

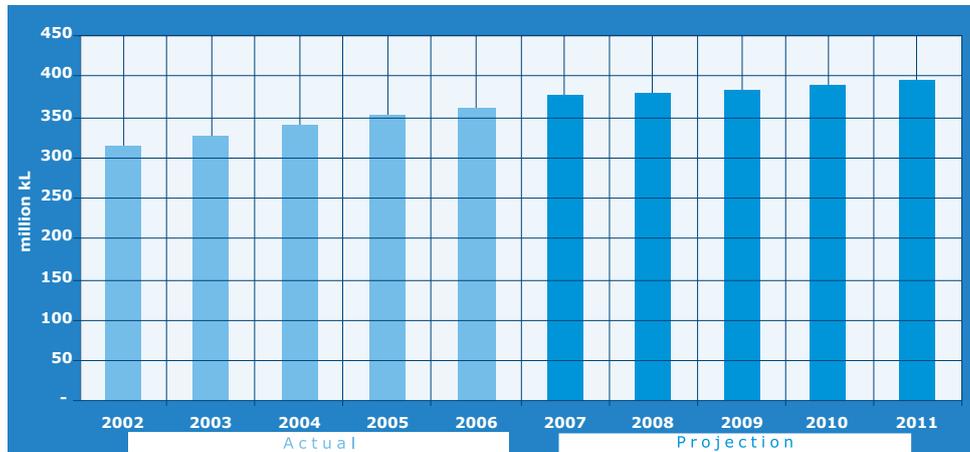


"Together we Deliver"

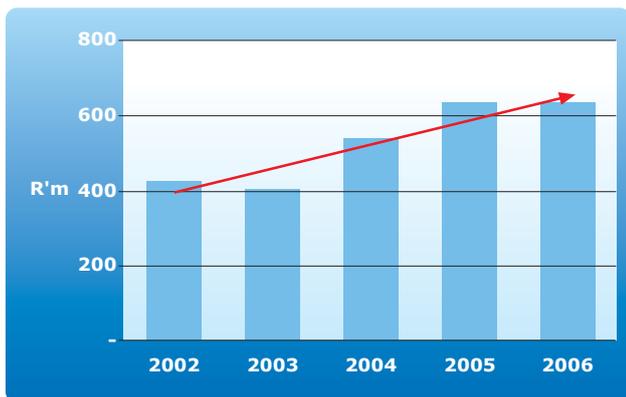
Annual Report

2005/2006

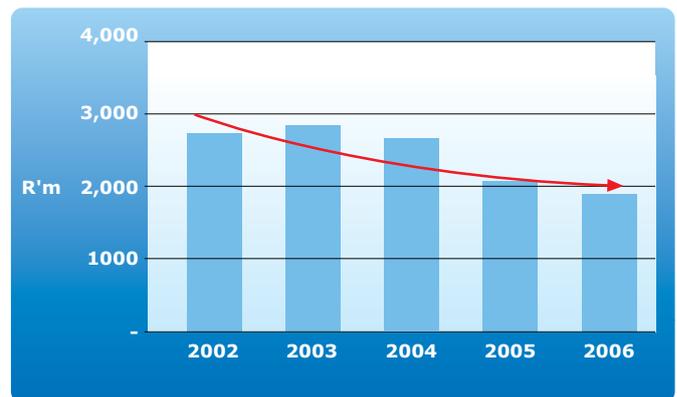
Umgeni Water at a glance



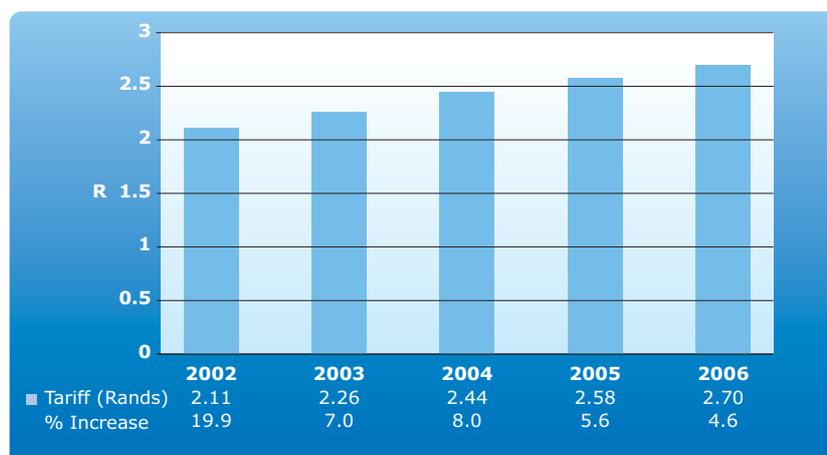
Water Volumes Sold and Projected Sales Volumes



Net Cash from Operating Activities



Net Debt



Potable Bulk Water Tariff per Kilolitre



Vision

To be the Number One Water Utility in the Developing World

Mission

To provide effective and affordable bulk water, bulk sanitation and related solutions to local government in accelerating the water sector's national developmental agenda

Strategic Intent

A key partner to enable local government in delivering effective water services

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About this report

Umgeni Water's activities for the 12-month period 1st July 2005 to 30th June 2006 are covered in this Annual Report, which has the theme "Together We Deliver". The Annual Report 2005/2006 reflects Umgeni Water's commitment and contribution to service delivery through sound corporate governance; stakeholder engagement and partnership; staff participation; and the organisation's accomplishments in both the social and environmental arenas.

This report has a strong focus on sustainability issues. As in previous years, the Umgeni Water Annual Report was guided by the Global Reporting Initiative (GRI) Sustainability Reporting Guidelines (2002). The Annual Report for 2005/2006 has been enhanced by stakeholder feedback, obtained from a formal survey conducted after the release of the 2004/2005 Annual Sustainability Report.

A cross-divisional task team was involved in preparing the Annual Report, thereby ensuring that all spheres of the organisation's activities and business have been captured, both collaboratively and comprehensively. The adoption of this approach has increased awareness of corporate strategies and sustainability across the organisation.

An electronic version of the Umgeni Water Annual Report 2005/2006 is available on the Umgeni Water website: <http://www.umgeni.co.za>.

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Who we are



Midmar Dam

1.1 ABOUT UMGENI WATER

In June 1974 Umgeni Water was established to supply bulk treated water to municipalities situated in Umgeni Water's designated KwaZulu-Natal operational area, comprising 2 176 square kilometres. The organisation began work in accordance with its mandate, issued first under the Water Act of 1956 and later the Water Services Act 108 of 1997. With a staff of five and operating from offices in Pietermaritzburg, Umgeni Water was then one of the smallest water utilities in South Africa.

In three decades, Umgeni Water has grown into a major bulk water and sanitation services provider. Umgeni Water is the largest bulk water supplier in KwaZulu-Natal, the second-largest water utility in South Africa and one of the most successful water management organisations on the African continent. Umgeni Water's operational area has increased nine-fold since 1974 and now covers 21 155 square kilometres. The organisation's customer base includes six municipalities in KwaZulu-Natal - eThekweni Metropolitan Municipality, Ilembe, Sisonke, uMgungundlovu and Ugu District Municipalities, and uMsunduzi Local Municipality. The organisation supplies annually about 361 million kilolitres of potable water to its municipal customers. About 4.8 million consumers ultimately receive water supplied by Umgeni Water.

Umgeni Water employs 789 staff, including highly skilled and experienced specialists. Umgeni Water is recognised in Africa and the developed world.

Umgeni Water is a state-owned business enterprise and it operates within the South African legislative parameters of the Water Services Act 108 of 1997, Public Finance Management Act 1 of 1999 and Public Audit Act 25 of 2004. The organisation is directly accountable to the Department of Water Affairs and Forestry.

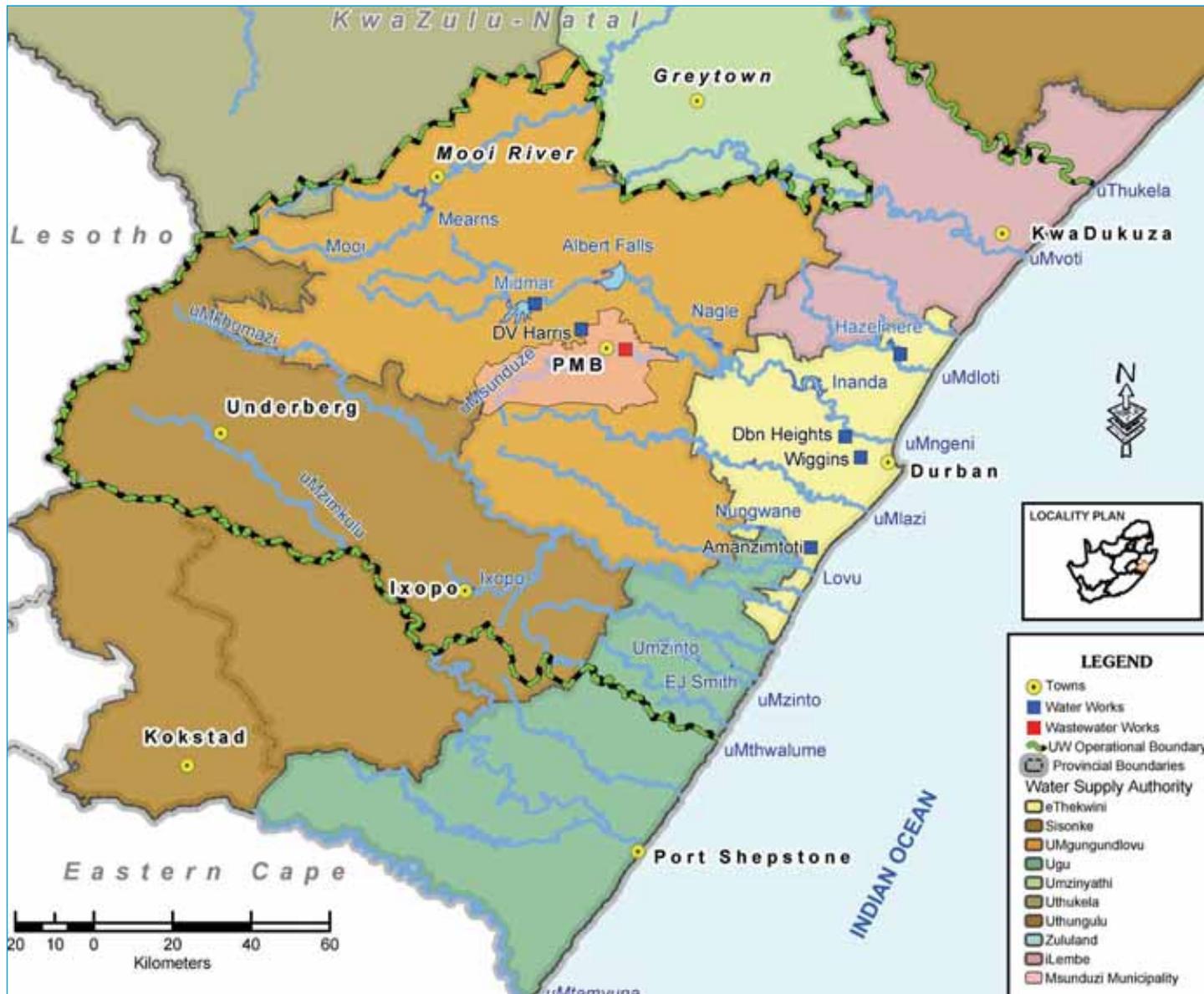
An Executive Management Team, comprising a Chief Executive Officer and four General Managers, guides the day-to-day activities of Umgeni Water. A non-executive Board, consisting of members appointed by the Minister of Water Affairs and Forestry, oversees the organisation. The Board reports to the Minister of Water Affairs and Forestry.

The primary function of Umgeni Water is to supply treated water in bulk to its municipal customers. The organisation is also involved in wastewater treatment as part of its primary activities. Bulk water sales constitute about 89% of the organisation's revenue, while the balance is derived from non-core activities, such as specialised services provided to municipalities, government departments and companies in the private sector.

In order to conduct its core function, Umgeni Water requires adequate and efficient infrastructure able to guarantee a high assurance of supply. The total asset value of the organisation is R2,997 billion.

Umgeni Water owns and manages 5 dams, 10 water works & 2 wastewater works.

Umgeni Water manages on behalf of the Department of Water Affairs and Forestry and municipalities: 7 dams (5 on behalf of the Department of Water Affairs and Forestry and 2 on behalf of the Ugu District Municipality); 2 water works (on behalf of the Ugu District Municipality); 1 wastewater works (on behalf of uMgungundlovu District Municipality).



Umgeni Water's Operational Area

1.2 REPORT OF THE BOARD CHAIRMAN

It is with a deep sense of pride that I reflect on the year under review. In a word, it has been a period of introspection, strategic positioning and accomplishment by Umgeni Water as the organisation surged towards unlocking greater shareholder and customer value while intensifying its humanitarian efforts in assisting with easing the water and sanitation backlogs. Another marvellous characteristic of 2005/2006 was the solid and growing alignment between the strategic focus of the Board, the Executive and Top Management, although the Board remains independent of operational activities of the organisation.

The tone and focus for the year was first set at an Executive Strategy Planning Session and later confirmed at a Strategy Session of the Board. The critical outcomes of both meetings led to a refinement of Umgeni Water's Corporate Strategy, shifting its emphasis from South Africa and Africa to provincial participation in accelerated service delivery. The organisation concentrates on providing capacity and support to enable municipalities to eradicate the water and sanitation backlogs in KwaZulu-Natal. This has defined the organisation's growth strategy, underpinning the crucial role Umgeni Water will play in the speedy roll out of water and sanitation provision on a commercial or cost-recovery basis.

The heartbreaking reality is that an estimated 750 000 households in KwaZulu-Natal do not have easy access to safe drinking water. This is a challenge that needs to be addressed with urgency. Effectiveness in overcoming this challenge is largely dependent on the level and quality of support municipalities receive from water boards. Umgeni Water is committed to providing that support, as an organisation with expertise and a strong corporate social responsibility culture. The organisation's corporate social responsibility ethos is also manifested in the work it does in water education and sponsorships towards job creation and empowerment initiatives.

Umgeni Water has formed a partnership with uThukela Water and Umhlatuze Water to extend bulk water infrastructure into unserved areas, thereby making a meaningful contribution towards the eradication of water backlogs identified in the Millennium Development Goals. The plan to achieve these goals is contained in the KwaZulu-Natal Bulk Water Supply Strategy. The national and provincial governments and the eThekweni Metropolitan Municipality, Umgeni Water's biggest customer, have warmly welcomed the strategy.

The partnership between Umgeni Water, uThukela Water and Umhlatuze Water is a reflection of Umgeni Water's endeavours to work closely with other similar organisations to form a formidable front to support municipalities in addressing poverty and providing basic services.

The strategic functions of Umgeni Water, as a Water Service Provider, partner and implementing agent, are neatly aligned to government plans to eradicate the water and sanitation backlogs and to precipitate a sustainable economic growth rate of 6% through the Accelerated and Shared Growth Initiative for South Africa (ASGISA).

Umgeni Water is proud of its achievements and, equally importantly, of the strategic contribution it continues to make to its shareholder, the Department of Water Affairs and Forestry, customers and sector representative organisation, the South African Association of Water Utilities (SAAWU). Umgeni Water is actively involved in the activities of SAAWU, which conducted high-level water services stakeholder interactions on key policy-related issues. SAAWU provided formal inputs and mandated submissions to DWA and other sector entities on Raw Water Pricing Strategy, The Draft Institutional Reform Strategy, the Draft Water Services Bill and the Draft Strategy for the Regulation of Water Services.

It has been a momentous year as the organisation stayed focused on its primary business of treated bulk water supply. In this period, a combined sale of 361 million kilolitres of treated water was made, representing an increase of 2,5% over the previous year. The revenue derived from this sale amounted to R1,076 billion, also up on the previous year by 8,4%. The net effect on the bottom line was a profit of R154,1 million for the parent company - up 356% on 2004/2005. This splendid performance was the result of unstinting support of Umgeni Water's customers and the hard work of its staff and the Executive in implementing cost saving measures and more effective debt management,

which resulted in the reduction of net finance cost. I extend my thanks to these customers for their confidence in Umgeni Water's product and in the organisation's ability to deliver an excellent service. At the same time, I thank the Executive and staff for working as a team in driving Umgeni Water's strategy to reduce debt and increase profit. Umgeni Water's employees are among its most valued investment.

The organisation's productive assets have similarly enabled it to meet its commitments.

Without exception, all the members of the Board have made crucial contributions to the achievements of Umgeni Water. Their wise and well-considered input, along with their expertise, have had the effect of ensuring the Board operates at the optimum and strategic level. The contribution of members has served to strengthen the work of Umgeni Water keeping it well focused on its legislative mandate and commercial objectives. I extend my thanks to the members of the Board and encourage them to continue to be active participants in the future of Umgeni Water.

The Board continues to examine its structure on an ongoing basis in order to be streamlined and effective. In the past year an amalgamation of some committees was undertaken, resulting in three main committees emerging from the process. They are the Audit and Risk Committee; the Remuneration Committee; and the Procurement, Fixed Assets and Capital Projects Committee. The Board's adherence to corporate governance in relation to, among others, the King Report on Corporate Governance 2002 (King II) Report and the Public Finance Management Act 1 of 1999 is an uncompromising prerequisite. The Board has performed splendidly in the area of corporate governance.

Umgeni Water is on the road to a financial turnaround, which will instil confidence that the organisation has reinvented itself and is now reaping the rewards of the turnaround strategy implemented in 2003.

Tribute, Thanks and Congratulations

- Umgeni Water's CEO, Ms Gugu Moloi resigned in the reporting year. I thank her for her enormous contribution to Umgeni Water and wish her the very best for the future.
- The General Manager: Corporate Services at Umgeni Water, Ms Pearl Maphoshe, also resigned. I take this opportunity to thank her for significant contribution to Umgeni Water and wish her every success in the future.
- I extend my gratitude to Mr Mzimkulu Msiwa, General Manager: Operations, for accepting the position of Acting CEO. Congratulations would also be in order for his appointment as CEO with effect from 1 September 2006.
- At the same time, I wish to congratulate Mr Sibusiso Sithole on his appointment as General Manager: Corporate Services.
- Ms Buyelwa Sonjica left the Department of Water Affairs and Forestry as Minister to take up the position as Minister of Minerals and Energy. I extend my thanks to her for her leadership and wisdom and wish her well in her new position.
- Ms Lindiwe Hendricks has been appointed Minister of Water Affairs and Forestry. She is the former Minister of Minerals and Energy. I warmly welcome her and look forward to working with her. She brings with her a wealth of knowledge and experience which Umgeni Water will value and cherish.



Nhlanhla Gasa
Chairman
Board of Umgeni Water

1.3 MESSAGE FROM THE CEO

Umgeni Water has completed another eventful year in the South African corporate world. It gives me great pleasure and a sense of excitement to present the Chief Executive Officer's review of the organisation's performance for the past 12 months.

As the Financial Year of 2005/2006 dawned, Umgeni Water was propelled into an exciting era of consolidation and growth after a remarkable 2004/2005, when, for the first time in five years, the organisation achieved profitability. In many respects, the accomplishments of 2004/2005 set the tempo for what has become one of the most robust years in the 31-year history of Umgeni Water. The year under review will remain a memorable period - in part because of the excellent cross-divisional synergies that have been developed within the organisation and the excellent rapport between the Board and Executive; and between the Board, Executive, Top Managers and all the customers of Umgeni Water.

The Annual Report 2005/2006, themed *Together We Deliver*, comprehensively captures the achievements and strategies to meet the expectations of our shareholder, the Department of Water Affairs and Forestry (DWAF), and Water Service Authorities (municipalities). A clear organisational focus and the optimum employment of capabilities have produced excellent results, as reflected in the audited financial statements. The Annual Report 2005/2006 lives up to its theme by illustrating how the tireless efforts of the Umgeni Water Board, Executive Management Team and employees at all levels have positioned the organisation as a significant contributor to the economy of our operational area. In all that Umgeni Water undertook and accomplished, it continued to meet an array of corporate governance challenges, as evidenced in the unqualified audit report.

In most instances achievement cannot be had without the spark that ignites the passion to obtain it. For us, that spark was the overwhelming support received from the Umgeni Water Board, staff, the National Education, Health and Allied Workers' Union and our customers. Their co-operation reflected more than a healthy relationship; it resembled a partnership that helped deliver one of the best performances yet. I acknowledge with appreciation the co-operation of municipal managers, heads of infrastructure divisions and the financial officers of eThekweni Metropolitan Municipality. I also acknowledge unhesitatingly the positive role played by organised labour.

Umgeni Water continues to enhance its relationship with major Water Service Authorities (WSAs). The better and stronger relationships developed played a crucial role in enabling us to conclude 20-year bulk potable water supply agreements with WSAs within our designated supply area. The agreements are modelled on similar documents of the South African Local Government Association (SALGA) and the South African Association of Water Utilities (SAAWU).

The Financial Year 2005/2006 was punctuated by several achievements, the most celebrated of which was the selection of Umgeni Water for top spot in the Best Industry for Public Sector and Most Improved Company. Umgeni Water won these accolades in the prestigious Deloitte Best Company to Work For Survey. This had the effect of giving credence to the Umgeni Water drive to become an employer of choice by heightening staff satisfaction levels. Other accomplishments included:

- A Climate Change Workshop held in Pietermaritzburg, where some of the finest academics presented papers. The workshop had attracted invaluable publicity.
- The presentation of the KwaZulu-Natal Bulk Water Supply Strategy to key stakeholders. The KZN Strategy is intended to provide infrastructure and support to eradicate the water backlogs in the province.
- The Strategy was endorsed by the Water Summit in Durban, and it has since also received the support of Umhlathuze Water and uThukela Water.

Umgeni Water had a positive effect on public perceptions through its handling of water quality issues in the Pietermaritzburg and Durban regions. The organisation was thanked for its commitment to satisfying customer and consumer expectations.

The Executive Management Team vigorously drove Umgeni Water strategy to become a centre of innovation and learning. This was reflected in the support given to several cross-divisional task teams that continue to make an important contribution to the business and its future. The task teams are involved in, among other strategic initiatives, benchmarking, research and development and women empowerment. The work undertaken by these teams, together with the primary business of Umgeni Water, have formed the basis of studies by visiting water utility delegations from Africa. Staff have been empowered to share ideas with the Executive at Site Visits and Staff Information Sessions; some of these suggestions have been incorporated into the Corporate Strategy.

The benefits of its organisational restructuring programme instituted in 2003 have been maintained and continue to be evident in the operational efficiencies, which have had a positive impact on customer relations and increased revenue and profits. Water sales amounted to 361 million kilolitres, an increase of 2,5% over the previous year, and revenue has increased by 7,6% to R1,076 billion. The profit for the year was R154,1 million, up significantly from 2004/2005.

The current profit is in term of the organisational 5 year Business Plan whereby Umgeni Water needs to generate profits, albeit within the parameters of its tariffing policy, to reduce the organisation's current debt levels.

The tariff increase to our customers was 4,6%, which is in line with the CPIX. Umgeni Water is fortunate to be in a healthy financial state, after a difficult past in which increasing debt levels had exacted its toll. The organisation has maintained its credit ratings of AA Long-Term and F1 + Short-Term, issued by Fitch. Thus enabling Umgeni Water to borrow with ease on the open market.

The organisation has forecast to generate sufficient cashflows from its operating activities to finance its 5 year Capital Infrastructure Programme. This programme is directed at meeting customer needs and contributing to the elimination of water and sanitation backlogs identified under national government targets and, from a broader perspective, the Millennium Development Goals.

Whilst we are pleased with our performance over the past year, we have certainly not lost sight of the purpose for our existence and the responsibility that comes with it; that is ensuring that the water we supply in bulk is affordable and available to as many people as possible. This is associated with the challenge of also ensuring that the infrastructure and services we provide assist with improving the quality of life of all communities within our operational area.

There are other future challenges facing Umgeni Water. The most crucial of these challenges are:

- Accelerating the implementation of the Capital Infrastructure Programme;
- Retaining skilled staff, especially in the face of the expected GDP rate of 6%; and
- Addressing the outcomes of the institutional reform process, as outlined in the Strategic Framework for Water Services.

Umgeni Water will respond to these challenges by continuously reviewing its Human Resources Development Plans, and by influencing the policy on institutional reform through active participation and engagement in the deliberations of the South African Association of Water Utilities.

Another key challenge facing Umgeni Water and other Water Service Providers is providing capacity and support that will serve as a catalyst to intensify the roll out of water and sanitation services. Umgeni Water is well placed to contribute, both in solo efforts and as a partner. The evidence is visible in school sanitation projects undertaken in conjunction with the KwaZulu-Natal Department of Education and in new pipeline projects that have already been launched or are in the planning stage. The pipeline projects require significant investment but Umgeni Water sees this to be of strategic importance as it will make it possible for basic services to be provided and for economic growth to be enhanced. Contracts awarded in terms of the Capital Infrastructure Programme and recurring operating expenditure are intrinsically linked to procurement legislation and its supply chain management principles and contribute to overcoming some of the challenges faced by the "second economy".

It has been a momentous year for Umgeni Water, but it does not end there. We cannot be complacent or oblivious of our natural environment. We have a place in this environment and we also carry the concomitant responsibility, as a state-owned business enterprise, to ensure that the environment is protected. Umgeni Water has been well positioned for the future and will be entering it, confident of its ability to continue playing an active part, first within the operational area, second within the Province of KwaZulu-Natal and thereafter elsewhere in South Africa and Africa.

Finally, I thank the staff of Umgeni Water for a job well done.



Mzimkulu Msiwa
Chief Executive Officer

1.3 UMYALEZO OVELA KU CEO

Umgeni Water usaqede omunye unyaka wezizigameko kulomhlaba wase Ningizimu Afrika obunezivunguvungu. Kunginika injabulo enkukhulu kanye nomuzwa wokuziqqaja, ukwethula umbono ojulile we Chief Executive officer, wokusebenza kwenhlangano ezinyangeni eziyisishumi nambili ezedlule.

Ngesikhathi uqala unyaka wezimali ka2005/2006, Umgeni Water wathatha amanyathelo abheke esikhathini esinelubelube (exciting era) lokuhlenganisa nokukhulisa, ngemuva konyaka obubalulekile ka2004/2005 lapho, okokuqala ngqa eminyakeni emihlanu, inhlango yafinyelela ekwenzeni inzuzo. Ngezindlela eziningi ukuzuza okwazuzwa ngo 2004/2005 kwabe sekuklama indlela yokwenza yalokho okwasekuthathwa ngokuthi ingeyokuziqhenya futhi enezinga eliphezulu emlandweni weminyaka engama 31 wo-Umgeni Water. Unyaka ongaphansi kobukezo uyohlala uyisikhathi esikhumbulekayo - ngenxa yokuhlenganisa imikhakha eyahlukahlukene ngendlela encomekayo esungulwe yinhlangano kanye nombiko wokuzwana, nobubele ophakathi kwe-Board kanye nabaphathi, nezimenenja eziphezulu kanye nawo wonke amakhasimende o-Umgeni Water.

