable to Pemex Exploration and Production, effective January 1, 2008 by means of decree which reformed Chapter XII of the Federal Law of Hydrocarbon Duties.

The standardized measure provided below represents a comparative benchmark value rather than an estimate of expected future cash flows or fair market value of PEMEX's production rights. There are numerous uncertainties inherent in estimating quantities of proved reserves and in projecting future rates of production and timing of development expenditures, including many factors beyond the control of the producer. Accordingly, reserve estimates may be materially different from the quantities of crude oil and natural gas that are ultimately recovered.

Standardized measure of discounted net cash flows

	As of December 31,		
	2007	2006	2005
Future cash inflows	U.S.\$ 945,566	U.S.\$ 615,337	U.S.\$ 653,914
Future production costs (excluding taxes)	(107,148)	(82,696)	(85,432)
Future development costs	(38,205)	(35,845)	(35,966)
Future cash flows before tax	800,213	496,797	532,516
Future production-and-excess-gains taxes	(632,321)	(410,021)	(448,162)
Future net cash flows	167,892	86,775	84,354
Effect of discounting net cash flows at 10%	(78,074)	(31,699)	(32,728)
Standardized measure of discounted future net cash flows	<u>U.S.\$ 89,818</u>	<u>U.S.\$ 55,076</u>	<u>U.S.\$ 51,626</u>

Note: Table amounts may not total due to rounding.

PETRÓLEOS MEXICANOS, SUBSIDIARY ENTITIES AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
FOR THE YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005
(Figures stated in thousands of Mexican pesos as of December 31, 2007 purchasing power and
in thousands of U.S. dollars or other currency units, except exchange rates and oil prices per barrel)

To comply with SFAS 69, the following table presents the aggregate standardized measure changes for each year and significant sources of variance:

Changes in standardized measure of discounted net cash flows

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Sales of oil and gas produced, net of production costs	U.S.\$ (74,299)	U.S.\$ (68,136)	U.S.\$ (55,988)
Net changes in prices and production costs	173,861	2,908	122,257
Extensions and discoveries	6,642	4,573	3,149
Development cost incurred during the year	8,951	7,803	7,067
Changes in estimated development costs	(14,634)	(6,796)	(11,453)
Reserves revisions and timing changes	29,947	14,910	3,419
Accretion of discount of pre-tax net cash flows	26,446	28,482	20,523
Net changes in production-and-excess-gains taxes	(122,172)	19,707	(83,972)
Aggregate change in standardized measure	<u>U.S.\$ 34,742</u>	<u>U.S.\$ 3,450</u>	<u>U.S.\$ 5,002</u>
Standardized measure			
As of January 1	55,076	51,626	46,624
As of December 31	<u>89,818</u>	<u>55,076</u>	<u>51,626</u>
Change	<u>U.S.\$ 34,742</u>	<u>U.S.\$ 3,450</u>	<u>U.S.\$ 5,002</u>

Note: Table amounts may not total due to rounding.

In computing the amounts under each factor of change, the effects of variances in prices and costs are computed before the effects of changes in quantities. Consequently, changes in reserves are calculated at December 31 prices and costs. The change in computed taxes includes taxes effectively incurred during the year and the change in future tax expense.

EX-12.1 2 y71170exv12w1.htm EX-12.1: CERTIFICATION

Exhibit 12.1

CERTIFICATION

I, Jesús Reyes Heróles González Garza, certify that:

1. I have reviewed this amendment to the annual report on Form 20-F/A of Petróleos Mexicanos;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, 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 in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent function):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: September 24, 2008

/s/ Jesús Reyes Heróles González Garza

Name: Jesús Reyes Heróles González Garza

Title: Director General/Chief Executive Officer

EX-12.2 3 y71170exv12w2.htm EX-12.2: CERTIFICATION

Exhibit 12.2

CERTIFICATION

I, Esteban Levin Balcells, certify that:

1. I have reviewed this amendment to the annual report on Form 20-F/A of Petróleos Mexicanos;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, 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 in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent function):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: September 24, 2008

/s/ Esteban Levin Balcells

Name: Esteban Levin Balcells

Title: Chief Financial Officer

EX-13.1 4 y71170exv13w1.htm EX-13.1: CERTIFICATION

Exhibit 13.1

Certification
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Petróleos Mexicanos, a decentralized public entity of the Federal Government of the United Mexican States (the "Company"), does hereby certify, to such officer's knowledge, that:

The Amendment No. 1 to Annual Report on Form 20-F/A for the year ended December 31, 2007 (the "Form 20-F/A") of the Company fully complies with the requirements of section 13(a) or 15 (d) of the Securities Exchange Act of 1934 and information contained in the Form 20-F/A fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 24, 2008

/s/ Jesús Reyes Heróles González Garza

Name: Jesús Reyes Heróles González Garza

Title: Director General/Chief Executive Officer

Date: September 24, 2008

/s/ Esteban Levin Balcells

Name: Esteban Levin Balcells

Title: Chief Financial Officer