Umbiko wonya ka2005/2006 ondikimba yayo ithi: Ndawonye seThula umSebenzi, lapho Umgeni Water unogqozi lokuzuza kanye nesu eligxile ekufezeni okulindelwe ngabanini nhlangano, wuMnyango weziNdaba zaManzi namaHlathi (DWAf), kanye nezidingo zababhekele amanzi (omasipala). Isu esikhuluma ngalo lihlanganisa izindlela zokwenza zenhlangano ezisezingeni eliphezulu, kanti futhi lenza sikwazi ukukhipha imiphumela emihle, njengoba ivezwe ezitatimendeni zezimali ezihloliwe. Umbiko wonya ka2005/2006 uhamba ngokwendikimba okukhombisa ukuthi imizamo emikhulu yo-Umgeni Water Board, Executive Management, kanye nabasebenzi abasebenza ngokuzikhandla kuwonke amazinga, benze kanjani ukuthi babeke inhlangano endaweni ebalulekile yeqhaza lomnotho ngesikhathi sokusebenza kwethu kanye nokufinyelela ezinhlosweni ezibikwe ngonyaka ka2005/2006. Kukhokoke lokho Umgeni Water uthathe futhi wenza, waqhubeka nokwenyuka futhi wafinyelela kwizinsalelo ezahlukahlukene njengoba kuvezwe embikweni wezimali ohloliwe.

Ezikhathini eziningi ukuzuza ngeke kwenzeka ngaphandle kwenhlansi ebasa umlilo wothando lokuzuza. Kuthina leyonhlansi kwakuwu xhaso olumangalisayo esaluthola kwi Board yo-Umgeni Water, abasebenzi, imfundo kazwelonke, inyunyana i-Health ne-Allied Workers Union, kanye namakhasimende ethu. Ukusebenzisana kwabo nathi kwagqama kwathi bha; kwafana nokusebenzisana ngokubambisana okwasiza ukwethula umsebenzi oncomeka kakhulu yinhlangano. Ngokukhulu ukuziqhenya ngazisa ukusebenzisana okuhle kwabaphathi bakaMasipala izinhloko zezingqalasizinda kanye nabaphathi zimali be-eThekwini Metropolitan Municipality. Ngiphinda futhi lapha ngazisa ngaphandle kokungabaza iqhaza elidalwe ngabasebenzi benhlangano.

Umgeni Water uyaqhubeka nokukhulisa ubudlelwano bawo nabaphathi bezokulethwa kwamanzi (Water Service Authorities) (WSAs). Ubudlelwano obungcono kanye nobuqinile obakhekile budlale iqhaza elibalulekile elenze ukuba sikwazi ukungena esivumelwaneni seminyaka esingama 20 lapho sizobe sisabalalisa amanzi awumthamo omkhulu aphahekayo kuma WSAs ezindaweni zethu zokusabalalisa amanzi. Izivumelwano zenziwe zahambisana nezidingo ze South African Local Government Association (i-SALGA) kanye neSouth African Association of Water Utilities (i-SAAWU).

Unyaka wezimali ka2005/2006 bewuqhutshwa yizimpumelela, impumelelo ethakaselwe kakhulu kube ukukhethwa ko-Umgeni Water njengomboni ephambili esebenzela umphakathi kanye nenkampani esingcono kakhulu. Umgeni Water ukuzuze lokhu kwiDeloitte Best Company to Work for Survey (ezokudabula). Lokhu kube nogqozi ekunikeni Umgeni Water intshisekelo ukuba ngumqashi wekhethelo kanye nokuzama ukwenelisa abasebenzi emazingeni abo. Okunye okufinyelelwe kukona kubandakanya:

- Ukwenza I workshop ye Climate Change Workshop.(ukushintsha kwezulu) eyaheha ezinye izifundiswa ezingogoti ezathula izinkulumo, kanye nokugqamisa inhlangano.
- Ukwakha emqondweni isu lokusabalalisa amanzi awumthamo omkhulu kwaZulu-Natal, elihlose ukwenza izingqala sizinda kanye nokusekela umkhankaso wokunciphisa ukusweleka kwamanzi KwaZulu Natali . Lelisu lethulwa futhi lamukelwa emhlanganweni wezamanzi (Water Summit) eThekwini, futhi kusukela lapho belisekelwa Umhlathuze Water kanye noThukela Water.

Umgeni Water futhi ube neqhaza elibalulekile ekubonweni wumphakathi ngendlela obuphethe ngayo izindaba zamanzi asezingeni eliphakeme ezindaweni zaseMgungundlovu nezaseThekwini. Inhlangano ibe nokubongwa kakhulu ngokwenza umsebenzi obala kanye nokuzinikela ekuxazululeni kwezinkinga zamanzi okwanelisayo.

Ngokombono wenhlangano, abaphathi bagqoquzele ngomfutho isu lo-Umgeni Water ukuthi libe ngu ngqa phambili futhi kube nokufunda ngalo. Lokhu kwabonakala ngoxhaso olwanikezwa yizigungu zokwenza okuthile (task teams) eziqhamuka emikhakheni ehluukahlukene olwaqhubeka nokwenza nokubamba iqhaza elibalulekile ekusebenzeni kwenhlangano kanye nekusasa layo. Ezinye zezigungu zokwenza ziyathinteka ekusungulweni kwezindlela ezintsha, ucwaningo kanye nokuthuthukisa abesifazane. Umsebenzi owenziwe yilezizigungu, ngokuhlanganyela kanye nomsebenzi wo-Umgeni Water, sewakhe isizinda sokufunda ngokuthi kuvakashe izithunywa zokusetshenziswa kwamanzi e-Afika. Enhlanganweni yonke abasebenzi sebenikezwe amandla okuthi bacebisane ngemibono nabaphathi ikakhulukazi ekuvakashelweni kwizindawo (Site Visits) kanye nokwenziwa kwesikhathi lapho kuweliselwa khona ulwazi kubasebenzi. Ezinye zeziphakamiso zifakiwe eswini eliqukethe konke (Corporate Strategy).

Ngaphandle kokungabaza Umgeni Water ubona izimbuyiselo (benefits) zohlelo lokuzihlela olwenziwa ngo 2003. Izimbuyiselo lezi zibonakala ekusebenzeni okugculisayo, osekube nomthelela omuhle ekwakheni ubuhlobo namakhasimende, ekudayiseni kanye nendlela ukusebenza okususelwa kuyo. Ukudayiswa kwamanzi kulo nyaka obukezwayo kufinyelele ku 361 million kilolitres-okukhomba ukukhula ngo 2,5% kusukela onyakeni odlule- kanti imbuyiselomali (revenue) yokudayiswa kwamanzi ifinyelele ku R1,076 billion. Isengezo esitholakele (profit) salo nyaka sibe ngu R154,1 milion, okubonakale sikhulile ngokunconywayo kusukela ngo 2004/2005. Imiphumela yezimali idalwe yisu lokuzihlela kwenhlangano.

Isizathu esimqoka sokwenyuka kwesengezo esitholakele kube ngumthamo wamanzi owengeziwe odayisiwe, yizindlela zokonga kanye nendlela enhle yokuphathwa komkhakha wokuqoqwa kwezikweletu, iyo le eholele ekutheni kube nokwehla kwezindleko zezimali. Ukwenyuka kwentengo emakhasimendeni ethu kube ngu 4,6% okuhambisanayo neCPI. Kuyinto enhle kuzo zonke izinhlangano zamabizinesi ukuthi zihlale zisesimweni esihle kwezizimali ngoba lokho kwakha ukuthenjwa ngumphakathi bese kuthi uma kufanele, izinkampani zidinge ukwelekelwa ngezimali zibe sesimweni esihle sokuheha abatshalizimali (investors) kanye notshalomali (investment). Umgeni Water usenhlahlani ngokuthi ube sesimweni sezimali esinempilo, emveni kwesimo esinzima esedlule lapho izikweletu zazikhule zeqa ikhanda. Inhlangano iphindile futhi yabamba izinga layo ngokwesikali se-AA Long-Term neF1 + Short-Term, esakhishwa nguFitch. Empeleni lokhu kusho ukuthi Umgeni Water ungakwazi ukuboleka kalula ezimakethe zemali ezivulekile futhi ungakwazi ukuhlangabezana nemigomo yezikweletu, ezikhathini ezinqunyiwe ezimfishane noma ezinde.

Ukusebenza kwethu kusikhiqizela imali engu kheshi ukuze sikwazi ukukhokhela izinhlelo zeziNgqalazizinda ezisemQoka, ezinqondiswe ekuhlangabezani nezidingo ezisemqoka zamakhasimende kanye nokunciphisa imisebenzi esilele yokusatshalaliswa kwamanzi kanye nokulahlwa kwetshe lentaba nomshobingo, imisebenzi eyayi khonjwe nguhulumeni kanye ne Millennium Development Goals. Isengezo esitholakele ku 2005/2006 sizosetshenziselwa ukwehlisa izikweletu zethu. Vele sesizehlise kakhulu izindleko zethu ngokwesu elincomekayo lokukhipha izimali.

Phezu kokuthi siyajabula ngendlela esisebenze ngayo ngonyaka odlule asizange neze sigudluke enhlosweni ngqangi yokuba khona kwethu kanye nemisebenzi ehambisana nakho ukuba khona kwethu, -inhloso wukwenza isiqiniseko sokuthi sisabalalisa amanzi angumthamo omkhulu, izindleko zawo abathengi abangakwazi ukungabhekwa nazo kanti futhi ebetholakala kubantu abaningi. Lokhu kuhambisana nezinsalelo zokugqunguzela inqubekela phambili kuleyo miphakathi encisheke amathuba ukuze ithole amanzi.

Yebo, empeleni zikhona izinsalelo ezibhekene no-Umgeni Water njengoba siyaphambili nje. Okuyizona zimqoka kakhulu lezi zinsalelo wuku:- sheshisa uHlelo lokufakwa kweziNgqalazizinda: ukwenza abasebenzi abanamakhono bangasishiyi, ikakhulukazi ubhekana nokulindelwe yiGDP okuyisilinganiso sika 6%: kanye nemiphumela yenqubo esenziwe ngcono, ehlahlwe ohlakeni lokusebenza i-Strategic Framework for Water Services. Umgeni Water uzobhekana nalezi zinsalelo ngokuthi uqhubeke nokubukeza izinhlelo zokuThuthukisa amakhono abantu ayingcebo, (Human Resource Development Plans), kanye nokuyenga inqubomgomo yokwenza ngcono inhlangano ngokubamba iqhaza uma kuboniswana ngezethulo kwi-SAAWU.

Enye insalelo emqoka ebhekene no-Umgeni Water, kanjalo futhi nezinye izinhlelo zamanzi ezaziwa ngokuthi "Water Service Provider", ukunikeza amandla kanye nokwesekala okuzoba yinhlelo (catalyst) yokuqinisekisa ukwenziwa kwemisebenzi yokulethwa kwamanzi nokulahlwa kwetshe lentaba nomshobingo. Umgeni usethubeni elihle lokuthi ubambe leliqhaza kanti futhi usuqalile ukusebenza kanzima, ngezindlela ezimbili ezizokusebenza wodwa kanye nokusebenza ngokubambisana nabanye, ukubhekana nale nselelo. Ubufakazi bubonakala ezikoleni lapho kunezinhlelo zemisebenzi yokulahlwa kwetshe lentaba nomshobingo eyenziwa ngokuhlanganyela noMnyango wezeMfundo wesifundazwe kanye nakwezinye izinhlelo zemisebenzi evela seyethuliwe ukuthi izokwenziwa noma ukwenziwa kwayo kuyahlelwa. Imisebenzi esohlelweni lokuthi yenziwe inezindleko ezidinga amamiliyoni (izigidi) amaningi amarandi, okukhombisa ukuzimisela ko-Umgeni Water mayelana nokwakhiwa kwezinqala zizinda ukuze ukudlulisela amanzi kubantu kwenzekile. Izinkontileka noma izivumelwano esenziwe ngokwe-Capital Infrastructure Programme kanye nezindleko zokuqhuba umsebenzi ezikhona njengamanje zixhumana ncamashi nenkambiso yemibhalo yesishayamthetho kanye nokuphathwa kwemigomomthetho yokusabalalisa, kanti futhi ziyalekelela kakhulu ukunqoba ezinye zezinsalelo ezibhekene nohlobo lomnotho olwaziwa ngokuthi-"second economy".

Kube unyaka onesasa ku-Umgeni Water, kodwa akupheli lapho. Asikwazi ukujabula ngokweqile noma singanaki lutho mayelana nesimo sempilo esiphila ngaphansi kwaso (environment). Sinendawo kulesi simo futhi siqhuba iqhaza lethu kuso, njengoba siyibhizinisi elingaphansi kukahulumeni, kumele senze isiqiniseko sokuthi lesi simo sibangcono. Umgeni Water ubekwe endaweni enhle ukuze ubhakane nesikhathi esizayo futhi uzongena kulesi sikhathi, njengoba unokuziqqaja ekutheni uzoqhubeka nokudlala indima ebalulekile, okukuqala ukwenza lokhu ngendlela yokusebenza yawo, okwesibili ngokwesifundazwe saKwaZulu-Natal emva kwalokho noma yilaphi eNingizimu Afrika.

Okokugcina, ngibonga abasebenzi bo-Umgeni Water ngomsebenzi omuhle abawenzile.



Mzimkhulu Msiwa
Chief Executive Officer

1.4 THE DIRECTORATE AND EXECUTIVE

The Board of Umgeni Water



Board Members from left - right

front row: Mr Zakes Dube, Ms Mina Lesoma, Ms Ndumi Medupe, Mr Nhlanhla Gasa, Ms Rosalie Manning

back row: Mr Vasu Gounden, Mr Neil Macleod, Mr Sidumo Dlamini, Mr Humphrey Buthelezi, Mr Busisani Mathebula, Ms Nombuso Afolayan, Mr Nhlanhla Dlamini, Ms Thokozile Shezi, Ms Jocelyn Armstrong & inset picture, Mr Josias de Kock

1. Mr Nhlanhla Gasa (55)

MComm, B Admin (Hons), National Dip. Physiotherapy
Re-appointed (second term) : July 2005
Chairman of the Board

Mr Gasa is the founder and Managing Member of Gasa & Associates CC, a Human Resources and Management Consultancy based in Umhlanga Rocks. He is an Executive Director of Digicore Fleet Management (Pty) Ltd and acting Chairman of the Digicore Holdings Board and Chairman of the ABSA Provincial Advisory Board. Mr Gasa also serves on the National Small Business Advisory Council (DTI).

2. Mr Vasu Gounden (45)

BA Law, LLB, LLM and graduate of Senior Executive Management Programme (SEP)
Re-appointed (second term) : July 2005
Deputy Chairman of the Board, Chairman of the Legal Committee and member of the Audit and Risk Committee

Mr Gounden is the founder and Executive Director of the African Centre for Constructive Resolution of Disputes (Accord) and has vast experience in Conflict Management. Mr Gounden also serves on the Boards of the University of KwaZulu-Natal, International Centre for Eye Care Education, The Working Group of Children in the Wilderness-Mkambathi project and International Advisory Board of the International Negotiation Journal.

3. Ms Nombuso Afolayan (29)

MBA, Executive Leadership, Cost & Management Accounting , B-Tech Management & OD Practitioner
Appointed (first term) : April 2004
Chairman of the Audit and Risk Committee

Ms Afolayan is the General Manager of Grindrod J & J Logistics. She also serves on the Natal Sharks Board as Deputy Chairman and on the Board of the Durban Chamber of Commerce. Ms Afolayan's speciality is Logistics and Supply Chain Management.

4. Ms Jocelyn Armstrong, (40)

CA (SA), MBA
Appointed (first term) : July 2005
Member of the Audit and Risk Committee

Ms Armstrong is Executive Director of Daylite Capital.

5. Mr Humphrey Buthelezi (41)

CA (SA)
Appointed (first term) : July 2005
Chairman of the Procurement, Fixed Assets and Capital Projects Committee.

Mr Buthelezi is the Executive Chairman of Wozani Berg Gasoline (Pty) Ltd. Mr Buthelezi is also the Chairman of the Audit and Corporate Governance Committees of AVI Limited and serves on the Competition Commission and Competition Tribunal.

6. Mr Josias de Kock (47)

CA (SA)
Re-appointed (second term) : July 2005
Non-executive member of Audit and Risk Committee

Mr De Kock brings extensive treasury and financial expertise to the Board.

7. Mr Nhlanhla Dlamini (48)

National Diploma in Public Health, Diploma in Advanced Management
Appointed (first term) : July 2005
Member of the Remuneration Committee and Audit and Risk Committee

Mr Dlamini is an entrepreneur with business interests in Port Shepstone, Durban and Pietermaritzburg.

8. Mr Sidumo Dlamini (40)

Diploma in General Nursing, Arts and Science and Diploma in Midwifery
Re-appointed (second term) : July 2005
Member of the Remuneration Committee and Legal Committee

Mr Dlamini is a Chief Professional Nurse at Prince Mshiyeni Hospital. He has vast experience in labour matters, which he acquired as an official of COSATU.

9. Mr Zakes John Dube (51)

BCom, MBA, graduate of the Harvard/Wits Business School Senior Executive Programme
Appointed (first term) : July 2005
Member of the Audit and Risk Committee and Fixed Assets and Capital Projects Committee

Mr Dube is the Regional General Manager of the SABC in KwaZulu-Natal.

10. Ms Mina Lesoma (42)

Diplomas in Public Relations, Local Government Management and Business Management
Re-appointed (second term) : July 2005
Chairman of the Remuneration Committee

Ms Lesoma is the Deputy Head: Customer Services of the eThekweni Metropolitan Municipality. She is also the Chairman of the KZN Playhouse Company and has extensive experience in Human Resources and local government matters. Ms Lesoma serves as an executive member of Durban Metro.

11. Mr Neil Macleod (55)

PrEng, BSc Eng, MBA
Appointed (first term) : July 2005
Member of the Procurement, Fixed Assets and Capital Projects Committee and Remuneration Committee

Mr Macleod is the Head of Water and Sanitation at eThekweni Metropolitan Municipality. Mr Macleod is also a Director of Johannesburg Water and Building Partners for Development.

12. Ms Rosalie Manning (44)

BA LLB
Appointed (first term) : July 2005
Member of the Remuneration Committee

Ms Manning is an independent consultant and has vast experience on matters relating to law, labour and marketing and strategy. Ms Manning serves as Director on various Boards, including Africa Heritage Investments, Trust Corporate Council, Sallister Diesel, Africa Heritage Corporate Solutions, CADE, Sizanani Engineering, AL Motori and Fervid Services Africa. Ms Manning is the owner of WORK AT IT.

13. Mr Busisani Mathebula (37)

BA Admin, Diploma in Project Management, Certificate in Local Government Administration and Management
Appointed (first term) : July 2005
Member of the Procurement, Fixed Assets and Capital Projects Committee

Mr Mathebula is the Chief Community Facilitation Officer for the City of Umhlatuze Local Municipality. Mr Mathebula is experienced in Water Services Policy, Water Services Infrastructure Project Management and Institutional and Social Development.

14. Ms Ndumi Medupe (36)

CA (SA)
Appointed (first term) : July 2005
Member of the Procurement, Fixed Assets and Capital Projects Committee and Audit and Risk Committee

Ms Medupe is a founder and partner of Xabiso Chartered Accountants and also serves as a Remco member of City Lodge. Ms Medupe has extensive experience in internal auditing, risk management and financial management.

15. Ms Thokozile Shezi (49)

BSc in Social Psychology and Education, Masters Degree in Measurement and Evaluation
Appointed (first term) : July 2005
Member of the Procurement, Fixed Assets and Capital Projects Committee and Remuneration Committee

Ms Shezi is a Director in the KZN Department of Agriculture and Environmental Affairs.

Executive Management



Ms Gugu Moloi
CEO
(Resigned in March 2006)



Mr Mzimkulu Msiwa
GM: Operations
(Acting CEO Effective April 2006)
(Appointed CEO Effective September 2006)



Mr Pumezo Jonas
GM: Engineering
and Scientific Services



Ms Nica Gevers
GM: Finance



Ms Pearl Maphoshe
GM: Corporate Services
(Resigned in January 2006)

1.5 CORPORATE GOVERNANCE

Umgeni Water is fully committed to sound corporate governance. The organisation actively embraces the King II Report, which advocates the need for institutions to be governed in accordance with its principles. Key initiatives during the period to ensure continued compliance with good corporate governance included:

- a review of the terms of reference of board committees;
- a review of board submission documents;
- a review of delegation of authority document;
- an evaluation of the performance of the Board and individual directors was conducted at the end of the financial year.

GOVERNANCE STRUCTURES

SHAREHOLDERS COMPACT

In accordance with the Treasury Regulations issued in terms of the Public Finance Management Act 1 of 1999 (PFMA), Umgeni Water must in consultation with its executive authority (the Minister of Water Affairs & Forestry), annually conclude a shareholders compact. The shareholders compact reflects the key financial performance measures and indicators to which Umgeni Water is committed.

Refer to page 63 for the main key performance indicators. The Board seeks to inform its Umgeni Water's Shareholders on all major developments affecting the organisation. This is accomplished through:

- Quarterly performance reports to the Shareholders;
- Annual Reports containing information about operations, financial and non-financial performance against key indicators;
- Detailed 5 year business plans as provided by the Water Services Authorities and the PMFA;
- Direct contact between the Chairman and Minister of Water Affairs and Forestry;
- Frequent communication at executive level on industry performance and policy issues.

BOARD OF DIRECTORS

Composition of the Board

In terms of the Water Services Act 108 of 1997 the Minister of Water Affairs & Forestry appoints the Board of Directors. The Umgeni Water Board consists of fifteen non-executive directors and the Chief Executive Officer. The Chairman of the Umgeni Water Board is Mr N Gasa.

The role of the Chairperson and that of the Chief Executive Officer are entirely separate. The Chairman is responsible for the overall leadership of the Board and is also a primary linkage between the Board, the executive authority and the Chief Executive.

The term of office of a non-executive director is for a period not exceeding four years. Non-executive directors may be re-appointed for a period not exceeding three consecutive terms of office. In terms of the PFMA the Board is the accounting authority of Umgeni Water.

The composition of the Board of Umgeni Water is reflected on page 12.

Board Charter

The Board Charter and Committees' Terms of Reference set out the operational and fiduciary responsibilities of the Board. In effect, the Board Charter and Committees' Terms of Reference serve to guide the Board and Committees in discharging their duties in order to ensure that the Board's independence is upheld.

Role and Functions of the Board

The key functions of the Board are to provide strategic leadership, ensure good corporate governance and be accountable for performance.

In order to ensure independence of the Board, the number of hours to be spent by the Directors doing Umgeni Water's work is limited.

Directors of the Board fulfil their roles through attendance of and participation at Board meetings. The Board of Umgeni Water meets at least bi-monthly to hold discussions and take decisions on matters relating to the organisation's business plan, budget, major capital expenditure, strategy and policies.

Remuneration

Directors are remunerated for their input, that is, for the time they devote to their duties as Board members. Their remuneration is calculated at an hourly rate determined by the Minister of Water Affairs & Forestry in April of each year. Different hourly rates apply to the Chairman, Vice-Chairman and Directors.

Company Secretariat Function

The Company Secretary is, *inter alia*, responsible for providing Directors with:

- guidance as to their duties, responsibilities and powers; and
- guidance on issues relating to compliance.

The Company Secretary also keeps the Board abreast of governance practices.

BOARD COMMITTEES

The Committees assist the Board in the performance of its duties and also in enabling effective decision-making. In terms of the Water Services Act 108 of 1997, the Board is authorised to delegate powers to the Committees established by the Board. The functions and powers delegated to Committees are set out in the Committees' Terms of Reference.

To enable the Committees to perform their duties, they have access to information and reasonable access to professional advice at the cost of the organisation.

The Board of Umgeni Water had six formally constituted Committees during the year.

Attendance at Board and Committee Meetings							
NAME	BOARD	MEETINGS OF THE BOARD					
		Strategy	Finance Committee #	Audit and Risk Committee	Procurement, Fixed Assets and Capital Projects Committee	Remuneration Committee	Chairs Committee
Mr N Gasa	8	2	N/A	N/A	N/A	6	1
Mr V Gounden	7	1	N/A	4	N/A	N/A	N/A
Ms T Shezi	7	2	N/A	N/A	1	6	N/A
Mr N Dlamini	8	2	N/A	5	N/A	5	N/A
Mr S Dlamini	9	N/A	N/A	N/A	N/A	3	N/A
Mr B Mathebula	8	2	N/A	N/A	2	N/A	N/A
Mr Z Dube	7	2	3	N/A	2	N/A	N/A
Mr N Macleod	6	2	N/A	N/A	1	6	N/A
Ms R Manning	6	2	N/A	N/A	N/A	4	N/A
Mr H Buthelezi	7	N/A	4	N/A	2	N/A	1
Ms J Armstrong	8	2	3	4	N/A	N/A	N/A
Ms N Medupe	8	2	N/A	4	1	N/A	N/A
Ms N Afolayan	8	2	3	6	N/A	N/A	1
Mr J de Kock	*	N/A	1	N/A	N/A	N/A	N/A
Ms M Lesoma	9	2	N/A	N/A	N/A	5	1
Ms R Mokate <i>Resigned In July 2005</i>	1	N/A	N/A	N/A	N/A	N/A	N/A
Ms G Moloi <i>Resigned as CEO In March 2006</i>	5	2	2	2	1	3	N/A
Mr M Msiwa <i>Acting CEO Effective April 2006</i>	5	2	1	2	1	3	N/A
Mr PMM Jonas	8	N/A	1	4	1	N/A	1
Ms N Gevers	8	2	4	5	2	N/A	N/A
Ms P Maphoshe <i>Resigned In January 2006</i>	4	N/A	N/A	N/A	N/A	3	1
TOTAL NUMBER OF MEETINGS	9	2	4	6	2	7	1

* Financial Specialist, attends meetings as and when required by the Board

The Finance Committee has been incorporated into the Audit and Risk Committee since April 2006

N/A = not a member of the specific Committee

Audit and Risk Committee

This Committee comprises six non-executive directors. Six committee meetings were held during the year. Most of the members of this Committee have financial backgrounds and the necessary skills and experience to ensure the effective functioning of the Committee.

The Committee monitors compliance with relevant legislation and ensures that there are appropriate internal controls and an integrated risk management process. The Committee also reviews the accuracy and reliability of the statutory financial reporting and monitors the organisation's financial risks.

The Committee reviews the activities and effectiveness of the internal audit function outsourced to the Gobodo Sizwentsaluba consortium. It is also responsible for meeting with the external auditors and reviewing accounting and auditing concerns identified by both the external and internal audit.

This Committee is assisted by two management committees, namely the Corporate Risk Management Committee and the Fraud Prevention Committee. The chairmen of both management committees attend all meetings of the Audit & Risk Committee and report on matters relating to risk and fraud prevention.

Remuneration Committee

This Committee comprises seven non-executive directors. Seven committee meetings were held during the year. The Committee reviews and considers all matters relating to:

- Human Resources policies;
- Conditions of employment of senior employees;
- Appointment of the Chief Executive Officer;
- Organisational transformation; and
- Remuneration for the Chief Executive Officer and members of executive management.

Procurement, Fixed Assets and Capital Projects Committee

This Committee comprises six non-executive directors. Two committee meetings were held during the year. The Committee was established to reaffirm and support Umgeni Water's commitment to timeous planning of capital projects, safeguarding of assets and improving the management of capital expenditure and capital programmes. This committee also ensures that proper procurement processes and empowerment targets are achieved.

Finance Committee

This Committee was in operation until June 2006 and has since been incorporated into the Audit and Risk Committee. This Committee comprised five non-executive directors. Its task was to oversee the management of financial assets and liabilities of Umgeni Water.

Chairs Committee

This Committee was set up to oversee stakeholder relations and to meet with stakeholders as and when necessary. The Committee met once during the financial year under review.

EXECUTIVE MANAGEMENT COMMITTEE (EXCO)

The Chief Executive Officer (CEO) is assisted by four General Managers in implementing the strategies, policies and decisions of the Board. In addition, the CEO is responsible for fostering a culture of compliance and for ensuring that all employees support and abide by the Code of Ethics.

The General Managers attend all meetings of the Board to report on the activities of their divisions.

The 2005/2006 Executive Management Committee was made up of Ms G Moloi (resigned as CEO in March 2006), Mr M Msiwa (General Manager: Operations and Acting CEO since April 2006 and CEO since September 2006), Ms N Gevers (General Manager: Finance), Mr PMM Jonas (General Manager: Engineering and Scientific Services) and Ms P Maphoshe (resigned as General Manager: Corporate Services in January 2006).

RISK IDENTIFICATION AND MANAGEMENT

The Board has taken an active role in ensuring that risk management is integrated into management systems and culture of the organisation. The Board has developed and approved a comprehensive risk management framework that articulates the risk management of the Board, its committees and management.

Risk management, being the responsibility of the Board, is discharged with the assistance of the Audit and Risk Committee. Umgeni Water has various processes in place to regularly identify and assess risks to its activities. These processes include effective control mechanisms to monitor and mitigate the impact of risk on its objectives. A Corporate Risk Management Committee, consisting of executives and senior managers, has been established to assist the Board to manage all business risks.

The organisation's zero-based risk management approach identifies, analyses and manages risks in order to achieve an optimal risk/reward profile for stakeholders by minimising losses and maximizing gains. A Risk Accountability Matrix has been developed to reflect a framework for risk accountability from a line management and functional perspective.

A fraud prevention plan has been developed by the Fraud Prevention Committee in accordance with the Public Finance Management Act. An external person chairs the Fraud Prevention Committee. Umgeni Water continues to operate the Fraud Prevention Hotline, which is administered by KPMG. The whistle blowing facility has assisted in ensuring that the risk of fraud is minimised, monitored and investigated when required.

AUDIT AND CONTROLS

The Board is responsible for the maintenance of effective and efficient systems of internal control. The internal control systems are designed to provide reasonable assurance that assets are safeguarded and that liabilities and working capital are efficiently managed.

Principal features of the group's internal finance controls are:

- A system of financial planning, budgeting and reporting which allows continuous monitoring of performance.
- Clearly defined delegations of authority.
- The establishment of a short, medium and long-term funding strategy.
- The tariff model which determines the financial impact of capital expenditure and the bulk water tariff on Umgeni's debt curve.

To assist the Board in the discharge of its responsibilities, Internal Audit undertakes independent assessments of the internal control systems and business risks and reports to the Board through the Audit and Risk Committee. The risk-based audit plan covers major risks emanating from Umgeni Water's integrated risk management process.

The external auditors are responsible for independently auditing and reporting on the financial statements in accordance with the International Financial Reporting Standards (IFRS).

STAKEHOLDER COMMUNICATION

Umgeni Water is a state-owned business enterprise and, as such, recognises the importance of presenting stakeholders with a fair, accurate, transparent and understandable assessment of its operational and financial results. It, accordingly employs a wide range of communication tools to engage with its staff, investors, strategic partners, executive authority and the general public. Umgeni Water also complies with the Promotion of Access to Information Act 2 of 2000.

The enhanced relations that emerged as the products of stakeholder interaction in 2005/2006 have set an exciting tone for the year ahead, when Umgeni Water will continue to invite stakeholder and customer input on matters of mutual interest and concern in the organisation's primary and Section 30 activities. These section 30 activities include management and training services, catchment management services, laboratory services and joint ventures with other water services authorities.

Umgeni Water engaged with stakeholders in a variety of ways in the year under review and the main interactions included:

- The 2006/2007 Bulk Water Tariff Consultation. Umgeni Water followed a full consultation process with its customers, SALGA, National Treasury and DWAF thereby meeting the requirements in terms of S42 of the Municipal Finance Management Act 56 of 2003. The process was transparent and took into account the organisation's financial requirements as well as customer needs in terms of affordable price increases. All stakeholders were supportive of the 4.6% tariff increase, which became effective from 1 July 2006.
- The participation of Umgeni Water's shareholder, DWAF and customers in an Umgeni Water Executive Strategy Planning Session.
- The signing of a memorandum of understanding between Umgeni Water and other water utilities in KZN, namely uThukela Water and Mhlathuze Water.
- Engagement on the KwaZulu-Natal Bulk Water Supply Strategy, which is intended to provide support to eradicate the water backlogs in KwaZulu-Natal. Presentations were made to the SALGA, municipalities and other water utilities.
- Regular meetings with a key internal stakeholder, the National Education, Health and Allied Workers' Union (NEHAWU), on corporate matters of an operational and strategic nature.
- A series of interactive briefing sessions on the new pipeline projects, which represent major infrastructure investments by Umgeni Water in KwaZulu-Natal.
- The media, both print and electronic, were briefed at regular intervals on activities of Umgeni Water that are in the public interest. In the period under review, Umgeni Water also interacted with the media on water quality-related issues that dominated public debate, among them the so-called rat-tailed maggots-in-domestic-water saga and municipal customer concerns relating to the colour and smell of water in certain areas.
- The provision of data on a monthly basis to the South African Association of Water Utilities on performance against Benchmarking Performance Indicators: Water and Sanitation.

COMPLIANCE LEGISLATION

As a good corporate citizen, Umgeni Water complies with the laws of the country. The organisation's policies are continually reviewed to ensure it responds to relevant legislation.

The Water Services Act 108 of 1997, as amended, and the PFMA set out the exact operational and fiduciary duties of the Board. In order to increase the Board's understanding of the legislation, Umgeni Water's induction programme for the Board includes briefs on these legislations.

In addition, Board members are kept abreast of developments in legislation through presentations and memoranda.



DV Harris Water Works



What we do



Nagle Dam Diversion Gates



Nagle Dam

2.1 THE UMGENI WATER VALUE CHAIN

The primary activity of Umgeni Water is to provide water services to other water services institutions within its service area. This includes water supply services, encompassing the abstraction, conveyance, treatment and distribution of potable water, as well as sanitation services, comprising the collection, removal, disposal or purification of domestic wastewater, sewage and effluent. With respect to water supply services, Umgeni Water provides a second tier (or bulkwater services) function. However, sustainability of its water services business relies intrinsically on sustainability of the water resources in its abstraction catchment areas as well as effluent receiving systems.

Recognising that the responsibility for managing water resources lies with Water Management Institutions, such as; DWAF and Catchment Management Agencies, amongst others, Umgeni Water's policies are to ensure that it influences the custodians in respect of its resource requirements and resource protection needs, and that the interests of Umgeni Water and its customers are supported by the relevant Water Management Institutions. In addition, Umgeni Water adopts a business approach to providing services to Water Management Institutions on an agency basis.

Notwithstanding legislative imperatives, Umgeni Water is very mindful of the need for environmental sustainability within the context of its social and economic development thrusts and its commitment to environmental management principles. Overall, the corporate environmental goal is to conserve scarce natural resources and reduce its environmental impacts in all aspects of its business and throughout the life-cycle of its projects. Umgeni Water therefore implements sound environmental impact assessment practices in implementing its water services business.



River

Resource quality is assured by monitoring and assessing rivers feeding our water supply dams, to flag risks to quality and to lobby the relevant catchment management authorities.



Dams

Through partnerships, Umgeni Water is developing water resource utilisation plans for the dams it manages in the interests of assuring a balance between economic development, community benefits and resource sustainability. A systems approach and operating rules are used to manage supply risk and cost effectiveness.



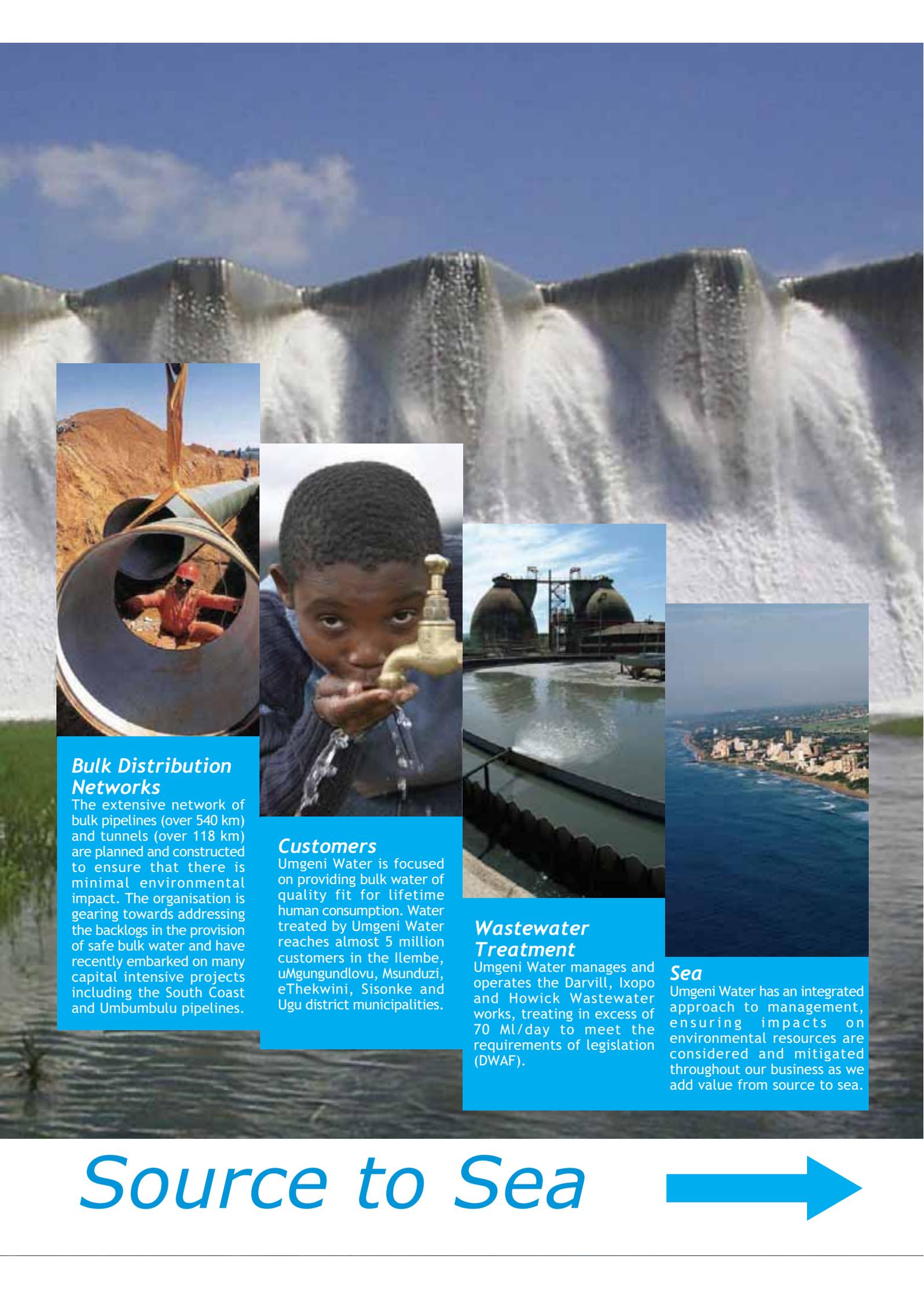
Water Treatment Works

ISO 9001: 2000 certified water treatment works treat over 1000 ML per day. Our treatment systems are informed by research and development utilising the most appropriate technology. Quality is assured by treating to current South African national standards for drinking water specifications.

The ISO 17025, SANAS accredited laboratory conducts a wide range of analyses used to assess the integrity of water and wastewater treatment and environmental water quality.

The laboratory boasts state of the art technology and continually strives to keep abreast of the latest advancements in water analyses.





Bulk Distribution Networks

The extensive network of bulk pipelines (over 540 km) and tunnels (over 118 km) are planned and constructed to ensure that there is minimal environmental impact. The organisation is gearing towards addressing the backlogs in the provision of safe bulk water and have recently embarked on many capital intensive projects including the South Coast and Umbumbulu pipelines.



Customers

Umgeni Water is focused on providing bulk water of quality fit for lifetime human consumption. Water treated by Umgeni Water reaches almost 5 million customers in the Ilembe, uMgungundlovu, Msunduzi, eThekweni, Sisonke and Ugu district municipalities.



Wastewater Treatment

Umgeni Water manages and operates the Darvill, Ixopo and Howick Wastewater works, treating in excess of 70 ML/day to meet the requirements of legislation (DWAf).



Sea

Umgeni Water has an integrated approach to management, ensuring impacts on environmental resources are considered and mitigated throughout our business as we add value from source to sea.

Source to Sea





Wiggins Water Works



**How we
are doing**



Mearns Weir

3.1 CO-OPERATIVE SERVICE DELIVERY

3.1.1 KwaZulu-Natal Bulk Water Services Strategy

The national government has committed itself to eliminating the backlogs in basic water services and to progressively improve levels of water service (i.e. water and sanitation) throughout the country. The Minister of Water Affairs & Forestry announced that since 1994 National Government “have reduced the water backlog by half and reduced the sanitation backlog from 52% to 31%” and the government will “stick to its targets of addressing the backlog of access to water and sanitation”. Provincial and Local Government are committed to achieving the same targets and are working tirelessly to this end. However, it is evident from table below that there is still a high percentage of households within the province of KwaZulu-Natal who live in poverty, without the basic service levels of water and sanitation. All other national and local stakeholders need to contribute towards improving the level of water services, particularly in the current backlog areas. Investments in water services have a direct impact towards stimulating economic growth and thereby reducing levels of poverty.

<i>Selected Living Conditions in KwaZulu-Natal per District Municipality</i>				
Municipality	Number of households ¹	Living in Poverty ²	Without Water ³	Without Sanitation ⁴
Amajuba District	98 219	46.3%	37.1%	42.0%
eThekweni Metropolitan*	824 371	35.5%	17.0%	28.5%
iLembe District*	130 016	61.8%	57.4%	62.7%
Sisonke District*	76 344	69.1%	48.1%	62.5%
Ugu District*	158 443	62.5%	65.6%	64.4%
uMgungundlovu District*	234 781	47.9%	26.2%	44.4%
uMkhanyakude District	105 731	71.8%	73.9%	76.9%
uMzinyathi District	95 020	72.2%	66.8%	69.9%
uThukela District	138 840	59.5%	50.8%	61.2%
uThungulu District	189 741	61.2%	51.7%	61.0%
Zululand District	150 993	66.4%	62.8%	71.0%
KwaZulu-Natal total	2 202 542	51.1%	39.0%	48.5%

Source: The Gaffney Group and South African Local Government Association, Gaffney’s Local Government in South Africa 2004-2006, December 2004.

- 1) Household refers to a formal and traditional housing, as opposed to informal dwellings/shacks
 - 2) Households living in poverty are defined as those spending less than R1 100 a month.
 - 3) Water refers to piped water on community stand at a distance of less than 200m from dwellings.
 - 4) Sanitation refers to the minimum of a pit latrine with ventilation.
- * Umgeni Water customers

Umgeni Water and Mhlathuze Water together with the multi-jurisdictional entity uThukela Water recognise that a large-scale co-ordinated and integrated approach on a regional basis is required to provide a holistic solution to providing water services. Umgeni Water was therefore instrumental in driving a regional initiative focused on improving access to water services through partnerships with national, provincial and local government in KZN.

This initiative will assist in accelerating water service provision by streamlining activities, especially in accessing finance and prioritising and driving delivery. The primary aims of the KZN Bulk Water Services Strategy are to:

- Provide a vehicle to align the water service delivery plans of the major role-players in the water sector, namely the national government through the DWAF and the Department of Provincial and Local Government (DPLG), provincial and local government and the regional and local water service providers;
- Ensure that water service delivery within KZN is improved through a sustainable implementation plan focussed on the eradication of water and sanitation backlogs;
- Improve the efficiency of the water service delivery mechanisms in KZN;
- Investigate funding options available for implementing large scale water infrastructure delivery programmes.

The initiative is not intended to erode or compete with the efforts of the Water Services Authorities, but is aimed at supporting them in addressing challenges. Umgeni Water is therefore committed to the co-ordinated implementation of regional bulk water supply schemes to ensure that high quality potable water is provided on a sustainable basis to the Water Service Authorities (WSAs) within its area of operation. This water is to be provided at strategic locations to enable the WSAs to reticulate potable water to those communities in most need.

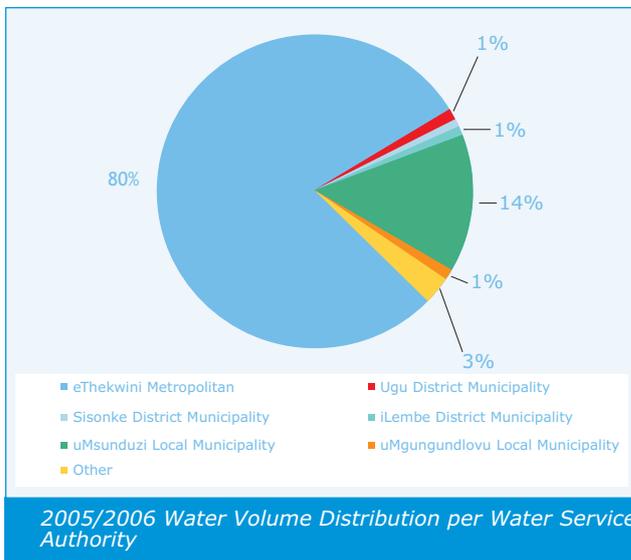
Umgeni Water, together with its partners has been actively working towards achieving the aims of this initiative and the following milestones have been achieved to date:

- Discussions and liaisons have already taken place with all spheres of government. In particular, one-on-one liaisons with the WSA's within the province to obtain commitment and participation in the initiative. Umgungundlovu District Municipality has passed a Council Resolution adopting the KZN Bulk Water Services Strategy. The need to have the KZN bulk water supply and sanitation plans incorporated into the relevant WSDPs and IDPs is recognised;
- The Steering Committee directing this initiative has been expanded from the Chief Executives of the three KZN water utilities to include officials from DWAF, DPLG, the Department of Local Government & Traditional Affairs (DLGTA) and the Municipal Managers of the WSAs within KZN;
- Task teams have been formed to provide expertise and input to the initiative. DWAF has nominated officials from both its national and KZN regional offices to participate in the Water Technical Task Team and the Sanitation Technical Task Team, while the Department of Local Government & Traditional Affairs is to be represented on the Financial Task Team;
- Terms of Reference for a Programme Office to co-ordinate all the activities associated with this initiative are currently being compiled. Leadership of this office is to be provided by DWAF and DPLG;
- The Concept Plan for regional bulk water supply schemes within KZN has been completed and has been used as the discussion document during liaison with all stakeholders and role-players; supply routes can also be linked to other economic development and service delivery initiatives;
- Liaison between the relevant Water Services Authorities, DWAF, and Umgeni Water is taking place to ensure that all water services planning and development is taking place in a joint and integrated manner;
- Bulk water supply infrastructure that is in line with the KZN Bulk Water Services Strategy is at various stages of planning and implementation, ranging from the Eston-uMbumbulu pipeline which has already been constructed to the Mzintlava Regional Scheme that is still at the conceptual planning stage;
- The Concept Plan for a regional approach to sanitation within KZN is currently being drafted. The sanitation component of this initiative is to be integrated as closely as possible to the water component and its roll-out will be driven by the proposed Programme Office;
- Project financial analysis techniques have been developed to assess multi-source funding options, and various funding alternatives have already been explored.



3.1.2 Bulk Supply Agreements

The Water Services Act 108 of 1997 compels Water Boards to regulate their business with their Customers through signed contractual agreements, known as Bulk Supply Agreements.



Umgeni Water has concluded 20 year agreements with its major customers, eThekweni Municipality, uMgungundlovu, Ugu and Ilembe District Municipalities. An agreement with the Msunduzi District Municipality has not yet been finalised.

The objective of the agreement is to formalise and regulate the level of service of providing bulk water. The technical parameters comprise quality and quantity specifications enhanced by monitoring, reporting and billing requirements. The Agreement also regulates meter testing requirements and planned and emergency interruptions to supply.

Umgeni Water meets its customers monthly to discuss operational matters and improvements. In the past year these joint efforts contributed to an emergency supply

condition at Cato Ridge being averted and a dynamic pumping load shed between the Durban Heights and Wiggins Water Works. A minimum disruption to supply due to maintenance shutdowns by Umgeni Water's Operations team is achieved by operational planning with the customer.

3.1.3 Water and Sanitation Programme in Schools

Umgeni Water established a partnership with the KwaZulu-Natal Department of Education for Water and Sanitation Infrastructure development in Schools within the uMgungundlovu, Sisonke and Ugu District Municipality areas. This partnership was founded on a common vision for creating a conducive learning environment for pupils and affording them a right to privacy. The facilities together with health and hygiene education will improve school attendance especially for the young girls facing sanitary challenges at puberty stage.

Umgeni Water's passion is supported by its corporate values and strategic objective to promote water and sanitation access in partnership with government structures and other institutions to improve the wellness, health and hygiene of communities. To this end, we are proud to report that 54 projects benefiting 30,200 learners were completed.



The programme had local economic development spin-offs with total spending on emerging contractors amounting to R36 million. Contractor payments to local labourers amounted to R4 million, 20% of whom are women. The programme is one of the cornerstones of poverty alleviation and creation of employment opportunities in line with the Expanded Public Works Programme. The success in terms of skills transfer to local unskilled labour and emerging contractors will go a long way in making some of the objectives of ASGISA a reality. Contractors who have always sub-contracted for small jobs were awarded contracts as high as R 3,2 million. This elevated their CIDB (Construction Industry Development Board) ranking and will now qualify them for even bigger projects in the fast growing construction industry.

Umgeni Water's commitment and performance resulted in the KwaZulu-Natal Department of Education gaining confidence in the organisation and have awarded Umgeni Water further projects. These entail forty new projects for the 2006/2007 financial year with a further three year roll over to other schools. The commitment for the 2006/2007 financial year is R46 million. The KwaZulu-Natal Department of Education a valued customer and has made an undertaking to go an extra mile by accepting further projects to help it build laboratories, computer rooms and resource centres as part of the school curriculum upgrade. The success of this partnership is a reflection of a good working relationship with the Department, the School Governing Bodies, Principals, Ward Councillors, Provincial Treasury, Department of Works, Department of Labour, contractors and local communities.

3.1.4 Process Engineering Support to District Municipalities

Umgeni Water has played a proactive and supportive role to municipalities both in its area of water supply in KZN and nationally. In this regard Umgeni Water has built a strong and close relationship with Water Services Authorities and other water utilities.

Umgeni Water assisted the uThukela District Municipality by designing the Moyeni Zwelisha Water Works and provided operator training and the development of an operating guideline as well as operation and maintenance manuals.

Water quality problems were resolved at the Creighton Water Works in the Sisonke District Municipality by the installation of an innovative constant head dosing system that works without electrical power.

Umgeni Water Process Engineers undertook a detailed assessment and optimization of the Kokstad Water Works and have compiled a long term plan to assist with on-going technical support.

High concentrations of iron and manganese were found to be the major cause of consumer complaints in the town of Richmond in the uMgungundlovu District Municipality. This was solved by modifying the treatment process and changing to an alternative raw water source.

Umgeni Water undertook a detailed process audit of 48 small water works in KwaZulu-Natal as part of a Water Research Commission Project. The aim of this project was to improve the efficiency of disinfection in small treatment plants in South Africa. This was part of a national survey of 188 plants in South Africa. Problems identified included a lack of technical support, poor design, a lack of maintenance management skills and technical training.

A multidisciplinary team of engineers from Umgeni Water responded to a call for assistance from the OR Tambo District Municipality. The team solved a water supply crisis and spent a few days in Umtata resolving water supply problems that were traced to non-functioning air valves.



Water fit for lifetime consumption

3.2 PRODUCT QUALITY ASSURANCE

3.2.1 Working Together with Municipalities for Water Quality Assurance

Umgeni Water has adopted a partnership approach to assuring water quality and protecting public health. During the year, a variety of water quality concerns were raised by end consumers - the general public, bulk water recipients, industrial users and the media. A number of investigations were undertaken, often in partnerships with the relevant Municipalities involved.

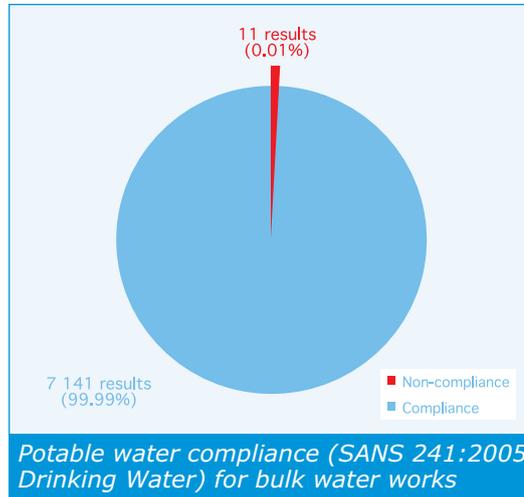
The most newsworthy, but possibly of the least real concern, was about “rat tailed maggots” being reported in Pietermaritzburg and elsewhere. Investigations conducted, both internally and independently by Municipality Health in the wake of the media inquiries, have found that the water treated and stored by Umgeni Water contains no maggots or any other insects and meets the required drinking water standards. This same story was encountered in many other parts of the country, to the extent that research papers have been written on the topic, always with the same outcome.

Umgeni Water’s routine water quality monitoring has, on several occasions, led to detailed follow up investigations if initial results indicated a potential for quality problems to develop, for example:

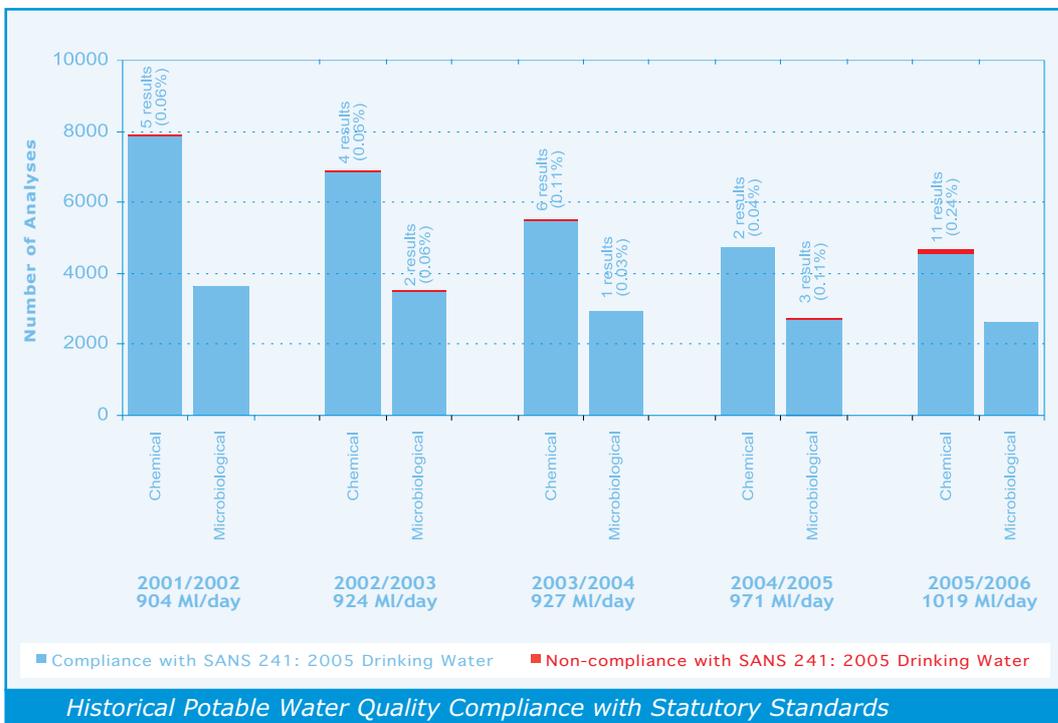
- In the North Coast supply area, a number of distribution reservoirs samples showed indications (despite the adequate presence of chlorine) of a concerning number of bacteria. Multiple samples of water from houses in the area all fully complied with drinking water requirements, which then led to close investigation of the reservoir sample taps themselves.
- In Pietermaritzburg, extensive follow up was undertaken after distribution reservoirs levels were allowed to drop below the ideal level, and when re-filled in a hurry, forced the very fine sediment accumulated over the course of years, to be re-suspended. This led to tap water throughout most of Pietermaritzburg becoming discoloured. Although the drinking water complied with the SANS 241 Drinking Water specification, the city’s residents who have for so long been used to exceptional water quality, raised considerable alarm. Thus, in addition to the distribution sampling normally undertaken by Umgeni Water in the Msunduzi Municipality area, intensive monitoring of house taps, public buildings and industries throughout the city and suburbs was also undertaken, in full collaboration with the Msunduzi Municipality. An independent laboratory also analysed many samples taken by the Municipality where specific complaints were made. Despite these concerns, the water remained safe to drink, and while the initial problem in the distribution network persisted for a while; ongoing alarms over this were due to localised problems caused by pipeline bursts and repairwork in the Pietermaritzburg area. Lessons have however been learned from this, and steps including a more vigorous reservoir cleaning campaign are being taken to avoid the re-suspension problem re-occurring.

3.2.2 Potable Water Quality Compliance

Umgeni Water regularly monitors potable water quality to assess its fitness for use by consumers. The nationally regulated SANS 241:2005 Drinking Water specification for chemical and microbiological quality of drinking water was used to assess the compliance of water produced at Umgeni Water water works. The overall compliance for the bulk water works, based on chemical and microbiological tests conducted and weighted according to volume produced was 99.99 percent. According to SANS 241: 2005 Drinking Water, this classifies the water quality as excellent.



The historical water quality compliance measured against SANS 241: 2005 Drinking Water for the bulk water works for the current and past four years is shown below. The number of tests conducted has decreased slightly due to operational efficiencies and monitoring rationalisations, while still meeting the minimum monitoring frequencies recommended in SANS 241: 2005 Drinking Water. Of a total of 7 152 analyses conducted on water works final waters, only 11 results did not comply.



The table below shows the performance of the different water works and lists those test results which caused failure for the different categories.

<i>Potable water compliance for water works</i>						
Bulk Water Works	Average volume treated daily (ML/d)	Compliance with SANS 241: 2005 Drinking Water		Classification of Water Quality supplied*	Magnitude of non-compliance	
		Chemical	Microbiological		Constituent	Concentration
Midmar	188	100	100	Excellent	-	-
DV Harris	46	100	100	Excellent	-	-
Ixopo	2.1	100	100	Excellent	-	-
Durban Heights	516	100	100	Excellent	-	-
Hazelmere	33	100	100	Excellent	-	-
Wiggins	186	100	100	Excellent	-	-
Ogunjini	1.01	100	100	Excellent	-	-
Amanzimtoti	28	100	100	Excellent	-	-
Craigieburn	5.8	100	100	Excellent	-	-
Mtwalume	4.3	100	100	Excellent	-	-
Umzinto	6.2	99.1	100	Excellent	Aluminium	674 – 939 µg/l (standard 500 µg/l)
					Trihalomethanes	308 µg/l (standard 300 µg/l)
Umbumbulu	2.2	95.4	100	Good	Turbidity	5.33 – 14.6 NTU (standard 5 NTU)
					Aluminium	566 µg/l (standard 500 µg/l)

* SANS 241 classifies:

Excellent water quality as ≥99% compliance with Microbiological requirements, ≥95% compliance with Class I Chemical requirements and ≥97% compliance with Class II Chemical requirements

Good water quality as ≥98% compliance with Microbiological requirements, ≥90% compliance with Class I Chemical requirements and ≥95% compliance with Class II Chemical requirements



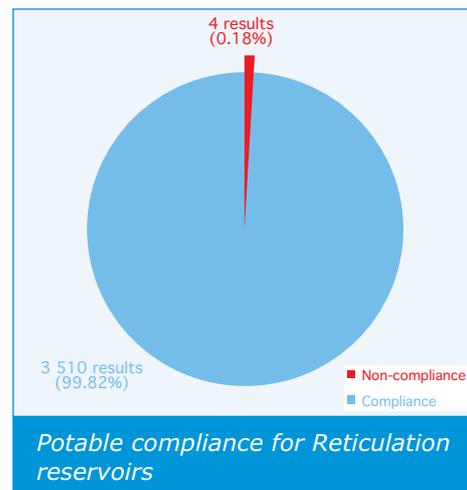
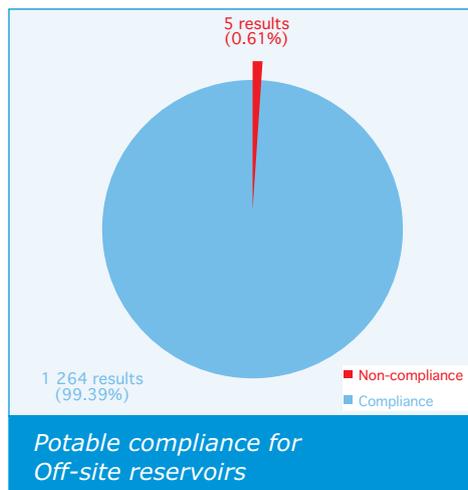
Sand Filters at Wiggins Water Works

The Umzinto Water Works failed to meet the required limit for trihalomethanes on a single occasion as a result of poor raw water quality due to pollution problems in the Mzimayi catchment. Mitigation measures introduced included the introduction of pre-oxidation with potassium permanganate at the water works and active participation in the Mzimayi Catchment Forum.

The turbidity and aluminium non-compliant results at the Umbumbulu Water Works were due to unforeseen operational problems. Mitigation measures introduced include increased chlorination and microbiological monitoring. At all stages the microbiological results indicated that the water was safe to drink.

Similar assessments were carried out for all off-site and reticulation reservoirs fed by Umgeni Water treatment works.

Excellent potable water quality compliance was achieved at the off-site and reticulation reservoirs, with 99.8 and 99.4 percent compliance respectively.



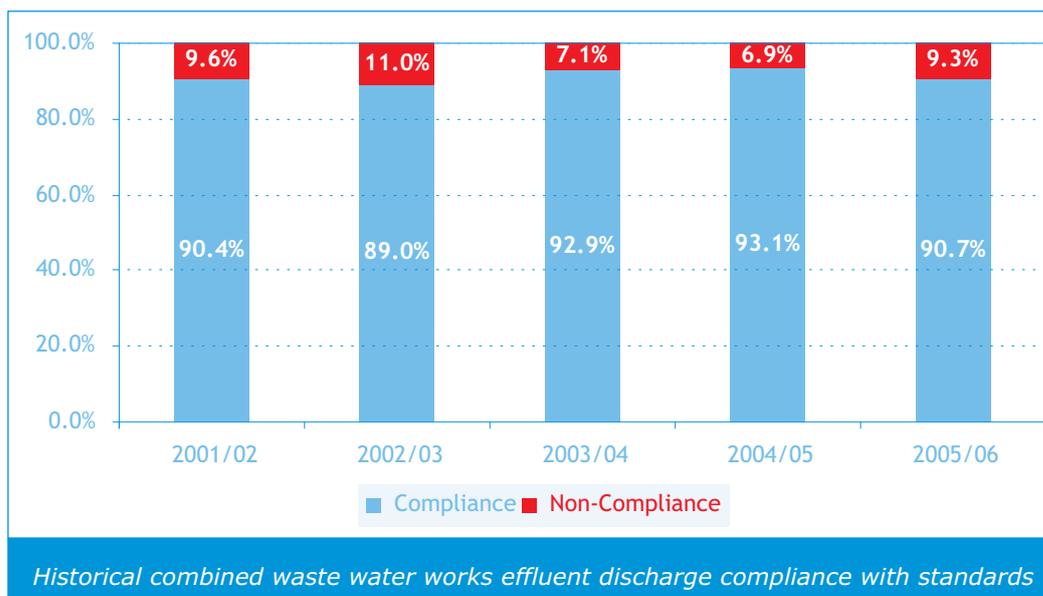
3.2.3 Wastewater Quality Compliance

Effluent Compliance

Discharges emanating from wastewater works operated, managed and/or owned by Umgeni Water were monitored to assess the compliance of wastewater effluent quality with prescribed DWAF standards for effluent. The DWAF standards to measure compliance were :

- The DWAF General/Special effluent discharge standards and Exemption Permit 2045B at the Darvill Wastewater Works.
- The DWAF General/Special effluent discharge standards and Exemption Permit 1887B at the Howick Wastewater Works.
- The DWAF General Authorisation General Limits at the Ixopo, ALbert Falls North and South Wastewater Works.

The historical wastewater works compliance for the past five years for all sites is shown on page 36. The overall effluent compliance was 90.7 percent between July 2005 and June 2006, indicating a slight deterioration compared to the previous period. Effluent compliance at the Umgeni Water owned and operated wastewater works at Darvill and Ixopo was satisfactory. However, effluent compliance at the Howick WWW was poor at 81% compliance, primarily due to non-compliant *E.coli* results. Despite frequent chlorine overdosing, the *E. coli* standard of zero per 100ml is unachievable at this site due to limitations associated with the small chlorine contact tank. This problem is currently being addressed with the relevant municipality who have since sourced funds for the upgrade of the chlorine contact tank.



Sludge Compliance

Sludge disposal from Darvill, Ixopo and Howick Wastewater Works is evaluated in terms of protecting the public and the environment from the negative impacts of sludge disposal. Each Works is scored on its planning, execution and monitoring of a responsible sludge disposal programme. The Umgeni Water owned and operated plants at Darvill and Ixopo have continued to perform well, demonstrating the organisation’s commitment to the sustainable operation of its works. The plant at Howick, operated under contract from the Municipality experienced sludge related operational problems due to the inadequate removal of sludge from the works. This problem has been highlighted to the local Municipality who have been attempting to resolve the matter.

Wastewater Works Sludge Disposal & General Site Acceptability *					
SITE	2001 - 2002	2002 – 2003	2003 – 2004	2004 – 2005	2005 - 2006
Darvill	74 %	82 %	87 %	94 %	86%
Ixopo	70 %	51%	61%	66 %	66%
Howick	-	-	18%	57 %	49%
Other small UW WWW	Not Assessed	65%	60%	63%	53%

* Overall assessment of compliance of operation (as a %) against best practical options available



Anaerobic Digestors at Darvill Wastewater Works



uMzinto River

3.3 WATER RESOURCES MANAGEMENT

3.3.1 Water Resource Quantity

Umgeni Water is directly involved in the management of the water resources from which it abstracts the raw water for treatment and distribution to its customers. A crucial management function is ensuring that the appropriate levels of assurance of supply are maintained. The rapid growth in the demand for water that has been experienced within the Umgeni Water area of supply over the past few years, coupled with sustained periods of low rainfall over some areas, has exerted pressure on the maintenance of current assurance levels. Raw water quantity is the primary factor that drives the operating rules throughout the water resource systems. There are however secondary disciplines which have the potential to influence, in varying degrees, the operating rule. Umgeni Water has initiated a risk assessment of the impact of raw water quality, environmental and social issues and dam safety matters, on the operating rule dominated by water resource quantity.

uMngeni System

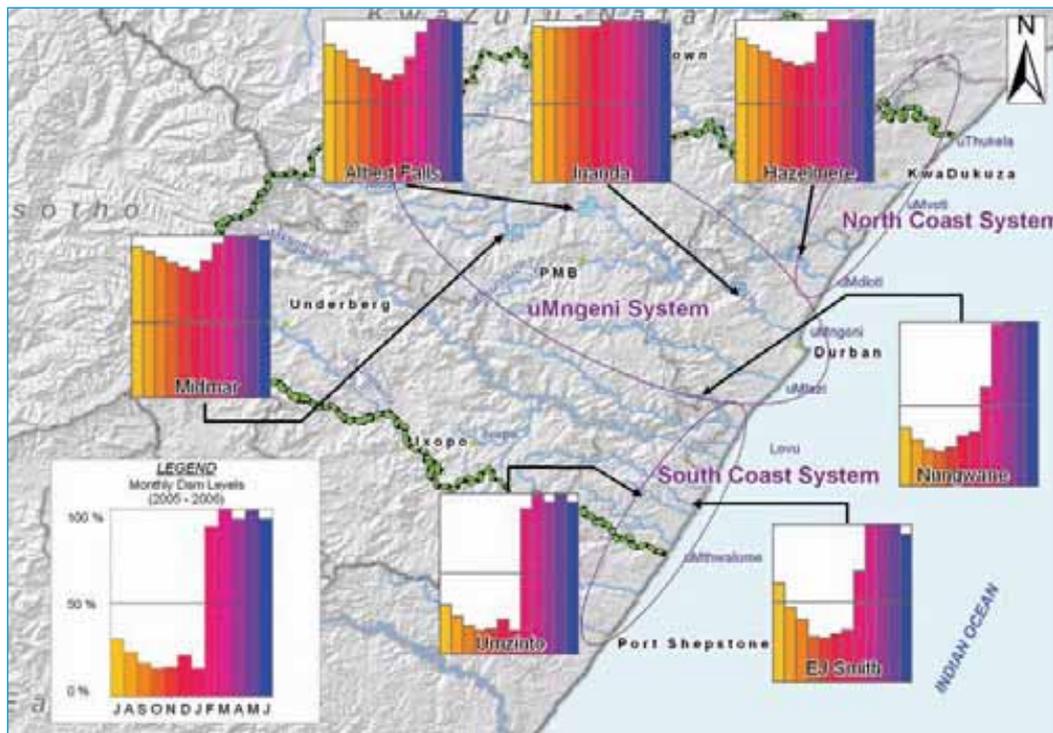
Due to the high concentration of industries and economic importance of the greater Durban and Pietermaritzburg area, water is provided to this region at a 99% level of assurance from the uMngeni system, which comprises Midmar, Albert Falls, Nagle and Inanda dams as well as the Mooi-uMngeni Transfer Scheme (Phase 1).

Over the past year, the water available for abstraction from the uMngeni system was maintained as high as possible by pumping water from the Mooi River to Midmar Dam whenever it was available. Pumping commenced in December 2005 and continued until the end of April 2006. This action ensured that all impoundments on the uMngeni System were spilling prior to the onset of winter.

Further augmentation of the uMngeni system is urgently required in order to ensure the levels of assurance are maintained in the long-term to meet the sustained increases in water demand. DWAF is currently making a concerted effort to expedite the implementation process for Phase 2 of the Mooi-uMngeni Transfer Scheme to include the construction of the Spring Grove Dam. They also need to commence with the detailed planning on the next augmentation scheme beyond this.

South Coast System

Water is provided to the upper and middle south coast areas at the standard 98% level of assurance from the South Coast system, which comprises the Umzinto, EJ Smith and Nungwane dams as well as abstractions from the uMkomazi and uMtwalume rivers.



Umgeni Water Operational Area showing Dam Level Status in the Three Systems

During 2005/2006, localised drought conditions persisted along the South Coast of KwaZulu-Natal. Below average rainfall was recorded for a second season in succession and this resulted in the Nungwane, Umzinto and EJ Smith dams being at record lows (20%, 14% and 5%, respectively). As a result, Ugu District Municipality implemented water restrictions in the middle south coast area during August 2005, eThekweni Water Services also imposed limited domestic restrictions in the lower parts of the eThekweni Metropolitan. Emergency water transfers were put in place from uMkomazi and uMtwalume rivers in order to augment the supply of water from the Umzinto and EJ Smith dams. In addition, Umgeni Water started using water from the uMngeni system for the Amanzimtoti area in order to conserve the water resources of Nungwane Dam. Late rains fell during the first three months of 2006 resulting in the three dams spilling by the end of March 2006. This allowed the water restrictions to be lifted in all affected areas.

The limited yield of the dams and river abstractions in this system highlights the need for a long-term intervention in the area to address the ongoing water resource shortages experienced. To this end, Umgeni Water has embarked, during its initial phase, on the implementation of the South Coast Pipeline to transport water from the uMngeni catchment as far south as Scottburgh .

North Coast System

The North Coast area from Verulam to KwaDukuza is provided with water at the standard 98% level of assurance from Hazelmere Dam on the uMdloti River.

Whilst this supply is presently able to meet the water demands in the area at the required level of assurance, the significant pace with which urban development is taking place in this region, is placing strain on the water resource. Hence, further augmentation is required within the next few years, and Umgeni Water has requested DWAF to commence with the raising of the full supply level of Hazelmere Dam to achieve this. DWAF also need to commence with the detailed planning of the next augmentation scheme for this region to follow the raising of the wall of Hazelmere Dam.

Currently, it is envisaged that Hazelmere Dam will need to be raised by 7m to its full height in the near future to meet the demands in the North Coast System. Even with this planned raising of the dam and the Hazelmere system's interconnection with the Tongati and uMvoti systems, this resource is inadequate for the long-term requirements of the North Coast System.

3.3.2 Water Resource Quality

Resource quality management at Umgeni Water is driven by the need to assure customers of sustainable water supplies. During the year under review water quality management interventions included minimising risks relating to aquatic and terrestrial weeds, eutrophication, pathogens, soil erosion, chemical contamination and river health.

Aquatic/Water Weeds Risk: An integrated approach to control of aquatic weeds comprising biocontrol and herbicide spraying was undertaken and required close cooperation between Umgeni Water and DWAF Working for Water. A major concern was development of large amounts of water lettuce in the Albert Falls system which required periodic introduction of biocontrol and herbicide application. At Ixopo, the re-emergence of Kariba weed in the Ixopo Bux dam catchment required aerial-spraying by Working for Water and biocontrol. At Inanda and Shongweni dams periodic herbicide spraying had to be undertaken as a result of the continued influx of Water Hyacinth from the upstream uMsunduzi system. Overall, aquatic weed infestation at the end of the reporting period was acceptable.

Pathogen Risk: Pathogen risk was assessed using *E. coli* as a risk indicator. No major risks were noted at abstraction points for large water works systems. The uMsunduzi system, however, continued to display impacts from sporadic pollution events. Work with the Msunduzi Municipality and catchment forums, including interaction on sewer and river quality problems, continued.

Soil Erosion Risk: During the year, complaints were received from the Hazelmere Water Works regarding sandmining impacts on the raw water resource, and follow up with the Department of Minerals & Energy was made to address these. In the Midmar catchment, cross-sectional surveys were carried out to assess the extent of erosion caused by the inter-basin transfer from the Mooi to uMngeni receiving streams.

Eutrophication Risk: Water quality assessment of Mearns in the Mooi river system showed increased trends in nutrient levels. Analysis showed highly intensive agriculture to be the cause of the eutrophication. A Water User Association had been established for the Mooi River by DWAF in 2006 and this together with the upper uMngeni catchment management forum will provide mechanisms for input into management strategies for the system.

Chemical Pollution Risk: Assessment of water chemistry included iron, manganese, organic carbon, conductivity/salinity and related constituents. No major health risks were noted.

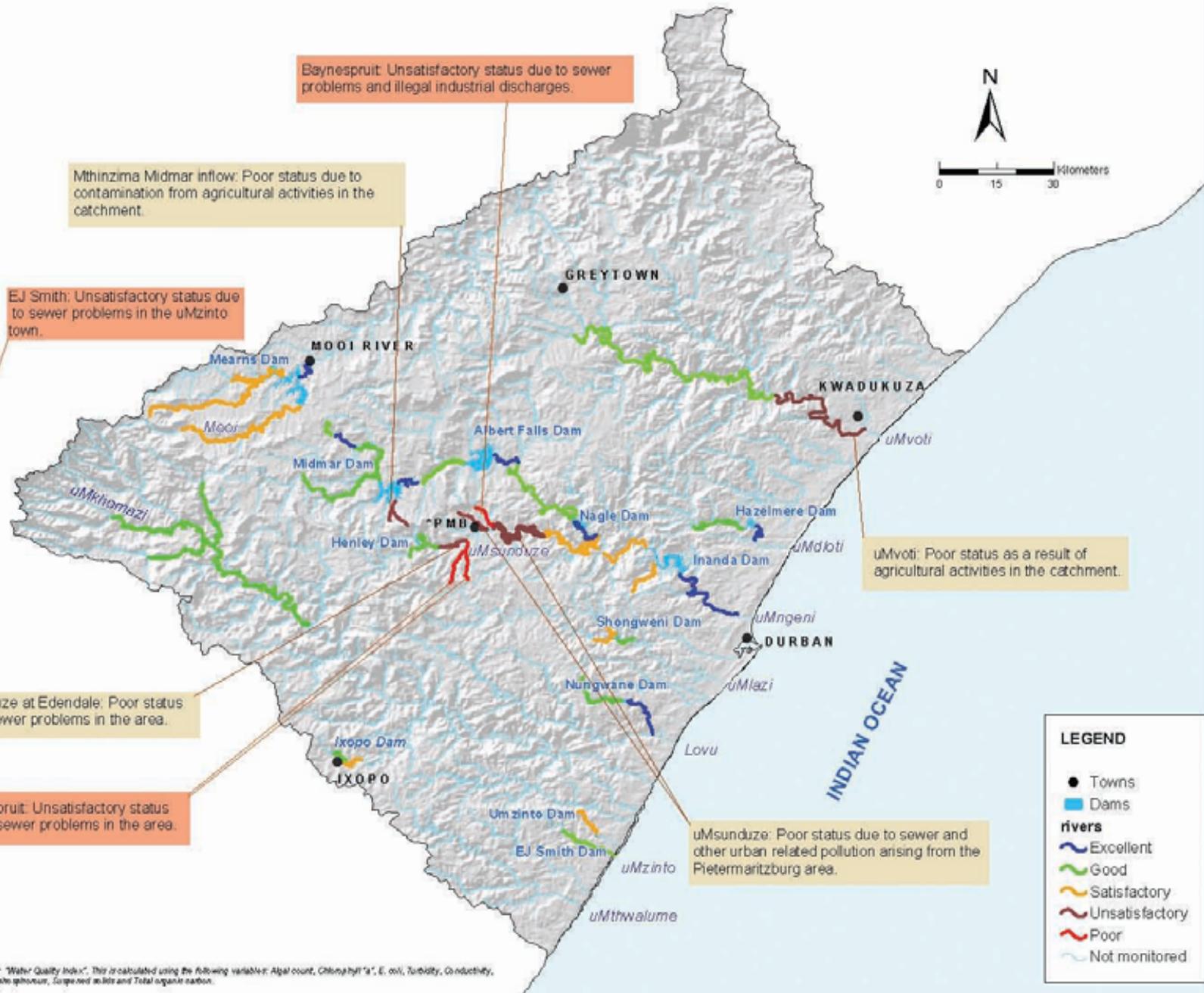
Biodiversity and Land Management: Umgeni Water owns two game reserves at Nagle and Shongweni Dams. The management programmes to minimise the major impacts on biodiversity: Invading alien weed species, which were reduced by spray control as part of the programmes by Msinsi and DWAF Working for Water; Poaching of game mammals, for which efforts to reduce included more frequent patrols by rangers, as well as community awareness programmes; Bush encroachment of grasslands, which was managed by defoliation, using controlled fires; and animals in excess of the ecological carrying capacity of the reserve managed through their removal from the reserve. Red data species in the reserves include blue duiker at Nagle dam, as well as blue duiker, red duiker and black storks at Shongweni dam.

Catchment Management Forums and Resource Quality Objectives: Umgeni Water played an active role in the facilitation of several Catchment Management Forums in its supply area in support of the Mvoti to Mzimkulu Catchment Management Agency. Support and facilitation of the Upper Mngeni Catchment Management Forum continued. The past year has seen multiple development proposals for the Midmar-Mooi catchments and Umgeni Water independently responded to these as an interested and affected party.

Planning for the resource management plan for Inanda dam commenced in 2006. This will provide a framework for consideration of development proposals and balance economic growth with community benefit while ensuring resource sustainability. Umgeni Water, eThekweni and DWAF are collaborating on this. Stakeholder liaison is being enabled through the Inanda catchment management forum, which was successfully launched in March 2006 in partnership with DWAF. The uMsunduzi river catchment management forum continued to meet quarterly and provided a platform for addressing water quality and quantity problems in the uMsunduzi River, which mainly arose from municipal sewers in Pietermaritzburg. Umgeni Water, in partnership with DWAF organised and held a successful catchment management workshop at the WISA Conference in May 2006 in Durban, South Africa.

Status of Impoundments

-  Mearns Dam
-  Midmar Dam
-  Albert Falls Dam
-  Nagle Dam
-  Inanda Dam
-  Henley Dam
-  Hazelmere Dam
-  Shongweni Dam
-  Nungwane Dam
-  Solly Bux Dam
-  EJ Smith Dam
-  uMzinto Dam



LEGEND

-  Towns
-  Dams
- rivers**
-  Excellent
-  Good
-  Satisfactory
-  Unsatisfactory
-  Poor
-  Not monitored

*PMB: Pietermaritzburg

The river impoundment quality is based on the Umgeni Water "Water Quality Index". This is calculated using the following variables: Algal count, Chlorophyll 'a', E. coli, Turbidity, Conductivity, Nitrate, Free ammonia, Total phosphorus, Soluble reactive phosphorus, Suspended solids and Total organic carbon.



Stuckenberg Tunnel

3.4 INFRASTRUCTURE DEVELOPMENT

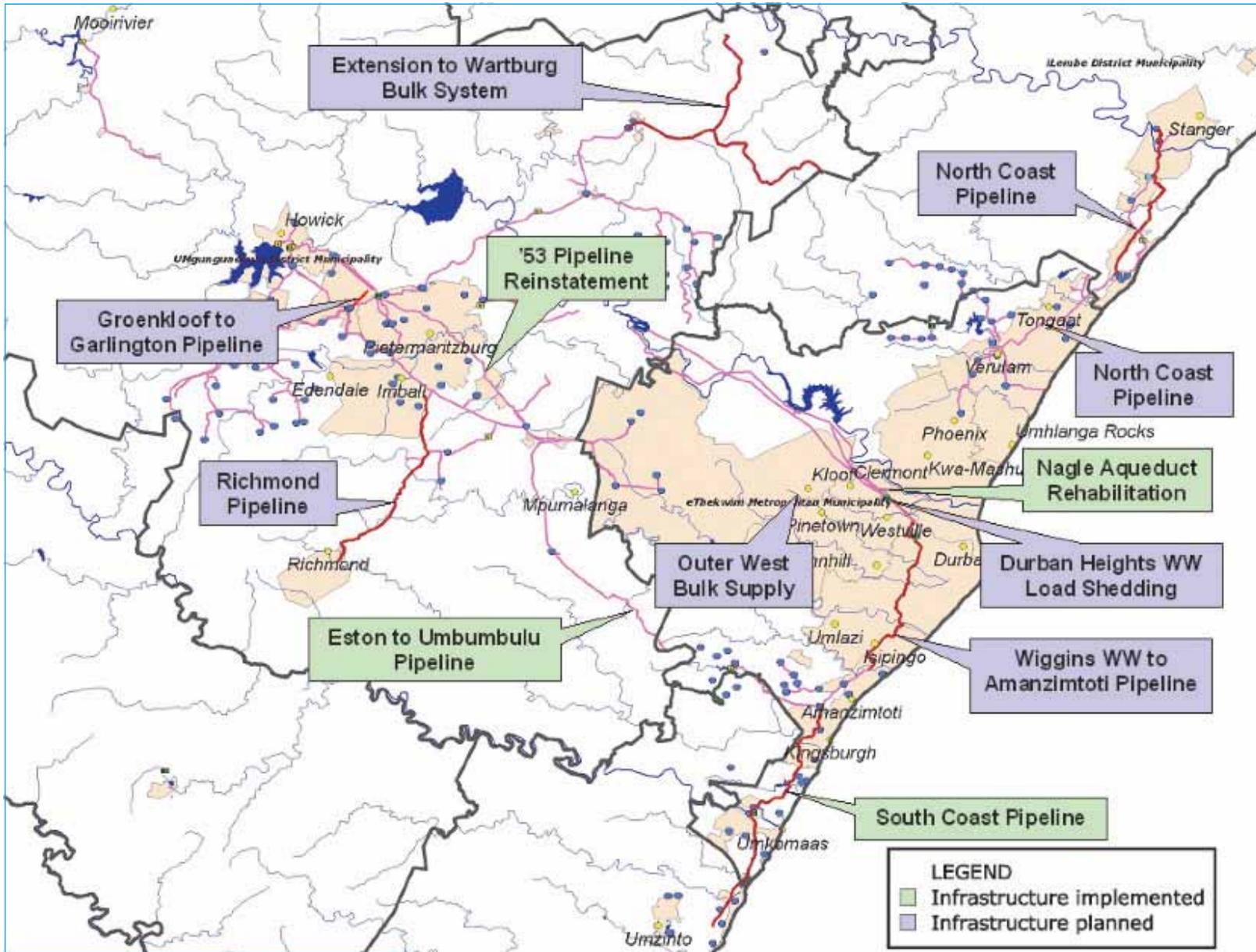
The approved budget for capital infrastructure projects in the year under review was R239 million. Actual expenditure totalled R79 million with the only completed project being the Eston-Umbumbulu Pipeline (R42 million). A R17 million “saving” against the budget was achieved when the Eston-Umbumbulu Pipeline was curtailed by 10 km. The following partially completed projects have accounted for a major portion of the balance of expenditure, namely, South Coast Pipeline, emergency re-commissioning of the 53 Pipeline, Nagle Aqueduct Rehabilitation and Head Office Upgrade.

A large portion of the approved budget was allocated to the South Coast Pipeline. However, the implementation took longer than expected due to the time taken in addressing the environmental impact assessment study, the appointment of consultants assisting with the design process and the delay in the supply of steel pipe.

The demand for services and materials has increased in-line with the growth currently being experienced in South Africa and this is making timeous implementation more challenging as Umgeni Water competes in the market place for the resources required to implement its capital expenditure programme.

3.4.1 Projects Completed during 2005/2006

Eston-Umbumbulu Pipeline: As a result of demand in the Umbumbulu area, Umgeni Water’s existing water treatment works at Umbumbulu reached maximum capacity and had to be augmented from an alternative water source. The Eston-Umbumbulu pipeline was implemented to supply water under gravity from Umgeni Water’s Umlaas Road node to consumers along a 35km route (the last 10 km of this pipeline was implemented by eThekweni Water Services (EWS)). The pipeline has a design capacity of 15 ML/day. This project was commissioned in June 2006. An Environmental Impact Assessment (EIA), with public participation and heritage assessment, was outsourced to independent consultants. Umgeni Water provided 65 jobs in the community.



Infrastructure and development plans

3.4.2 Projects Under Implementation

South Coast Pipeline: This project falls within the ambit of the KZN Bulk Water Services Strategy providing a sustainable potable water supply to the area from Amanzimtoti to Park Rynie. The pipeline has been designed for the average annual daily demand of 65 ML/day. The first phase comprises a 40km pipeline, several service reservoirs and two booster pump stations. Construction is scheduled to commence in the new financial year and is estimated to be completed within 8 months.

Nagle Aqueduct Rehabilitation: Investigations have identified the need to replace a length of the Nagle Aqueduct No 1, one of four aqueducts used to supply approximately 600 ML/day of raw water from Nagle Dam to Durban Heights Water Treatment Works. A budget of R8,8 million was approved and construction has commenced. An environmental screening study was undertaken to assess the possible impact of the refurbishment on the natural and social environment. Public concerns about the proposed development were addressed. Environmental and social impacts were identified and appropriate interventions proposed. Phase 1 of the project is scheduled for completion in September 2006.

The 53 Pipeline is a pre-stressed concrete pipe, 26 km long and built in the 1960's to supply 50 ML/day of raw water to Umlaas Road Water Works. This pipeline was decommissioned together with Umlaas Road WW in 2002, when the new 61 pipeline was commissioned. The 61 pipeline, supplying potable water to eThekweni area is proving inadequate in meeting the peak water demand due to development growth. In order to provide an immediate solution to remedy this constraint, Umgeni Water is re-commissioning the 53 pipeline by converting it to a potable water pipeline. A budget of R20 million was approved and the project is scheduled to be completed in July 2006.

3.4.3 Major Projects in Planning

Umgeni Water initiated several water supply infrastructure studies during the past year, focussing on the augmentation of Umgeni Water's existing bulk infrastructure, and the extension of existing bulk supply networks into unserved and under-served areas in line with the KwaZulu-Natal Bulk Water Services Plan. The 5 year CAPEX programme starting in 2007 totals R1 billion. The major projects are highlighted in blue in the previous map:

Outer West Bulk Water Supply: To determine the most feasible option for long term natural growth in water demand in eThekweni Municipality's Outer West area, taking into account current infrastructure constraints and operating costs. The most economic approach to meet the growth in demand would be achieved by upgrading the inland gravity supply system from Midmar Water Works.

Durban Heights Water Works Load Shedding: The growth in water demand in certain areas of eThekweni has resulted in the Durban Heights Water Works (WW) having to operate and near full supply capacity. eThekweni Municipality intend to construct the Western Aqueduct pipeline and shed load from Durban Heights WW onto this new pipeline and consequently into Midmar WW.

Richmond Pipeline: This study assesses the potential development of a bulk pipeline from Pietermaritzburg to Richmond to supply the town of Richmond and surrounding areas with potable water. Off-takes from this pipeline to Thornville, Hopewell and Ambleton will augment existing supplies to these areas.

Groenkloof to Garlington Pipeline: Planned high-income housing developments to the north of Hilton have prompted the uMgeni Municipality to approach Umgeni Water for the installation of a bulk supply pipeline from Groenekloof Reservoir to the Garlington area. The planning and initial environmental investigations have been completed and detailed design has commenced.

Extension of the Wartburg Bulk System: A pre-feasibility investigation was carried out to assess the various options to upgrade and extend the existing Wartburg Bulk System to the Greater Efaye and Ozwatini rural areas. An optimal route was determined and the study will now proceed to a detailed feasibility level. The environmental assessment process was initiated to identify potential impacts that the proposed project could have on the environment, and a pre-screening report prepared. The environmental assessment process will be followed as the project progresses.

Wiggins Water Works to Amanzimtoti Pipeline: In order for the proposed South Coast Bulk Pipeline (SCP) to be utilised to its design capacity and to therefore also accommodate the later Phase 2 component from Park Rynie to Hibberdene, a feasibility study was initiated to find the best way to upgrade the capacity of the existing South Coast Augmentation (SCA) pipeline from Wiggins Water Works to the start of the SCP at Amanzimtoti.

North Coast Bulk Pipeline: Significant increases in water demands are being experienced along the North Coast from Verulam to KwaDukuza due to the large number of developments that are taking place in this area. The planning investigations into increasing the capacity of Umgeni Water's North Coast Bulk Supply System, which currently supplies this area, have been completed and the design of the upgrade to the Hazelmere Water Works and of new pipelines from the water works to KwaDukuza are currently underway.

3.4.4 Asset Management

Sound asset management is a structured approach to asset maintenance, both on a day-to-day basis (operations and maintenance) and in the medium to long-term (strategic and forward planning).

Asset management is directly associated with the current or desired levels of service for Umgeni Water's customers, the associated costs in providing these services and the practices and systems that assist the organisation in achieving this in the most efficient and cost effective ways.

Umgeni Water's mission, in relation to Asset Management is to ensure optimum levels of availability, reliability and operability of equipment through effective maintenance practices while constantly improving the safety of the working environment, to meet the client demands. Key objectives and strategies for the efficient use of assets include:

- ensuring that all assets operate at the required performance and availability levels
- continuously increasing the reliability and performance of assets
- improving human resources to maximise added value to Umgeni Water's operations
- creating and maintaining safe work procedures and a safe environment to preserve the overall environment.

In order to prevent asset failure, the department has formalised a risk based assessment management and maintenance plan;

- Prevention of asset failures
- Formalised risk based asset assessments
- Maintenance plans.

The total expenditure on asset management listed below amounted to 4.9% of the revenue for 2005/2006. The table below reflects the outcome of the preventative maintenance strategy implemented by the department. The high spend on planned and corrective maintenance emanates in minimizing spend on ad-hoc interventions, while modifications and minor projects play a significant role in ensuring sustained and extended life of the assets.

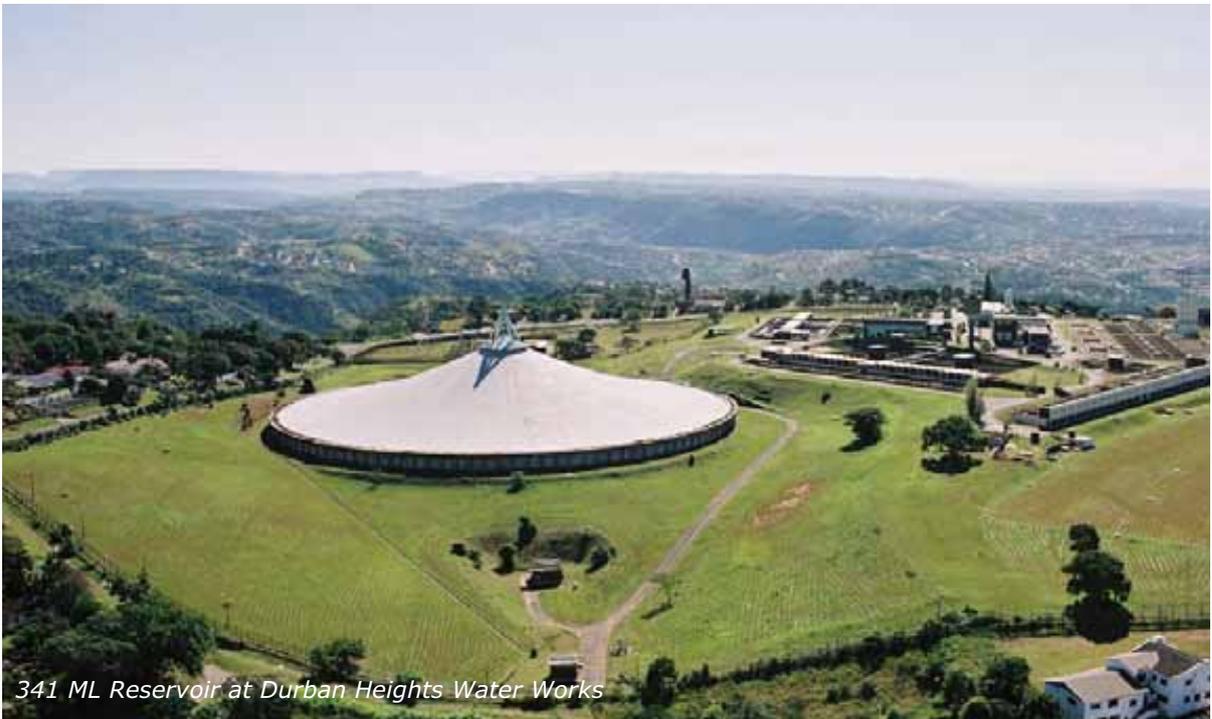
Breakdown of Expenditure on Asset Management

Work Type	Actual Spend R' 000	Percentage to Total
Planned & Corrective Maintenance	42 341	81.6 %
Callouts - Normal	889	1.7 %
Breakdowns	3 609	6.9 %
Callouts - Breakdown	942	1.8 %
Projects (minor)	1 882	3.6 %
Modifications	1 673	3.2 %
Safety	627	1.2 %
	51 963	100%

The Asset Management Department has also implemented appropriate levels of maintenance technology to support the maintenance plan. This includes facilities (workshops, stores, handling equipment, cleaning equipment, machining facilities), tools and condition monitoring facilities. A computerised maintenance management system has been implemented to assist the general team performance and efficiency in terms of quality and timeous response. To ensure that the human resources are fully equipped, the individual development plans comprised formal training (as engineer or artisan), management and supervision training, specific technology training and training in maintenance technology.



Pump house at Midmar Water Works

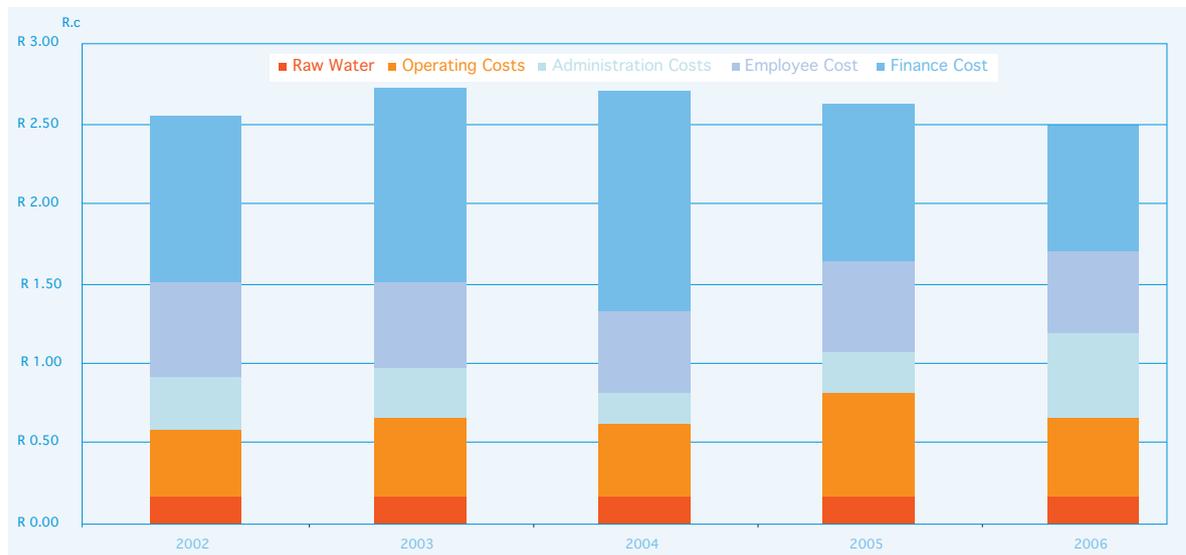


341 ML Reservoir at Durban Heights Water Works

3.5 OPERATIONAL PERFORMANCE

3.5.1 Potable Bulk Water Production Costs

The cost per kilolitre over the last 5 years continued to decrease. The cost of producing water has been impacted on by volume growth and the restructure process which resulted in improved operational efficiencies and lower financial costs. The increase in operating costs in 2005 was attributable to asset impairments. Whereas the significant increase in administration costs in the current year is attributable to the amortisation of the financial asset derived from the transfer of the reticulation schemes to the Water Service Authorities.

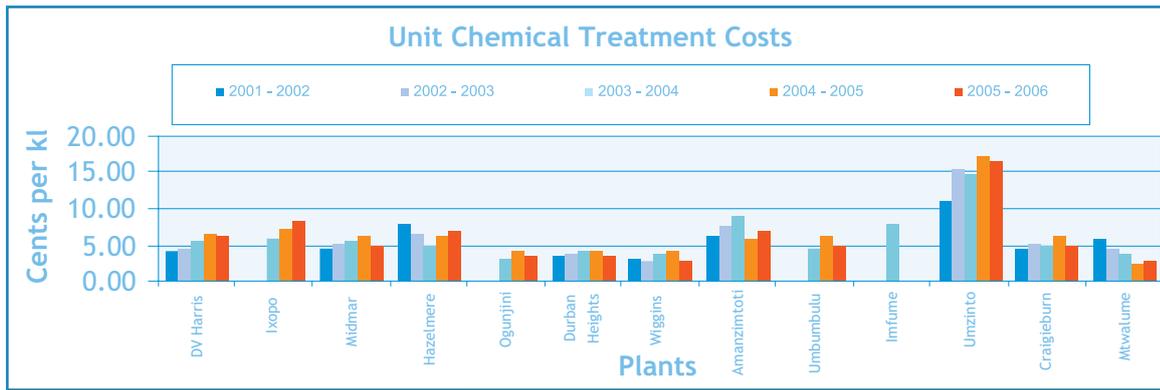


Cost of Potable Bulk Water per Kilolitre

3.5.2 Chemical Usage

The amount of chemicals used in the treatment of raw water is a variable that contributes to operational costs. Umgeni Water is committed to monitoring and reporting on chemical usage throughout its operational area.

Chemical usage generally depends on quality of raw water received from the dams. Abstraction points are carefully selected to obtain water of an acceptable quality. Catchment management activities assist in protecting rivers and reducing pollution of raw water sources.



Water works unit chemical costs

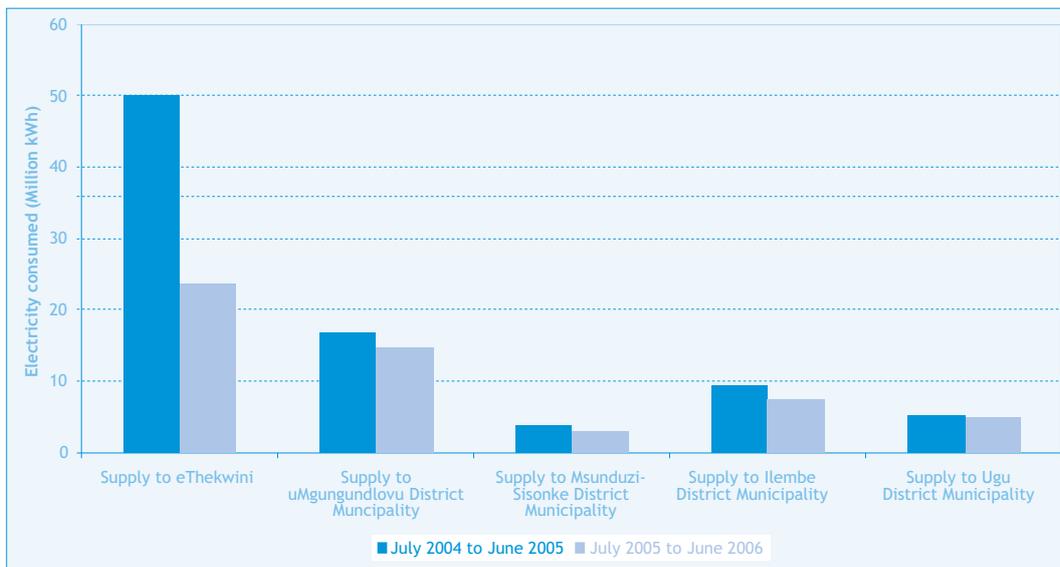
Continuous improvement initiatives and the benefits derived from the ISO 9001:2000 Quality Management System have played a role in process optimisation and increased overall efficiency. This is evident in most Waterworks where the trends reflect a decrease in chemical consumption. Improved raw water quality has also contributed to overall efficiencies in the major waterworks viz. Durban Heights, Wiggins and Midmar.

Hazelmere Water Works had experienced poor water quality after the summer rains with higher than average turbidities promoted by the presence of kaolin. Similar conditions were experienced at both Ixopo and DV Harris Water Works, where poor raw water quality had lead to an increase coagulant usage.

The drought in the Ugu District Municipality contributed to a rise in the chemical consumption at Mtwalume and Umzinto Water Works, due to a deterioration of the raw water quality upstream in the EJ Smith and Umzinto Dams. The mitigation implemented included dosing of powdered activated carbon and potassium permanganate to remove manganese and unpleasant taste and odours (2-Methylisoborneol).

3.5.3 Energy Consumption

The organisation’s core business uses electricity as its primary energy source. The electricity consumption for the last two reporting periods (2004/2005 and 2005/2006) is depicted below. It was noted that there has been a decrease in the energy consumed. The main reason for this is that there was no need for additional pumping of water from Inanda Dam to the Durban Heights Water Works due to an adequate level of supply at Nagle Dam which feeds the Durban Heights Water Works.



Total annual electricity consumption

Electricity generated in South Africa is mostly from fossil fuel, coal, which is a non-renewable resource. The use of fossil fuel for the production of electricity impacts negatively on the environment contributing to global warming. The carbon dioxide (CO₂) emissions associated with the energy consumed by the organisation in the last cycle (2004/2005) was approximately 36 900 tonnes which was reduced to approximately 23 500 tonnes in the current reporting period for 2005/2006. This was the organisations contribution to global warming through energy consumption and the release of CO₂ to the atmosphere. To further reduce its energy consumption and the associated impacts, the organisation has embarked on a joint project with Eskom. This project is aligned with Eskom's Demand Side Management (DSM) initiative which aims to extend the life expectancy of the current generating capacity. This project reviews the current status of electrical energy usage at Umgeni Water and assesses the opportunities for electricity efficiency and load management projects, with particular reference to intelligent pump scheduling. The project will also quantify (to within 10%) the costs and benefits associated with each opportunity. The deliverables of the project are:

- A comprehensive investigation and identification of electricity efficiency and load management opportunities;
- A recommended action plan which will outline the steps Umgeni Water should take to become more electricity efficient and which areas should receive priority;
- An estimate of the costs and benefits that can be expected if the recommended Eskom DSM projects are implemented.

3.5.4 Safety Health Environment and Quality

Umgeni Water achieves sound safety, health and environmental performance by controlling the impacts of its activities, products and services on the health and safety of employees, contract workers, the community and the environment. Safety, Health, Environmental and Quality (SHEQ) management is included in the job profiles of key staff across the divisions through the inclusion of safety, health and environmental key performance indicators in the corporate and divisional Balanced Scorecards.

An integrated approach to SHEQ risk management, using the International Organisation for Standardisation (ISO) management principles is used at the operational worksites and aligned with the triple bottom line performance reporting criteria. Most of Umgeni Water's water works and dams have achieved Quality Management System certifications (ISO 9001: 2000) as shown below.

<i>Status of ISO Management Systems Adopted at Umgeni Water</i>	
Operational Sites	ISO 9001 : 2000 certification
Midmar WW	Complete
DV Harris WW	Complete
Ixopo WW	In Progress
Nagle Dam	Complete
Durban Heights WW	Complete
Wiggins WW	Complete
Inanda Dam	Complete
Hazelmere WW	Complete
Amanzimtoti WW	Complete
Cragieburn WW	Complete
Umzinto WW	Complete
Mtwalume WW	Complete
Mfume WW	In Progress
Umbumbulu WW	In Progress
Pineside Regional Complex	Complete
Darvill WWW	Complete
Midmar Dam	Complete
Mearns Dam	Complete
Albert Falls Dam	Complete



Chemical house at Midmar Water Works

Umgeni Water's operational sites utilised the National Occupational Safety Association (NOSA) SHE Management system (integrated - Safety, Health and Environmental System - CMB 253), until June 2004, when NOSA was liquidated. Since then the operational sites have been using the corporate Umgeni Water standards and various requirements in terms of Occupational Health and Safety Act 85 of 1993 (OHASA), National Environmental Management Act (NEMA), together with the relevant SABS codes of practices.

All the dams and reservoirs above a certain capacity and/or having a real danger to human life and/or property in the event of a failure, are registered with DWAF's Dam Safety Office. These structures are registered as 'Dams' with a safety risk as defined by the National Water Act, 1998 and Regulations R1560 and are inspected periodically at five year intervals.

Umgeni Water ensures that dam safety inspections are carried out in order to protect its capital investments and to ensure that the lives of inhabitants and property in areas downstream of the dams and reservoirs, at risk due to flooding arising from a failure, are protected. These inspections are carried out by an Approved Professional Person, or Team, appointed by Umgeni Water on behalf of DWAF's Dam Safety Office. Umgeni Water's site operations and asset management teams carry out regular maintenance in accordance with the operating and maintenance manuals issued by the Approved Professional Person/ Team.

The Umgeni Water Laboratory has three ISO/IEC 17025 accredited laboratories (Chemistry, Microbiology & Hydrobiology). Accreditation is a means of demonstrating a laboratories technical competence hence allowing a laboratory to maintain its competitiveness both nationally and internationally. In addition, the Laboratory Services Business Unit is supported by an ISO 9001:2000 certified sampling facility providing a professional sampling service that adds value to the integrity of results generated.





Umgeni Water Staff Information Session

3.6 MANAGING UMGENI WATER'S HUMAN RESOURCES

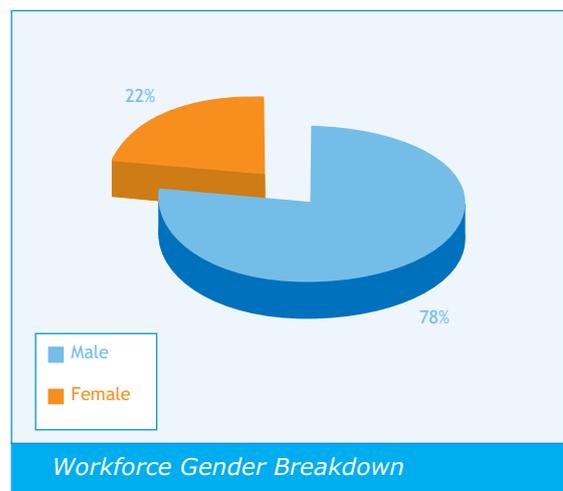
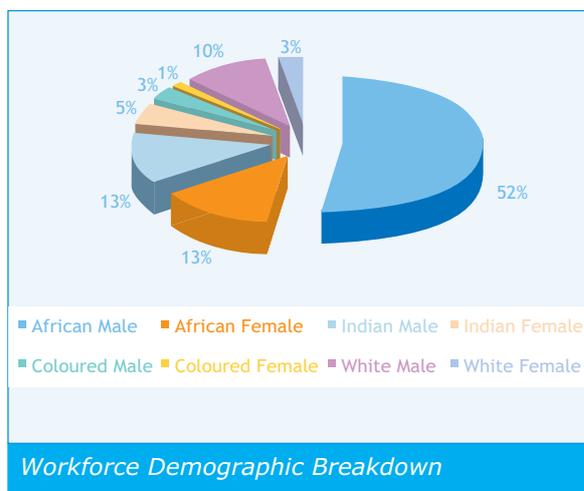
Umgeni Water's strategy to be the employer of choice is a reflection of its endeavours to find its competitive edge through its employees. During the period under review, Umgeni Water introduced a number of quality improvements, from fundamental resourcing decisions to development and retention strategies.

3.6.1 Staff Complement

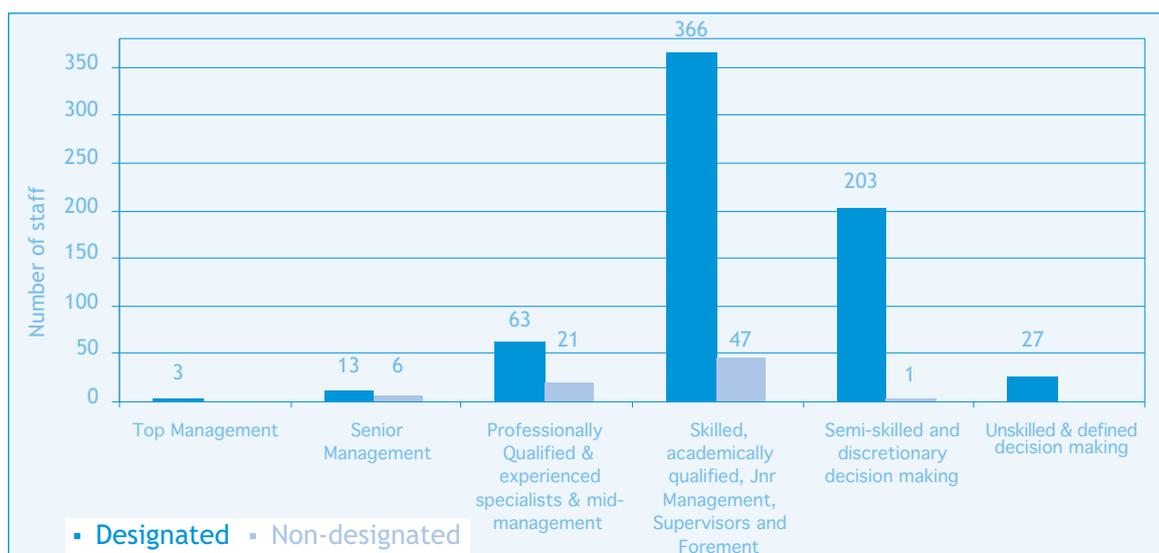
During the period under review, the number of employees of Umgeni Water averaged 789, which is 7 employees less than the previous financial year. About 8% of the workforce comprises employees on fixed-term contracts. The turnover of 63 permanent employees in 2005/2006 is an improvement on the turnover of 90 employees in the 2004/2005 year.

3.6.2 Workplace Transformation and Employment Equity

Umgeni Water's corporate demographics indicate progress in attaining its objective to ensure a diverse workforce. Based on the 5 year Employment Equity targets (ending December 2005) set by the organisation, the workforce should comprise 89% designated groups, 25% women and have 2% disabled employees.



The percentage of women in the organisation improved by 1% over the previous financial year. A slight improvement on disabled employees of 0.3% is also noted. Continued efforts to improve on these figures are ongoing.



The workforce according to Occupational Categories and Designated versus Non-designated Groups

3.6.3 Performance Management

The organisation has instituted a campaign to further enhance a culture of performance among its employees. To this end, three levels of performance reviews have been put in place: organisational, divisional and individual. This approach links performance achievement to a reward system linked to each employee's biennial average performance rating, divisional performance rating and corporate financial performance. This bonus scheme was used for the first time in 2006.

3.6.4 Cross-functional Task Teams

The concept of using Task Teams for specific projects is moving Umgeni Water towards the vision of becoming the number one water utility in the developing world. The contributions of various Task Teams resulted in refocusing Umgeni Water's business strategy. These task teams include the:

- Benchmarking Task Team - involved in benchmarking various areas of the operation against other organisations operating in the same business environment. The task team made final recommendations to EXCO in every aspect of business benchmarked for consideration.
- Strategy, Business Plan and Business Task Team - instrumental in the compilation of the Umgeni Water Business Strategy document.
- Best Company to Work for Task Team - responsible for coordinating the process set up by Deloitte and Touche to survey the views of employer and employees regarding the working climate at Umgeni Water. Umgeni Water ultimately won the Government and Utilities Award for 2005 and was placed 25 out of 108 organisations as the best company to work for.
- Awards Task Team - set up to look at various means of giving recognition to those employees who made special achievements in their areas of operation. This was designed to motivate employees to be achievers in their areas of responsibilities in order to make Umgeni Water the best company to work for.

3.6.5 Labour / Management Relations

A co-operative environment has been created and sustained by the desire of both management and organised labour for transparency. One of the key outcomes of this relationship has been that agreements are reached more readily.

In compliance with the water board sector agreement, Umgeni Water recently accepted the appointment of two full-time Shop Stewards. This further strengthens internal communication between management and organised labour and contributes to the strategic thrust of the organisation. The milestones characterising Labour/Management relations in the past year include:

- Acknowledgement of the Umgeni Water employee contribution to the remarkable turnaround, from being an unprofitable organisation to a financially sound one. Employees were rewarded by a performance bonus. This has galvanized employees and instilled a strong sense of purpose.
- The early conclusion of the salary/wage agreement in January 2006 proved that the relationship is being further enhanced. This resulted from joint consensus seeking in resolving problems of common interest.

Umgeni Water has a well documented disciplinary and grievance handling procedure to ensure efficient and effective resolution of disciplinary breaches as well as collective and individual grievances. Invariably these procedures have to be approved by both Organised Labour and Management before implementation.

Umgeni Water has included Labour representatives in the decision-making process at operational and strategic levels.

3.6.6 Skills Development and Training

Umgeni Water received full accreditation from the Energy SETA (**ESETA**) for the following courses/qualifications, as gazetted under the ESETA Scope of Coverage:

1. Water & Waste Water Treatment up to **NQF** Level 2
2. Water Treatment up to **NQF** Level 2

The accreditation now enables Umgeni Water to conduct learnerships for its employees and external organisations in water and wastewater-related operations.

During 2005/2006, a total of R7 617 000 (4.1 % of the payroll) was spent on Training and Skills Development and includes all job related technical training and a Bursary Scheme that was re-introduced in 2006 as well as all the programmes mentioned below:

Assisted Education Programme (AEP)

The AEP continues to provide employees with financial assistance to improve their knowledge and skills through study at external institutions. Currently, ninety three employees are registered in this programme.

Adult Basic Education Programme (ABET)

ABET continues to provide literacy and numeracy skills. The programme is co-ordinated through the Energy SETA and is outsourced to a registered institution. Fifty Umgeni Water employees are registered in this programme.

In-Service-Training and Graduate Programme

A total of seventeen trainees benefited from Umgeni Water's in-service and graduate training programme. Two trainees were bursary holders, who have since graduated.



Team who participated in the Wits University Business School Programme

Leadership Development Programme

Thirty Senior, Middle and Junior Managers were registered for a leadership development programme, titled “Certificate Programme in Leadership Development, presented and designed by Wits University Business School. The objective of the programme was to develop the leadership ability of managers and potential managers through a theory-based and experiential programme of learning. The expected outcome is that participants are better equipped to manage business units. The programme was complete in May 2006.

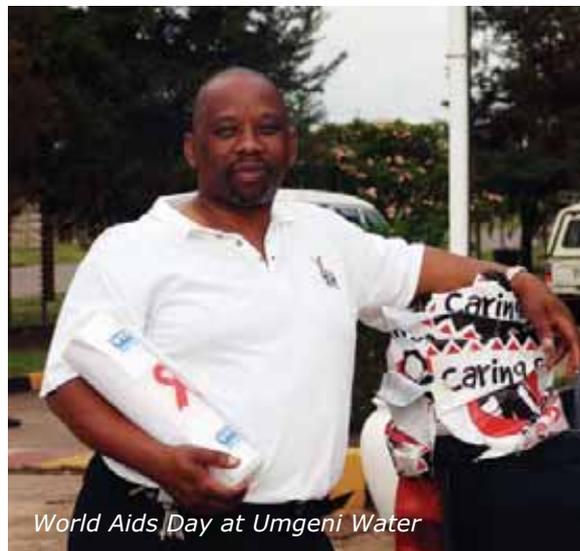
3.6.7 Corporate Wellness Management

In responding to the AIDS pandemic, Umgeni Water has developed the Umgeni Water Corporate Wellness Programme Strategy, which includes an effective HIV/AIDS Programme.

A voluntary counselling and testing initiative forms part of the strategy to curb the spread of infection. Employees are encouraged to voluntarily come forward for HIV testing so that they can register in a programme that is offered by the respective medical fund.



Wellness Day at Umgeni Water



World Aids Day at Umgeni Water



Community of eMangwaneni with Umgeni Water Staff

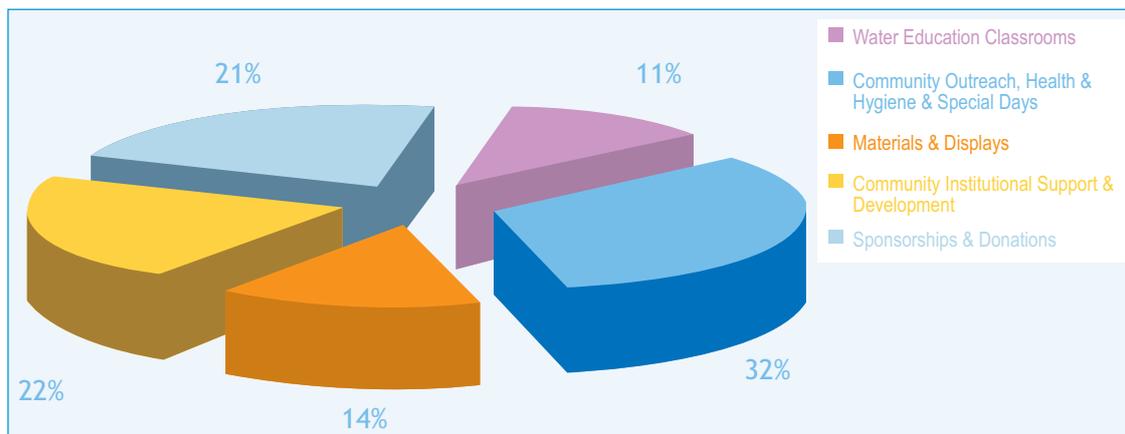
3.7 CORPORATE SOCIAL INVESTMENT

Umgeni Water has a proud history as a corporate citizen that cares for its environment and communities. As far back as 1991, the organisation received recognition for one of its earlier initiatives, the Rural Areas Water and Sanitation Plan, which made it possible for water services to be supplied to marginalised rural communities. The project, a trailblazer in its own right, gave tangible meaning to Umgeni Water’s corporate social investment strategy.

Umgeni Water has revised and intensified its corporate social investment with a multi-pronged strategy that is intended to contribute to: job creation and, consequently poverty alleviation; skills and literacy enhancement; women empowerment; further education with financial assistance; in-service training for tertiary education students; water and sanitation education through structured programmes and institutional support aligned to community outreach.

The key objective of the Umgeni Water Corporate Social Investment (CSI) policy is to ensure that the work undertaken and financial sponsorships provided have the effect of improving the quality of life of communities within Umgeni Water’s operational area and beyond.

In the financial year 2005/2006, a total of R2,5 million was spent on CSI initiatives.



Distribution of the R2,5 million Corporate Sponsorship for 2005/2006



3.7.1 eMangwaneni Women's Day Celebration

Opportunities are emerging for women to participate at all levels in the sustainable management of water resources. Umgeni Water is actively responding to this change and has recognised the need to move towards deepening the competency and skills of women to enable them to become full participants in the water industry and contribute towards the mainstream economy. Umgeni Water has also recognised that it has to play a critical role in enabling women-especially breadwinners - to have access to basic services.

In order to fulfil this role, Umgeni Water launched the Women Initiative Task Team in July 2005, to drive the Women's Initiative. The strategic intent of the initiative is to improve the lot of women, both within and outside the organisation. The internal component of the initiative is intended to ensure that female employees have opportunities to progress within Umgeni Water and reach senior managerial positions. This will have the effect of consolidating Umgeni Water's position as an employer of first choice.

The external component of the Initiative was launched in eMangwaneni on Women's Day in August 2005, after the Umgeni Water Women Initiative Task Team created a programme to improve the lives of the women of eMangwaneni, a rural settlement outside Bulwer. This programme entails skills transfer for small business development, training and capacity building, as well as the enhancement of knowledge about water, health and hygiene.

The women of eMangwaneni prioritised the need to rehabilitate the existing water supply infrastructure in the area. Umgeni Water's Operations Division staff assisted the community by supplying expertise, training and materials to repair and upgrade the existing water supply network.

The Women's Day celebration was a proud occasion for Umgeni Water staff, who contributed R30 each for the purchase of groceries and the staging of the event. Almost 60% of staff travelled to eMangwaneni for the celebration, which received wide media coverage. Staff also carried 25-litre containers of water on their heads and distributed the water to households as a symbolic gesture of understanding and empathy for women who have to carry water over long distances.

3.7.2 Community Vegetable Gardens

Umgeni Water initiated meetings with traditional leaders (*aMakhosi*) in the Inanda Dam area to try to ascertain how it can assist with promoting garden projects that would benefit the local community. Five requests for assistance were received from established community gardening and farming associations. Investigations revealed that water could be drawn from a raw water pipeline to supply three established vegetable gardens. Umgeni Water is to supply the pipes and fittings as off-takes and assist with installation.



Bring a Girl Child to Work Day

3.7.3 Bring a Girl Child to Work Day

As part of a national initiative to expose learners to the work environment, staff at Umgeni Water's Wiggins Water works held an open day for various schools in the area to provide an opportunity for learners to interact with process engineers and scientists. Clearly, the interaction created an interest in the professional engineering and science fields of the potable water industry.

3.7.4 Environmental and Water Education

Umgeni Water continues to form partnerships with stakeholders to promote health, hygiene and environmental awareness through education, community participation and empowerment programmes



School tour of a water treatment plant

Umgeni Water conducts "water classrooms" and water treatment tours for schoolchildren at its Durban Heights and Midmar Water Works. Wastewater Treatment tours are conducted at its Darvill Wastewater Works in Pietermaritzburg.

In the 2005/2006 financial year, 5 587 learners representing 60 institutions visited the water classrooms in Durban and Pietermaritzburg. In the same period, 200 learners from the Hambanathi Primary School in Tongaat were taken on a tour of the Hazelmere Plant in Verulam during which they were exposed to water education.



School children who participated in various environmental awareness programmes

In the period under review, several schools in the eThekweni Metropolitan and the Ilembe, Umgungundlovu and Ugu district municipalities were visited to promote greening projects which would be aligned to the ECO Schools Project. The ECO Schools Project promotes the importance of environment-friendly schools.

The target audience of about 5 140 included educators and learners, who were given presentations and attended workshops. Two hundred and twenty educators were provided with skills to make the projects sustainable.

Special environmental days intended to create awareness about alien plants and wetlands rehabilitation were also held in the period 2005/2006. Umgeni Water and DWAF's Working for Water also assisted with Arbor Day and Weed Buster Week projects in the Ugu District.



Children from KwaDumisa area in KwaBangibizo working during Weed Buster Week

In the KwaBangibizo area, South of Durban, 30 children received basic training from Umgeni Water and Working for Water in alien plant removal and wetlands rehabilitation. This group will now share their skills with other members of their communities.



A BEE construction company sub-contracted by Umgeni Water

3.8 BROAD BASED BLACK ECONOMIC EMPOWERMENT

Umgeni Water has aligned itself with National Government procurement principles of good governance and the 90/10 or 80/20 preference system. Umgeni Water has implemented Broad Based Black Economic Empowerment and measures contributions made by different categories of suppliers towards its objective of the empowerment of previously disadvantaged groups. All tenders are evaluated and scored in a transparent manner by cross functional teams consisting of members of appropriate disciplines.

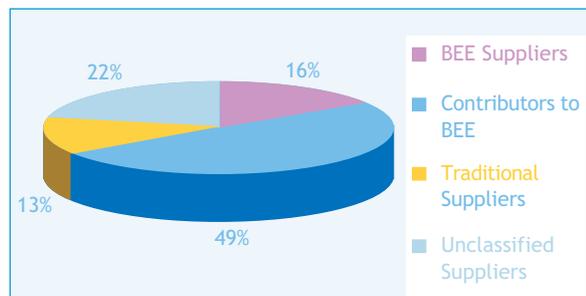
Supply Chain Management (SCM) comprising of the core elements of Demand Management, Acquisition Management, Logistics Management, Disposal Management and Supply Chain Performance is presently being introduced.

The introduction of the elements of Demand and Performance Management are particularly important. Demand Management allows the department to become proactively involved at the planning phase of a project. This allows SCM practitioners to add their expertise to the compiling of specifications and more importantly allows more time to locate, or if required develop ISO accredited Black Economic Empowerment (BEE) suppliers. Performance Management dictates that mechanisms are put in place to accurately measure and report on the performance against preset objectives of the SCM department and the organisations suppliers. These measurements include performance against budget, risk management and the SCM department’s ratings by its internal and external customers.

Challenges for the department are a reduction in the “total costs of ownership” and an increase in the spend with BEE suppliers. The introduction of, particularly Demand Management will ensure that both these challenges are achieved.

Classification and Numbers of Suppliers on the Umgeni Water Procurement Database

DESCRIPTION	TOTALS
BEE suppliers	296
Black-Owned Company	215
Black-Women Company	52
Black Empowered Company	16
Black Influenced Company	13
Contributors to BEE	358
Limited Contributor to BEE	256
Satisfactory Contributor to BEE	82
Good Contributor to BEE	20
Traditional suppliers	705
Unclassified	223
Total number of suppliers on database	1582



Breakdown of Procurement Expenditure for 2005/2006 by Supplier

Tshebedisano mmoho ke tswelopele



Umgeni Water's technologically advanced Chemistry Laboratory

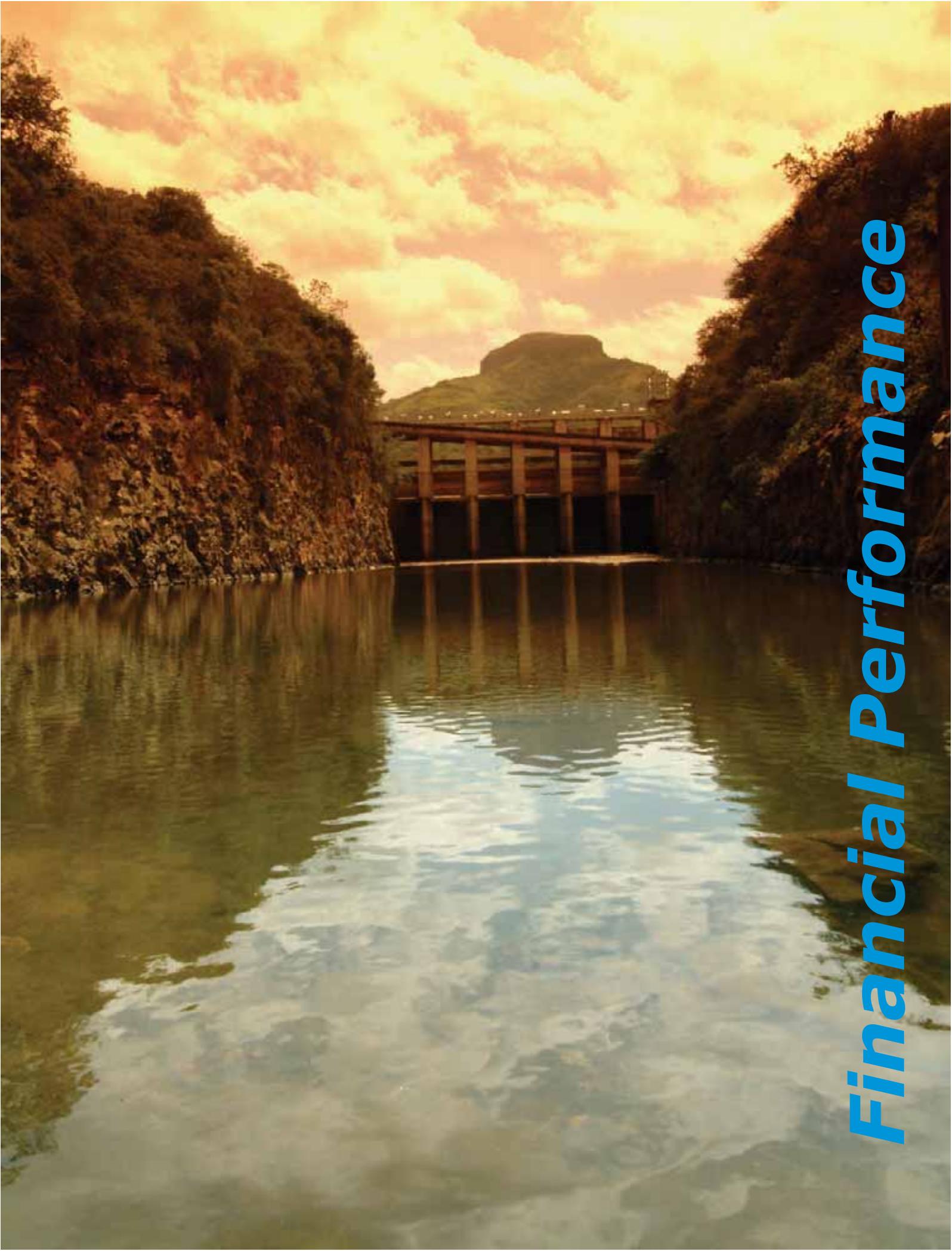
3.9 RESEARCH AND DEVELOPMENT

The Innovation, Research and Development Task Team is pursuing a number of projects with either potential for commercial revenue, increasing operating efficiencies, supporting social development or preparing the organisation for future scientific and technical challenges as listed below:

- School sanitation
- Package sewage treatment plants
- Energy use optimisation at Umgeni Water
- Sustainable consumption and production
- Xenobiotic substances
- Analytical methods for quantification of polymeric coagulants
- Disinfection systems for rural application
- Short-term solutions for rural water supply
- Alternative water sources

The Zinkwazi desalination initiative was an outcome of innovation, research and development at Umgeni Water, to provide drinking water to this holiday village on the KwaZulu-Natal North Coast. The desalination option serves as a means to provide good quality drinking water to Zinkwazi that experiences water shortages due to the current inadequate borehole supply. Umgeni Water submitted a proposal to the Ilembe District Municipality to implement the desalination project on behalf of the municipality. The cost of the project will be in the region of R15 million, which will include the beach well abstraction, desalination plant and brine disposal system. The public participation and environmental impact assessment have been completed and a scoping report will now be submitted to the Department of Agriculture & Environmental Affairs for a Record of Decision. Umgeni Water views desalination as an important water supply technology in the future. Although it is unlikely that desalination will be as prevalent in KwaZulu-Natal as in drier areas, such as the Western Cape and Middle East, there are several benefits to be obtained from understanding and using this technology.

To supplement the resources and knowledge base of the IRD Task Team, a Memorandum of Understanding (MOU) has been developed and is being implemented in conjunction with the University of KwaZulu-Natal. Similar MOU's will be signed with other tertiary institutions and research organisations.



Financial Performance

REPORT OF THE INDEPENDENT AUDITORS

To the Minister of Water and Forestry Affairs

We have audited the annual financial statements and group annual financial statements of Umgeni Water as of 30 June 2006 set out on pages 61 to 92. These financial statements are the responsibility of the directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards of Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance that the annual financial statements are free of material misstatement. The audit was also planned and performed to obtain reasonable assurance that our duties in terms of Sections 27 and 28 of the Public Audit Act No. 25 of 2004, have been complied with. 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 financial statements present fairly, in all material respects, the financial position of Umgeni Water and the group at 30 June 2006 and the results of their operations and cash flows for the year then ended, in accordance with International Financial Reporting Standards and in the manner required by the Public Finance Management Act No. 1 of 1999, as amended, and the Public Audit Act No. 25 of 2004.

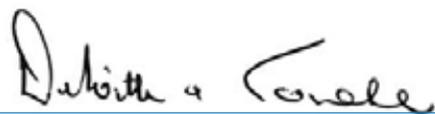
The transactions of Umgeni Water, which were examined during the course of our audit, were in all material respects in accordance with the mandatory functions of Umgeni Water as determined by law or otherwise.

The performance review furnished on page 66 in terms of sub-section 55(2)(a) of the Public Finance Management Act No. 1 of 1999, as amended, fairly presents in all material respects Umgeni Water's performance for the year ended 30 June 2006 against pre-determined objectives.

The information set out on pages 93 to 94 do not form part of the audited annual financial statements and as such we do not express an opinion on them.



Ngubane & Co.
Per H Mpungose
Partner
Durban



Deloitte & Touche
Per D McArthur
Partner
Pietermaritzburg

Chartered Accountants (SA)
Registered Accountants and Auditors

Pietermaritzburg - 21 September 2006

DIRECTORS' REPORT

Nature of Business

Umgeni Water defines its activities in line with the Water Services Act No. 108 of 1997, namely primary (section 29) and other (section 30) activities. Primary activities, being the provision of bulk potable water and bulk waste water, are split accordingly in the segmental report.

Further details on the nature of Umgeni Water's business are reflected on page 4 of the annual report.

Acts and Legislation

The annual financial statements are prepared in accordance with the following relevant statutes:

- Water Services Act No. 108 of 1997; and
- Public Finance Management Act No. 1 of 1999, as amended ("PFMA").

These acts require preparation of the financial information to be in compliance with the Companies Act No. 61 of 1973 and International Financial Reporting Standards ("IFRS"). In line with these requirements, we are pleased to present this year's annual financial statements.

In terms of the PFMA, the Board of Umgeni Water is the accounting authority.

Corporate Governance

The board supports the principles of the Code of Corporate Practices and Conduct as set out in the King II Report and substantially complies therewith.

Share Capital and Directors' Interests

The entity has no share capital and therefore no director has any equity interest in the organisation.

Financial Performance

Details of the financial performance of Umgeni Water, the group and the business segments are contained in the annual financial statements set out on pages 61 to 92.

Users are also referred to the Operational and Financial reviews for further details on the year's financial results.

Accounting Policies

Accounting policies were changed due to first time adoption of IFRS. The most significant change has been to property, plant and equipment - where assets have been componentised and as a result depreciation has been increased. The impact of this adoption is reflected in Note 3.2 of the annual financial statements.

Tariff Policy

Umgeni Water's tariff policy is to set the lowest possible constant tariff in real terms. The underlying principles of this policy are:

- the promotion of the efficient and sustainable use of water;
- the equitable access to water supply services, whereby the basic water service should be affordable; and
- the solvency and sound financial management of Umgeni Water.

Umgeni Water's tariff model uses the cash flow methodology and is based on a constant tariff in real terms. This implies that the tariff increase be linked to CPIx annually. The trade-off is a changing debt level. Debt will first increase as net cash flows are negative, and then decrease as net cash flows become positive.

Capital Expenditure and Commitments

Capital expenditure for the year amounted to R79.3m (2005: R21.0m) for property, plant and equipment and R1.4m (2005: R0.4m) for intangible assets (software). The capital expenditure for the 2007 financial year will be funded from internal resources, and if appropriate from borrowings in line with the short, medium and long term-funding policy. Further details on Umgeni Water's capital commitments are set out in note 27 of the annual financial statements.

Subsequent Events

No material change has taken place in the affairs of the group between the end of the financial year and the date of this report.

Going Concern

The going-concern basis has been adopted in preparing the financial statements. Based on forecasts and available cash resources, the directors have a reasonable expectation that the entity has adequate resources to continue as a going concern in the foreseeable future.

Fruitless and Wasteful Expenditure

No significant fruitless and wasteful expenditure was incurred during the year.

Materiality Framework

In terms of Section 55(1)(d)(i) of the PFMA the materiality level applied during the year is based on 0.5% of gross revenue. Management, however, apply a qualitative aspect to all errors found.

Directorate

The Board as it is currently constituted is set out on pages 12 to 13.

Members of the Board and Executive committee's emoluments are disclosed in note 33 of the annual financial statements in terms of regulation 28.1 of the PFMA.

Changes in directorate that occurred during the year were as follows:

- Dr R Mokate resigned from the board on 27 July 2005 and was replaced as the Chair by Mr NA Gasa, the effective date was 1 August 2005.
- Ms Moloi's resignation was effective from 31 March 2006, and Mr Msiwa was the Acting CEO from 1 April 2006, and was appointed CEO on 1 September 2006

Directors' Responsibility

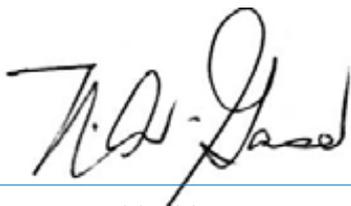
The preparation and presentation of the annual financial statements of Umgeni Water and all other information included in the Annual Report, which must be accurate and consistent with the financial statements, are the responsibility of the directors. The financial statements set out in this report have been prepared in accordance with International Financial Reporting Standards, and in the manner required by the Water Services Act No. 108 of 1997 and sub-section 55(1)(b) of the PFMA.

In discharging their responsibilities, both for the integrity and fairness of these financial statements, the directors rely on systems of internal control procedures applied by management. The Audit Committee of the Board of Directors has met with management and the external auditors to review the financial statements and accounting policies, as well as the effectiveness of the management information system. Nothing has been brought to the attention of the directors to indicate that any material breakdown in the systems of internal control occurred during the period under review.

The entity's external auditors, Deloitte & Touche and Ngubane & Co., have audited the annual financial statements after having been provided unrestricted access to all financial records and related data. The directors believe that all representations made to the external auditors during their audit were valid, appropriate and complete.

Approval of Annual Financial Statements

The annual financial statements set out on pages 61 to 94, are hereby approved by the Board of Directors on 21 September 2006, and signed on its behalf by:



Mr Nhlanhla Gasa
Chairman of the Board
21 September 2006



Mr Mzimkulu Msiwa
Chief Executive Officer
21 September 2006

FINANCIAL REVIEW

Significant increase in profit for the year and strong cash flows result in continued debt reduction.

This financial review should be read in conjunction with the accounting policies adopted by the Board of Umgeni Water, which appear on pages 73 to 78, together with the relevant notes to the annual financial statements containing explanations and analyses of certain key areas.

KEY INDICATORS FOR 2006

- Increased bulk water sales
- Improved interest cover
- Strong positive cash flows from operating activities
- Reduction and restructuring of debt

HIGHLEVEL OVERVIEW

The group has continued to focus on producing improved operating results and in strengthening the balance sheet through debt reduction and, where opportunities are presented, in restructuring the balance sheet.

The first quarter focused on the redemption of the UG55 on 30 September 2005, which was 92.7% funded by the end of the previous financial year. The remaining portion of R61.3m (7.3%) was funded through the sale of a long-dated zero coupon bond, which resulted in proceeds of R287.0m. The remainder of the proceeds were invested into a redemption asset to match a R150.0m loan maturing at the end of the financial year.

During the last quarter of 2006 an opportunity to raise debt at favourable rates resulted in a R350.0m 10-year amortising loan at 8.3% fixed interest rate being used to fund the buy back of R300.0m 13% UG65 bonds, which have a maturity date of 1 June 2010.

The group has applied IFRS for the first time and the most significant impact of this adoption was in terms of IAS 16 (Revised) - property, plant and equipment, which required the componentisation of infrastructure and an annual review of the residual values and useful lives of assets. The changes increased the annual depreciation charge to the 2006 income statement by R23.5m and the prior and previous years by R48.4m collectively.

RESULTS FROM OPERATIONS

Revenue and Other Income

Group revenue, overall, increased by R76.2m year-on-year (7.6%). R66.0m of the increase was derived from the combination of 2.5% increase in volumes of bulk water sold and the tariff increase of 4.6%.

Umgeni Water is pleased with the increase of R15.4m (33.4%) in revenue generated by the Section 30 activities. However, the group increase was only R8.5m as the Share Incentive Trust was wound up in the prior year and generated no income for the 2006 year.

Other income has been split from revenue and is now shown separately below the gross profit line. The parent showed a substantial increase in other income, due to R20.9m from the Share Incentive Trust's final distribution being recognised as sundry income. The group had however recognised this income in prior years, thus the consolidated figure has been reduced accordingly.

Cost of Sales

Water purchases have increased by 5.8%, which is mainly due to the increase in volumes of water sold. Gross profit percentage for the group and parent have remained constant, showing a marginal decrease to 89.6% from 90.4% for the group, and similarly to 89.5% from 90.3% for the parent.

Operating and Administration Expenses

Group operating and administration expenses have increased by 8.5% during the financial year to R575.8m (2005: R530.6m). Significant adjustments recognised during this year were asset impairments of R42.8m (2005: R70.0m), increase in provision for doubtful debts R25.1m (2005: R7.2m) and the amortisation of the reticulation schemes financial asset of R91.6m, which is partially offset by the reduction in depreciation of R29.2m no longer applicable on transfer of the reticulation schemes to the municipalities.

Profit from Operations

Group profit from operations increased by 8.4% from R389.2m to R421.9m.

Net Finance Costs

Group net finance costs for the year totalled R283.7m (2005: R346.5m) a decrease of 18.1%, which was as a result of balance sheet restructuring and lower levels of funding requirements.

The net weighted average cost of capital (“WACC”) at balance sheet date is 12.3% (2005: 15.8%), with the significant improvement arising from the redemption of the UG55 and the removal of the resultant costs associated with the redemption assets. WACC was previously stated based on liabilities only. During the year in order to improve disclosure, a net basis was adopted. The impact is significant in the previous year where WACC increased from 13.3% to 15.8%, and is largely attributable to the negative carry costs on redemption assets.

The interest cover ratio is at a satisfactory level of 1.49 times and reflects a continued improvement from the previous year of 1.12 times.

Profit for the Year

The group profit for the year has shown a substantial increase of 238.8% to R137.6m from the prior year’s restated profit of R40.6m. Details of the restatement can be found in note 3 of the annual financial statements.

FINANCIAL POSITION

Financial Structure

Umgeni Water continues to enjoy its Fitch rating of: F1+ short-term and AA long-term rating. These ratings were reaffirmed on 6 April 2006.

Umgeni Water has one major bond in issue, namely the UG65. The other bond previously in issue (UG55) matured on 30 September 2005.

The UG65 bond together with the DBSA loans constitute 94.8% of the total funding structure of R2,367.8m. Further details relating to the loan structures can be found in Annexure 1 and 2 of the annual financial statements.

During the year, Umgeni Water and DBSA concluded an infrastructure development loan of R50.0m at 5.0% fixed for 15 years to fund the Eston-Umbumbulu pipeline and a 10-year R350.0m fixed interest loan to further restructure the balance sheet through the buy back of UG65 bonds.

Umgeni Water strives to achieve an optimal debt structure of 70% fixed to 30% floating interest rate. The ratio (on a net basis) at year end was 76% fixed to 24% floating interest rate (2005: 78%:22%).

Group net debt to equity ratio at year end is 4.93, which reflect a 20.2% improvement from the prior year’s 6.18.

Balance Sheet

Group property, plant and equipment shows a reduction of R394.7m, which is made up of: R369.9m transfers to reticulation financial assets; R79.3m additions; R3.9m interest capitalised; R0.3m disposals; current depreciation of R64.9m; and impairments of R42.8m.

Group total financial investments at year end were R361.2m (2005: R1,330.0m) reflecting a decrease of R968.8m, which is primarily attributable to the decrease in redemption assets used in the redemption of the UG55 bond.

Group total borrowings at year end were R2,284.8m (2005: R3,355.0m) showing a decrease of R1,070.2m. The R1,070.2m reduction in debt is made up of R335.4m planned repayment of long-term annuity debt, R400.0m additional long-term funding raised through the DBSA, R300.0m buy back of the UG65 and R834.8m repayment of the UG55.

The significant decrease in the short-term funding to R116.2m (2005: R1,214.4m) is due largely to the redemption of the UG55, which in the prior year was classified as short-term funding.

Cash Flow

During the current year the group generated R644.7m (2005: R630.4m) net cash from operating activities. The overdue amount by the Msunduzi Municipality totalling R41.4m had a negative impact on the operating cash flow for the year.

Net cash used in investing activities totalled R80.6m (2005: R4.8m).

Net cash used in financing activities totalled R556.9m (2005: R625.6m), of which R107.9m (2005: R408.6m) was used to meet finance costs.

Debt Management

The treasury strategy focuses on solvency and debt management through the cash flow tariff model, after taking into account the long-term business plans, water demand curves, and future capital expenditure. The liability curve and debt redemption is then actively managed through asset and liability matching after taking into account the sensitivity of the liability curve to changes in real interest rates, inflation rates, water demand and capital expenditure.

Umgeni Water manages its short to medium-term cash flow needs with overdraft facilities and its commercial paper programme. As there was no funding requirement at financial year end, no commercial paper funding was raised (2005: R130.0m). Umgeni Water invested R190.0m in short-term financial investments.

In 2005 Umgeni Water received a three-year borrowing limit for the period 2006 to 2008. Against the current year's borrowing limit of R3,500.0m (2005: R5,200.0m), the unutilised portion is R1,127.5m (2005: R1,711.0m). Management of Umgeni Water viewed the decrease in the limit as a positive factor in light of its debt reduction.

Umgeni Water seeks to minimise its liquidity risk by using amortising loans when required to raise new debt and a redemption portfolio. In line with the redemption policy, financial assets will be set aside for the redemption of the UG65, which matures in June 2010.

Treasury Management

As a result of the removal of Ministerial Intervention on Umgeni Water's treasury operations with effect from 1 January 2005, Umgeni Water has assumed full responsibility of its treasury function. A two-year service level agreement with TCTA is in place whereby strategic support is still being provided.

Capital Expenditure

Umgeni Water expends monies in capital infrastructure requirements to meet its obligation of delivering bulk water. Of the R238.9m capital expenditure approved for 2005/2006, R79.3m was actually spent in the current year, with the remainder carried forward into the next financial year. Details of major projects undertaken during the year are:

Project	Commissioning date	Costs as at 30 June 06	Future expected costs
Umbumbulu pipeline	Jun-06	R42.1m	-
South coast pipeline	Nov-06	R7.8m	R114.2m
53 Pipeline recommissioning	Jul-06	R16.3m	R3.7m
Nagle aquaduct rehabilitation	Sep-06	R0.6m	R8.2m

Reticulation Water Schemes

All reticulation water schemes have been transferred to the relevant Water Service Authorities resulting in the disposal of the rural reticulation assets from Umgeni Water's fixed asset register at 1 July 2005 totalling R369.9m. The disposal of these assets gave rise to a corresponding financial asset representing the amount owed. The financial asset is being amortised over a 6-year period.

During the current year Umgeni Water carried out the retail functions on the reticulation water schemes on behalf of both Msunduzi Municipality and the Umgungundlovu District Municipality.

Performance Review

Ratios (Parent)

Indicator	Unit	DWAF benchmark	F'06 target	Performance			
				Jun-06	Jun-05*	Jun-04	Jun-03
Return on assets	%	>5.0 ✓	>16.4 ✓	20.35	14.94	15.90	11.40
Debt to assets ratio	No.	#	<0.79 ✓	0.76	0.83	0.86	0.73
Interest cover ratio	No.	>1.35 ✓	>1.50 ✓	1.54	1.10	0.92	0.82
Net debt to equity ratio	No.	<1.25 ✗	<4.67 ✗	4.96	6.56	8.42	6.95
Current ratio	No.	>1.75 ✗	>0.45 ✓	1.20	0.70	0.90	0.75
Debtors' collection period	Day	<38 ✗	<38 ✗	47	42	39	47
Tariff increases	%	#	CPIx ✓	4.60	5.60	8.00	7.02
Credit rating - Long term	(ZAF)	#	AA ✓	AA	AA	AA	AA
- Short term	(ZAF)	#	F1+ ✓	F1+	F1+	F1+	F1+

(*) restated amounts used where applicable
 (#) no benchmark set

✓ Achieved
 ✗ Not achieved

Refer to the Five-year financial review for definition of ratios

The targeted net debt to equity ratio was calculated prior to the implementation of IFRS, if excluded, the actual net debt to equity ratio would have been 4.19, thus having achieved the target.

The deterioration in the debtors' collection period is largely attributed to R41.4m overdue by Msunduzi Municipality.

Subsidiary and Associate Companies

Msinsi Holdings (Pty) Ltd ("Msinsi") (100%)

Msinsi continues to provide a valuable service to Umgeni Water in terms of land and wildlife management of the land surrounding some of Umgeni Water's major dams and treatment works. During the current year Msinsi reported a profit of R4.6m, mainly due to the recognition of game stock on its balance sheet.

Umgeni Water Services (Pty) Ltd ("UWS") (100%)

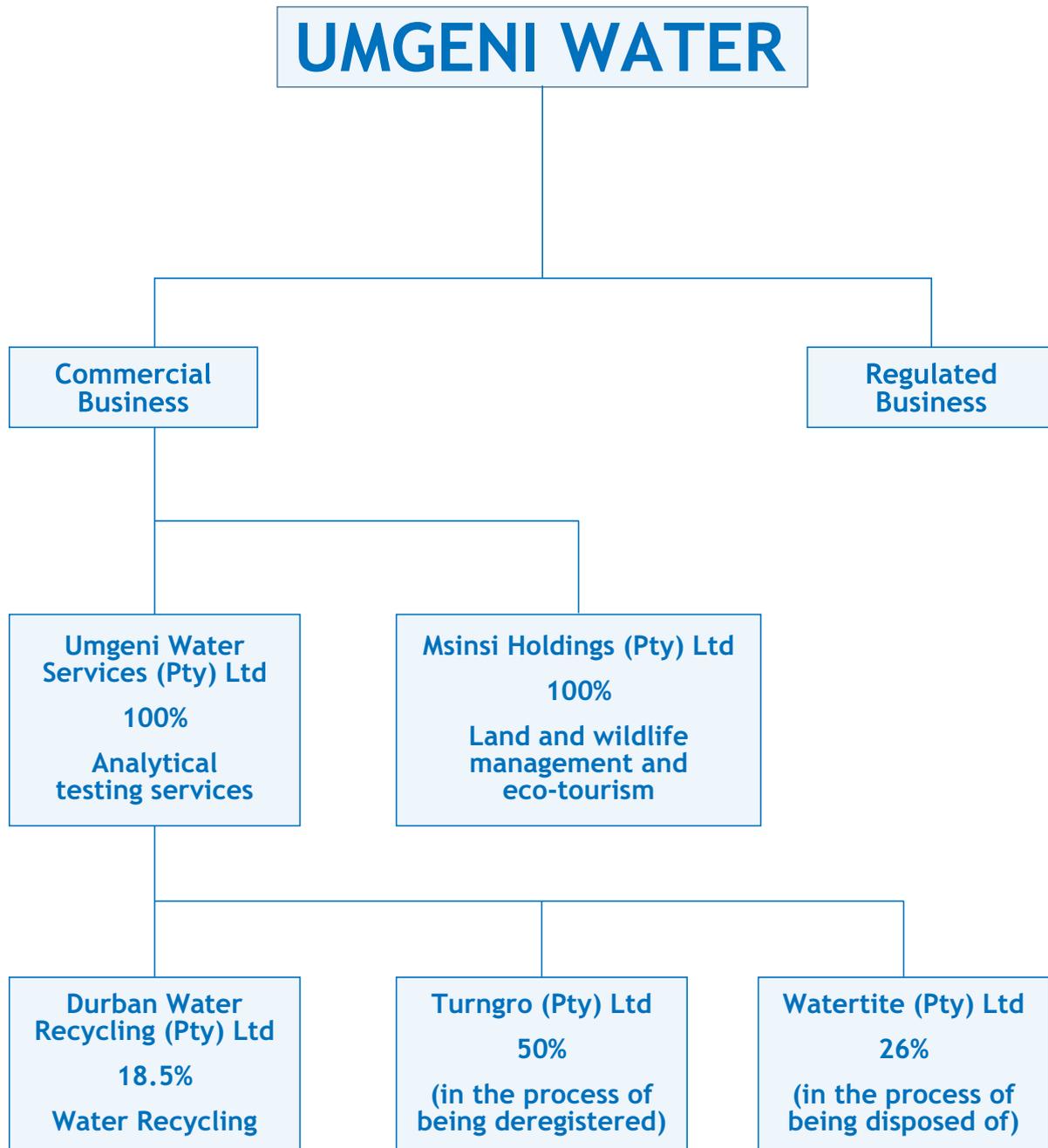
UWS' main business is holding of investments and carrying out other commercial activities. UWS generated a small profit for the year of R1.3m, attributable to Durban Water Recycling. UWS has investments in other companies with business in wastewater recycling and water services and billing solutions. In May 2004, Turngro Water Services (Pty) Ltd, one of UWS' subsidiaries stopped trading and is in the process of being deregistered.

All losses and impairments were recognised in 2003 thus no further adjustments will be necessary.

Umgeni Water Share Incentive Trust

The Trust has been wound up and a final distribution of R20.9m has been recognised by Umgeni Water, as the parent. The group had recognised these profits over the past years as they arose.

ORGANISATIONAL STRUCTURE



CONSOLIDATED INCOME STATEMENTS

For the year ended 30 June 2006

	Notes	Group		Parent	
		2006	2005 Restated	2006	2005 Restated
		kI'000	kI'000	kI'000	kI'000
Treated water volume sold		361,438	352,634	361,438	352,634
		R'000	R'000	R'000	R'000
Revenue	4	1,084,544	1,008,352	1,076,703	993,578
Cost of sales	5	(112,825)	(96,656)	(112,825)	(96,656)
Gross profit		971,719	911,696	963,878	896,922
Other income	6	26,057	8,137	40,216	6,545
Operating and administration expenses		(575,832)	(530,581)	(566,431)	(523,088)
Staff costs	7	(207,098)	(210,115)	(194,318)	(200,360)
Energy		(23,420)	(35,719)	(23,420)	(35,719)
Depreciation	3.2 & 7	(64,945)	(84,859)	(63,505)	(83,763)
Amortisation	3.2 & 7	(93,466)	(1,619)	(93,466)	(1,619)
Chemicals		(21,731)	(18,413)	(21,731)	(18,413)
Other operating and administration expenses		(165,172)	(179,856)	(169,991)	(183,214)
Profit from operations	7	421,944	389,252	437,663	380,379
Net finance costs		(283,741)	(346,469)	(283,586)	(346,610)
Interest income	8	190,165	121,618	190,309	121,525
Finance costs	9	(473,906)	(468,087)	(473,895)	(468,135)
Profit before taxation		138,203	42,783	154,077	33,769
Taxation	10	(640)	(2,175)	-	-
Profit for the year		137,563	40,608	154,077	33,769

CONSOLIDATED BALANCE SHEETS

As at 30 June 2006

	Notes	Group		Parent	
		2006	2005	2006	2005
		R'000	Restated R'000	R'000	Restated R'000
ASSETS					
Non-current assets					
		2,589,713	2,972,035	2,585,371	2,973,565
Property, plant and equipment	11	2,152,478	2,547,147	2,150,801	2,544,547
Intangible assets	12	3,300	3,730	3,300	3,730
Investments - financial instruments	13	92,977	413,740	92,977	413,740
Investments - subsidiaries and associates	14	5,175	4,084	7,309	8,214
Other non-current assets	15	335,783	3,334	330,984	3,334
Current assets					
		407,363	1,056,739	405,921	1,054,584
Current investments	16	268,208	916,315	268,208	916,315
Inventories	17	6,940	8,171	6,870	8,112
Trade and other receivables	18	117,451	125,713	117,187	125,256
Interest and premium receivable	19	1,335	301	1,335	301
Bank and cash	20	13,429	6,239	12,321	4,600
Total assets		2,997,076	4,028,773	2,991,292	4,028,149
EQUITY AND LIABILITIES					
Capital and reserves					
		390,171	327,661	387,882	308,858
Capital	21	442,847	442,847	442,847	442,847
Investment revaluation reserves		13,275	88,328	13,275	88,328
Accumulated loss		(65,951)	(203,514)	(68,240)	(222,317)
Non-current liabilities					
		2,266,488	2,220,660	2,266,488	2,220,660
Long-term liabilities	22	2,168,572	2,140,595	2,168,572	2,140,595
Other non-current liabilities	23	97,916	80,065	97,916	80,065
Current liabilities					
		340,417	1,480,452	336,922	1,498,631
Accounts payable	24	154,849	167,939	152,647	187,315
Provisions	25	29,369	27,030	28,076	25,833
Short-term funding	26	116,190	1,214,396	116,190	1,214,396
Interest payable		40,009	71,087	40,009	71,087
Total equity and liabilities		2,997,076	4,028,773	2,991,292	4,028,149

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

For the year ended 30 June 2006

	Notes	Group			
		Capital R'000	Investment revaluation reserve R'000	Accumulated loss R'000	Total R'000
Balance as at 30 June 2004		442,847	63,219	(217,368)	288,698
Effect of adoption of IFRS	3				
IAS16: Adjustment to opening accumulated loss in respect of depreciation of property, plant and equipment				(34,107)	(34,107)
Restated balance as at 30 June 2004		442,847	63,219	(251,475)	254,591
Movement for the year					
Restated profit for the year				40,608	40,608
Profit for the year as previously reported				54,928	54,928
Effects of adoption of IFRS	3			(14,320)	(14,320)
Mark-to-market adjustment - long-term investments			32,462		32,462
Transfer (from) to reserves			(7,353)	7,353	-
Restated balance as at 30 June 2005		442,847	88,328	(203,514)	327,661
Movement for the year					
Profit for the year				137,563	137,563
Mark-to-market adjustment - long-term investments			(75,053)		(75,053)
Released on sale of assets	8		(74,035)		(74,035)
Adjustment on revaluation			(1,018)		(1,018)
Balance as at 30 June 2006		442,847	13,275	(65,951)	390,171

	Notes	Parent			
		Capital R'000	Investment revaluation reserve R'000	Accumulated loss R'000	Total R'000
Balance as at 30 June 2004		442,847	55,866	(221,979)	276,734
Effect of adoption of IFRS	3				
IAS16: Adjustment to opening accumulated loss in respect of depreciation of property, plant and equipment				(34,107)	(34,107)
Restated balance as at 30 June 2004		442,847	55,866	(256,086)	242,627
Movement for the year					
Restated profit for the year				33,769	33,769
Profit for the year as previously reported				48,089	48,089
Effects of adoption of IFRS	3			(14,320)	(14,320)
Mark-to-market adjustment - long-term investments			32,462		32,462
Restated balance as at 30 June 2005		442,847	88,328	(222,317)	308,858
Movement for the year					
Profit for the year				154,077	154,077
Mark-to-market adjustment - long-term investments			(75,053)		(75,053)
Released on sale of assets	8		(74,035)		(74,035)
Adjustment on revaluation			(1,018)		(1,018)
Balance as at 30 June 2006		442,847	13,275	(68,240)	387,882

CONSOLIDATED CASH FLOW STATEMENTS

For the year ended 30 June 2006

	Notes	Group		Parent	
		2006	2005	2006	2005
		R'000	Restated R'000	R'000	Restated R'000
OPERATING ACTIVITIES					
Cash receipts from customers		1,093,486	987,250	1,079,860	971,342
Cash paid to suppliers and employees		(448,832)	(356,838)	(437,303)	(352,054)
<i>Net cash from operating activities</i>	A	644,654	630,412	642,557	619,288
INVESTING ACTIVITIES					
Proceeds on disposals of property, plant and equipment		504	2,407	440	2,407
Additions to property, plant and equipment		(79,376)	(20,353)	(78,859)	(18,353)
Additions to intangible assets		(1,423)	(370)	(1,423)	(370)
Additions to biological assets		(1,540)	-	(1,540)	-
Investments in subsidiaries and associates		1,190	13,482	3,210	21,796
<i>Net cash (used in) from investing activities</i>		(80,645)	(4,834)	(78,172)	5,480
FINANCING ACTIVITIES					
Long-term borrowings raised		400,000	-	400,000	-
Long-term borrowings repaid		(1,405,179)	(147,085)	(1,405,179)	(146,282)
Short-term borrowings repaid		(126,840)	(31,000)	(126,840)	(31,000)
Investments decreased (increased)		683,107	(38,858)	683,107	(38,858)
Interest received		302,756	46,981	302,900	46,500
Finance costs paid		(410,663)	(455,598)	(410,652)	(455,257)
<i>Net cash used in financing activities</i>		(556,819)	(625,560)	(556,664)	(624,897)
CASH AND CASH EQUIVALENTS					
Net increase (decrease) for the year		7,190	18	7,721	(129)
At beginning of year		6,239	6,221	4,600	4,729
At end of year	20	13,429	6,239	12,321	4,600

NOTES TO THE CASH FLOW STATEMENTS

A. RECONCILIATION OF PROFIT FOR THE YEAR TO NET CASH GENERATED FROM OPERATING ACTIVITIES					
Profit for the year		137,563	40,608	154,077	33,769
Adjusted for non-cash items:					
Interest income		(190,165)	(121,618)	(190,309)	(121,525)
Finance costs		473,906	468,087	473,895	468,135
Fair value adjustment of biological assets		(5,754)	-	(955)	-
Asset impairments and write-offs		42,822	70,030	42,822	70,030
Investment impairments (reversed) raised		(1,009)	250	(2,304)	(863)
Amortisation - reticulation asset		91,613	-	91,613	-
Amortisation - intangible asset		1,853	1,619	1,853	1,619
Depreciation		64,945	84,859	63,505	83,763
Profit on disposal of property, plant and equipment		(233)	(190)	(170)	(377)
Increase in provisions		20,200	39,620	20,094	39,849
Increase in doubtful debts provision		25,106	7,144	25,035	7,204
Share Incentive Trust declaration		-	-	(20,932)	-
Profit from associate		(1,877)	(1,592)	-	-
Taxation on profit from associate		605	479	-	-
Operating surplus before working capital changes		659,575	589,296	658,224	581,604
Working capital changes		(14,921)	41,116	(15,667)	37,684
Increase in accounts receivable		(13,022)	(28,687)	(15,172)	(28,780)
Decrease in inventory		1,232	1,928	1,242	1,942
(Decrease) increase in accounts payable		(3,131)	67,875	(1,737)	64,522
Net cash from operating activities		644,654	630,412	642,557	619,288

SEGMENTAL REPORT

For the year ended 30 June 2006

Umgeni Water has two reportable segments, namely primary and other activities (as defined by Section 30 of the Water Services Act). The accounting policies of the segments are consistent with those described on pages 73 to 78.

The primary segment is made up of bulk water and waste water reticulation. The other activities segments is made up of non-regulated activities by Umgeni Water and its subsidiaries, Msinsi Holdings (Pty) Ltd and Umgeni Water Services (Pty) Ltd.

For the year ended 30 June 2006	Group			
	Primary activities		Other activities R'000	Total R'000
	Bulk water R'000	Waste water R'000		
Revenue	972,569	42,420	69,555	1,084,544
Cost of sales	(60,892)	-	(51,933)	(112,825)
Gross profit	911,677	42,420	17,622	971,719
Other income	19,277	-	6,780	26,057
Operating and administration expenses	(318,194)	(45,820)	(11,594)	(375,608)
Depreciation and amortisation	(156,329)	(642)	(1,440)	(158,411)
Impairments	(42,822)	-	1,009	(41,813)
Profit from operations	413,609	(4,042)	12,377	421,944
Interest income	190,021	-	144	190,165
Finance costs	(467,789)	(6,103)	(14)	(473,906)
Taxation	-	-	(640)	(640)
Profit (loss) for the year	135,841	(10,145)	11,867	137,563
Capital expenditure - for the year	78,438	421	517	79,376
Segment assets	2,068,445	82,356	1,677	2,152,478
Interest in associate	-	-	5,175	5,175
Unallocated				839,423
Consolidated total assets				2,997,076
Segment liabilities	2,202,406	82,356	-	2,284,762
Unallocated				322,143
Consolidated total liabilities				2,606,905

For the year ended 30 June 2005 (restated)

Revenue	906,566	40,735	61,051	1,008,352
Cost of sales	(65,509)	-	(31,147)	(96,656)
Gross profit	841,057	40,735	29,904	911,696
Other income	6,545	-	1,592	8,137
Operating and administration expenses	(479,996)	(24,197)	(26,388)	(373,823)
Depreciation and amortisation	(84,767)	(615)	(1,096)	(86,478)
Impairments	(70,030)	-	(250)	(70,280)
Profit from operations	212,809	15,923	3,762	389,252
Interest income	121,526	-	92	121,618
Finance costs	(459,689)	(8,445)	47	(468,087)
Taxation	-	-	(2,175)	(2,175)
Profit for the year	(125,354)	7,478	1,726	40,608
Capital expenditure	17,868	485	2,000	20,353
Segment assets	3,117,775	83,540	2,600	3,203,915
Interest in associate	-	-	4,084	4,084
Unallocated				820,774
Consolidated total assets				4,028,773
Segment liabilities	3,271,451	83,540	-	3,354,991
Unallocated				346,121
Consolidated total liabilities				3,701,112

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

For the year ended 30 June 2006

1. ACCOUNTING POLICIES

PRESENTATION OF FINANCIAL STATEMENTS

The financial statements were prepared in accordance with International Financial Reporting Standards (“IFRS”) for the first time and as such the group’s opening balance sheet as at 1 July 2004 has been restated to reflect all IFRS statements applicable at 30 June 2006. The disclosures required by IFRS 1 concerning the transition from SA GAAP to IFRS are set out on page 79. The principal accounting policies adopted are set out below.

CONSOLIDATION

The consolidated financial statements incorporate the financial statements of Umgeni Water and other entities controlled by Umgeni Water (its subsidiaries) acquired up to 30 June each year. Control is achieved where Umgeni Water has the power to govern the financial and operating policies of the acquired entity so as to obtain benefits from its activities.

The assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill.

Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired, such as a discount on acquisition, is credited to profit and loss in the period of acquisition. The interest of minority shareholders is stated at the minority’s proportion of the fair values of the assets and liabilities recognised. Subsequently, any losses applicable to the minority interest in excess of the minority interest are allocated against the interests of the parent.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used in line with those used by the group.

All material inter-company balances and transactions are eliminated.

REVENUE

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for water sales to customers, revenue from waterworks, wastewater works, management fees from the management of waste water works and revenue from other activities conducted as defined in terms of section 30 of the Water Services Act, net of discounts and Value Added Taxation.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset’s net carrying amount.

RAW WATER PURCHASES

Raw water purchases are considered to be the primary segment’s direct costs. All other costs are considered to be operating expenses. The cost directly attributable to sales for other activities, as defined in section 30 of the Water Services Act, are shown as cost of sales.

TAXATION

Umgeni Water and Msinsi Holdings (Pty) Ltd are tax-exempt entities in terms of Section 10 (1) (cA) (i) of the Income Taxation Act and therefore the policy is only in respect of its subsidiaries and associates.

Umgeni Water Services (Pty) Ltd and Umgeni Water Share Incentive Trust are subject to taxation as follows:

- The tax expense represents the sum of the tax currently payable and deferred tax.
- The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.
- The group’s liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.
- Deferred tax is the tax expected to be payable or recoverable on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.
- The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

1. ACCOUNTING POLICIES (continued)

PROPERTY, PLANT & EQUIPMENT

Land, buildings and infrastructure, and capital work in progress

Assets in commission, with the exception of land, which is not depreciated, are stated at net book value and depreciated on a straight-line basis on the depreciable portion over their estimated useful lives. Work in progress is stated at cost and is commissioned on date of significant completion. The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Asset category	Depreciable portion %	Estimated useful life (years)
Dams and weirs	10	45
Reservoirs and intake works	100	45
Tunnels	10	45
Pump stations		
• Structural	40	30
• Mechanical	100	15
• Instrumentation	100	10
• Electrical	100	10
PVC and concrete pipelines	100	45
Steel and GRP pipelines	100	30
Water treatment works		
• Structural	30	45
• Mechanical	100	15
• Instrumentation	100	10
• Electrical	100	10
Wastewater works		
• Structural	30	45
• Mechanical	100	15
• Instrumentation	100	10
• Electrical	100	10
Buildings	100	40

Equipment and vehicles

Equipment and vehicles are stated at cost and are depreciated over their useful lives to estimated residual values, on a straight line basis as follows:

Asset category	Depreciable portion %	Estimated useful life (years)
Furniture and fittings	100	5
Scientific services equipment	100	5
Vehicles and plant	100	5
Other equipment	100	5
Computers		
• Desktops, servers, networks and printers	100	5
• Notebooks	100	3
• Radio equipment	100	5

Leased assets

Classification

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

1. ACCOUNTING POLICIES (continued)

In the capacity of a lessor

Amounts due from lessees under finance leases are recorded as receivables at the amount of the group's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on the group's net investment outstanding in respect of the leases.

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease.

In the capacity of a lessee

Assets held under finance leases are recognised as assets of the group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the group's general policy on borrowing costs.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

CAPITALISATION OF BORROWING COSTS

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing cost eligible for capitalisation to those assets.

All other borrowing costs are reflected in the income statement in the period in which they are incurred.

INVESTMENT PROPERTY

Investment property, which is held to earn rentals and for capital appreciation is shown at cost, less subsequent depreciation and impairment.

INVESTMENTS IN ASSOCIATES

An associate is an entity over which the group has significant influence and that is neither a subsidiary nor a joint venture. Significant influence is the power to participate in the financial and operating decisions of the investee but is not control or joint control over those policies. Consolidated financial statements incorporate the assets, liabilities, income and expenses of associates using the equity method of accounting from the acquisition date to the disposal date, except when the investment is classified as held for sale, in which case it is accounted for as non-current assets held for sale. The carrying amount of such investments is reduced to recognise any decline, other than a temporary decline, in the value of individual investments.

Losses of associates in excess of the group's interest are not recognised unless there is a binding obligation to contribute to the losses.

Goodwill arising on the acquisition of associates is accounted for in accordance with the accounting policy for goodwill as set out below, but is included in the carrying amount of the associate.

Where a group entity transacts with an associate of the group, unrealised profits and losses are eliminated to the extent of the group's interest in the relevant associate.

INTANGIBLE ASSETS

Research and development

Research expenditure is expensed immediately. Development expenditure is recognised as an expense, unless it is probable that it will give rise to a product that will generate future benefits for the organisation, in which case it is capitalised.

Development costs are only recognised as assets if all the following conditions are met:

- an asset is created that can be identified;
- it is probable that the asset created will generate future economic benefits; and
- the development costs of the asset can be measured reliably.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

1. ACCOUNTING POLICIES (continued)

INTANGIBLE ASSETS (continued)

Software

Software and licences are carried at cost less accumulated amortisation and any impairment in value.

Internally developed and packaged software and the direct costs associated with the development and installation thereof are capitalised and recognised as intangible assets.

Software is amortised in full on a straight-line as follows:

- customised software 5 years
- shelf software 2 years

Costs associated with research and development of computer software programs are recognised as an expense as they are incurred. Development costs are capitalised if all the following conditions are met:

- a separately identifiable asset is created;
- it is probable that the asset created will generate future economic benefits or will be put to use by Umgeni Water; and
- the development costs of the asset can be measured reliably.

Costs relating to the acquisition of licences are treated as an expense in the period in which the licence is acquired.

Other intangible assets

Intangible assets are initially recognised at cost if acquired separately or internally generated, or at fair value if acquired as part of a business combination. If assessed as having an indefinite useful life, it is not amortised but tested for impairment annually and impaired if necessary. If assessed as having a finite useful life, it is amortised over their useful lives using a straight-line basis, and tested for impairment if there is an indication that they may be impaired.

IMPAIRMENT

At each balance sheet date, the group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Where the asset does not generate cash flows that are independent from other assets, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs. An intangible asset with an indefinite useful life is tested for impairment annually and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value-in-use. In assessing value-in-use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset, or cash-generating unit, is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit, is reduced to its recoverable amount.

An impairment loss is recognised as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, in order that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset or cash generating unit, in prior years.

A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

BIOLOGICAL ASSETS

Game stock and plantations are measured at their fair value less estimated point-of-sale costs. The fair value of biological assets are determined annually based on market prices of similar age, type, and genetic merit. All changes in fair values are recognised in income in the period in which they arise.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

1. ACCOUNTING POLICIES (continued)

INVENTORIES

Inventories are stated at the lower of the weighted average cost and net realisable value. Obsolete, redundant and slow-moving inventories are identified and written down to the estimated net realisable value.

Net realisable value is the estimate of the selling price in the ordinary course of business, less the estimated costs of completion, selling and distribution expenses.

FINANCIAL INSTRUMENTS

Financial instruments are initially measured at cost, which includes transaction costs, when the group is party to a contractual arrangement. Subsequent measurement of financial instruments is set out below.

Set-off

Financial assets and financial liabilities are only offset if there is a legal right to offset and there is an intention either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Investments

Investments in the long-term investment portfolio are classified as available-for-sale assets and stated at fair value, which is determined with reference to exchange quoted prices at the close of business on the balance sheet date.

Realised profits and losses on sale of investments are reflected in the income statement as and when incurred. Umgeni Water has elected to reflect the mark-to-market unrealised profit or loss on valuation of these investments in equity until the asset is disposed of, at which time it is recognised in the income statement.

Investments held in the redemption portfolio are classified as held-to-maturity and are reflected at amortised cost on the yield-to-maturity basis.

Investments in securities are recognised on a trade date basis and are initially measured at cost. At subsequent reporting dates, debt securities that the group holds are measured at fair value.

For available-for-sale investments, unrealised gains and losses are recognised in equity, until the security is disposed of or is determined to be impaired, at which time the net profit or loss is released to the income statement.

Trade and other receivables

Short duration receivables with no stated interest rate are measured at original invoice amount less provision for doubtful debts.

Cash and cash equivalents

Cash and cash equivalents comprise bank balances and cash on hand.

Interest bearing liabilities

Interest bearing liabilities comprise loan stock and other loans utilised to finance water supply, and other related infrastructure. Locally registered bonds in issue are stated at amortised cost, applying yield-to-maturity basis.

Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption, are accounted for on an accrual basis and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Loan discounts

Loan discounts are amortised over the life of the underlying loans on a yield-to-maturity basis.

Trade and other payables

Trade payables are initially measured at fair value and are subsequently measured at amortised cost using the effective interest rate method.

UMGENI WATER CAPITAL AND GRANT FUNDING

Capital grants received by Umgeni Water after 1 July 2000 are reflected against property, plant and equipment. These are amortised against income over the remaining useful life of the assets to which the grants relate. Capital grants received prior to 1 July 2000 are shown on the balance sheet as Umgeni Water capital and included under capital.

NON-DISTRIBUTABLE RESERVES

Investment revaluation reserve

This reserve arises as a result of the mark-to-market valuation of the long-term investments that are available for sale.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

1. ACCOUNTING POLICIES (continued)

RETIREMENT BENEFITS

Pension and provident fund

Benefits are provided to all eligible employees. Current contributions to the Retirement Fund or the Provident Fund operated for employees are charged against income as incurred. The costs of any improved pension fund benefits or deficits arising from time to time on the funds are charged against income.

Payments to defined contribution retirement benefit plans are charged as an expense as they fall due.

For defined benefit retirement benefit plans, the cost of providing benefits is determined using the projected unit credit method with actuarial valuations being carried out every three years. Actuarial gains and losses are recognised immediately in the year in which they arise.

Medical aid

The full past service liability is provided for at the end of the reporting period. Payments made against the past service liability are reflected against the provision, whilst the current portion of the past service liability and actuarial gains and losses are raised against the income statement.

PROVISIONS

Provisions are recognised when the group has a present obligation as a result of a past event and it is probable that this will result in an outflow of economic benefits that can be reliably estimated.

Provisions for restructuring costs are recognised when the group has a detailed formal plan for the restructuring and the group has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

Restructuring provisions only include those direct expenditures, which are necessarily incurred by the restructuring and not associated with the ongoing activities of the enterprise.

FINANCIAL GUARANTEE CONTRACTS

Financial guarantee contracts are accounted for as insurance contracts and consequently are measured initially at cost and thereafter in accordance with IAS 37 - Provisions, contingent liabilities and contingent assets.

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

CRITICAL JUDGEMENTS IN APPLYING THE GROUP'S ACCOUNTING POLICIES

In the process of applying the group's accounting policies, management has made the following judgements that potentially have the most significant effect on the amounts recognised in the financial statements:

- Retirement benefit (defined benefit plan and medical aid)

Medical aid benefits

The group is providing for the cost of retirement medical aid benefits. An analysis of the impact of changes in the central assumptions on the accrued liability are presented in the table below:

Sensitivity factor	Central Assumption	%	Accrued liability		
			Increase	Decrease	
			R'000	%	R'000
1% change in medical aid inflation rate	7.5%	19.1	12,465	-15.1	(9,863)
1 year change in average retirement age	63 years	-4.8	3,334	5.1	(3,158)

The information presented above is as per the latest valuation, which was performed on 31 December 2004. For further information refer to note 30.

- The mark-to-market valuation of available for sale investments, where no market or suitable proxy exists is calculated using a constant spread above the prevailing zero curve.
- The judgment applied to amortisation of the reticulation asset is 6 years, this was based on the debt curve of Umgeni Water at the time of raising the financial asset.

KEY SOURCES OF ESTIMATION UNCERTAINTY

There are no other key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date that management have assessed as having a significant risk of causing material adjustment to the carrying amounts of the assets and liabilities within the next financial year.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

3. COMPARATIVES

3.1. REVENUE AND OTHER INCOME

During the year, "other income" was removed from revenue and disclosed separately on the face of the income statement after the calculation of gross profit.

3.2. ADOPTION AND FIRST TIME RECOGNITION OF IFRS

As a consequence of adopting IFRS in the current year, certain accounting policies have been revised as set out below:

IAS 16 - Property, plant and equipment

IAS 16 requires property, plant and equipment to be componentised. The componentisation approach requires that depreciation be determined separately for each significant part of an item of property, plant and equipment. Adjustments arising as a result of new or different depreciation have resulted in prior year figures being restated and adjustments made to opening accumulated loss.

IAS 38 - Intangible assets

IAS 38 requires software be disclosed as an intangible asset and thus the amount relating to software has been reclassified out of property, plant and equipment and separately disclosed as intangible assets. The amortisation of intangible assets has been reclassified out of depreciation to a separate line item, thus there is no impact on profit for the year.

The revised accounting policies have been applied retrospectively, and have resulted in the following changes:

- > IAS 16: Revised depreciation calculations
- > IAS 38: Intangible asset - software amortisation

	As previously reported	Group IAS 16		IAS 38	As restated
		Previous years	Prior year		
Income Statement					
Depreciation	72,158	-	14,320	(1,619)	84,859
Amortisation - intangible assets	-	-	-	1,619	1,619
Net profit for the year	54,928	-	(14,320)	-	40,608
Balance Sheet					
Property, plant and equipment	2,599,304	(34,107)	(14,320)	(3,730)	2,547,147
Intangible assets	-	-	-	3,730	3,730
Accumulated loss	(155,087)	(34,107)	(14,320)	-	(203,514)

	As previously reported	Parent IAS 16		IAS 38	As restated
		Previous years	Prior year		
Income Statement					
Depreciation	71,062	-	14,320	(1,619)	83,763
Amortisation - intangible assets	-	-	-	1,619	1,619
Net profit for the year	48,089	-	(14,320)	-	33,769
Balance Sheet					
Property, plant and equipment	2,596,704	(34,107)	(14,320)	(3,730)	2,544,547
Intangible assets	-	-	-	3,730	3,730
Accumulated loss	(173,890)	(34,107)	(14,320)	-	(222,317)

3.3. CASH FLOW STATEMENT

The cash flow statement is now presented using the direct method. The indirect method information is disclosed through a note. In line with IFRS, finance costs have been reclassified as financing activities and no longer operating activities.

3.4. SEGMENTAL REPORT

The segmental report no longer reflects the reticulation segment as this has been discontinued, and now reflects the two primary segments as being bulk water and waste water.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 Restated R'000	2006 R'000	2005 Restated R'000
4. REVENUE				
Water sales	972,569	906,566	972,569	906,566
Waste water	42,420	40,735	42,420	40,735
Other activities	69,555	61,051	61,714	46,277
Total revenue	1,084,544	1,008,352	1,076,703	993,578
5. COST OF SALES				
Water purchases	69,318	65,509	69,318	65,509
Other activities	43,507	31,147	43,507	31,147
Total cost of sales	112,825	96,656	112,825	96,656
6. OTHER INCOME				
Sundry income	16,404	4,820	37,240	4,820
Rental income	2,022	1,725	2,021	1,725
Fair value adjustment of biological assets	5,754	-	955	-
Share of profit from associates	1,877	1,592	-	-
Total other income	26,057	8,137	40,216	6,545
7. PROFIT FROM OPERATIONS				
Profit from operations is stated after the following discloseable items:				
Asset impairments and write-offs	42,822	70,030	42,822	70,030
Amortisation	93,466	1,619	93,466	1,619
- Reticulation financial asset (refer to note 15)	91,613	-	91,613	-
- Intangible assets (refer to note 12)	1,853	1,619	1,853	1,619
Auditors' remuneration	1,662	1,155	1,465	1,100
- Audit fees - current year	1,438	900	1,241	845
- Audit fees - prior year under provision	224	232	224	232
- Fees for other services	-	23	-	23
Doubtful debts provision	25,106	7,144	25,035	7,204
Board members' emoluments (refer to note 33)	3,399	3,061	2,640	2,234
Depreciation (refer to note 3 & 11)	64,945	84,859	63,505	83,763
- Buildings and infrastructure	56,521	75,057	56,521	75,057
- Equipment and vehicles	8,424	9,802	6,984	8,706
Investment impairments (reversed) raised	(1,009)	250	(2,304)	(863)
Profit on disposal of property, plant and equipment	(233)	(190)	(170)	(377)
Operating lease payments	1,534	1,633	1,534	1,633
Staff costs	207,098	210,115	194,318	200,360
- Salaries and wages	171,840	160,312	160,113	150,557
- Retirement benefit expenses				
- Medical aid	9,431	26,474	9,431	26,474
- Defined contribution plan	4,541	3,075	3,488	3,075
- Defined benefit plan	21,286	20,254	21,286	20,254
Average number of employees during the year for the group were 908 (2005: 920), and for the parent were 789 (2005: 787).				
8. INTEREST INCOME				
Interest received	116,130	121,618	116,274	121,525
Realised profit on sale of investments	74,035	-	74,035	-
Total interest income	190,165	121,618	190,309	121,525

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006	2005	2006	2005
	R'000	Restated R'000	R'000	Restated R'000
9. FINANCE COSTS				
Interest expense	428,972	468,686	428,961	468,734
Realised capital loss on UG65 buy back	48,868	-	48,868	-
Less: borrowing costs capitalised	(3,934)	(599)	(3,934)	(599)
Interest is capitalised to work-in-progress at a rate of 12.32% (2005: 13.25%) per annum.				
Total finance costs	473,906	468,087	473,895	468,135

10. TAXATION

10.1 The group

Umgeni Water and Msinsi is exempt from taxation in terms of section 10 (1) (cA) (i) of the Income Tax Act.

10.2 Umgeni Water Services (Pty) Ltd

Taxation expense

(605) (479) - -

10.3 Umgeni Water Share Incentive Trust

Taxation expense

(35) (1,696) - -

Current year taxation payable

- (1,689)

Prior year under provision

(35) (7) - -

Total taxation

(640) (2,175) - -

11. PROPERTY, PLANT AND EQUIPMENT

	Land R'000	Buildings and infrastructure R'000	Equipment and vehicles R'000	Capital work in progress R'000	Total parent R'000	Subsidiaries R'000	2006 Group R'000	2005 Group Restated R'000
Year ended 30 June 2006								
Net book value 1 July 2005	7,139	2,509,394	11,058	16,956	2,544,547	2,600	2,547,147	2,683,301
Cost	7,139	3,085,954	85,719	16,956	3,195,768	8,147	3,203,915	3,275,528
Accumulated depreciation	-	576,560	74,661	-	651,221	5,547	656,768	592,227
Additions	-	-	-	78,859	78,859	517	79,376	20,353
Borrowing costs capitalised	-	-	-	3,934	3,934	-	3,934	599
Disposals	-	(11)	(259)	-	(270)	-	(270)	(2,217)
Cost	-	(33)	(842)	-	(875)	(507)	(1,382)	(6,715)
Accumulated depreciation	-	22	583	-	605	507	1,112	4,498
Transfers to financial asset	-	(369,942)	-	-	(369,942)	-	(369,942)	-
Cost	-	(622,909)	-	-	(622,909)	-	(622,909)	-
Accumulated depreciation	-	252,967	-	-	252,967	-	252,967	-
Depreciation charge	-	(56,521)	(6,984)	-	(63,505)	(1,440)	(64,945)	(84,859)
Impairment	-	(42,822)	-	-	(42,822)	-	(42,822)	(70,030)
Cost	-	(73,987)	-	-	(73,987)	-	(73,987)	(85,849)
Accumulated depreciation	-	31,165	-	-	31,165	-	31,165	15,819
Transfers/commissioning	-	46,904	14,873	(61,777)	-	-	-	-
Total property, plant and equipment	7,139	2,087,002	18,688	37,972	2,150,801	1,677	2,152,478	2,547,147
Cost	7,139	2,435,929	99,750	37,972	2,580,790	8,157	2,588,947	3,203,915
Accumulated depreciation	-	(348,927)	(81,062)	-	(429,989)	(6,480)	(436,469)	(656,768)
Total property, plant and equipment	7,139	2,087,002	18,688	37,972	2,150,801	1,677	2,152,478	2,547,147

Infrastructure consists of pipelines, dams, weirs, reservoirs, tunnels, pump stations, sludge plants, water treatment works and waterworks. Equipment and vehicles consists of motor vehicles, computer hardware and furniture & fittings.

The impact of adopting IFRS is a R34.1m increase in opening accumulated depreciation, a R14.3m increase in the prior year's depreciation charge for infrastructure and buildings, and software has been reclassified to intangible assets.

The impairment losses on infrastructure arose due to the cession of use in the production of income.

During the year reticulation assets were transferred to financial assets at their carrying value of R369.9m, refer to note 15 for further details.

A schedule of land and buildings is available for inspection at the registered office of Umgeni Water.

Subsidiaries

The subsidiaries property, plant and equipment is all classified as equipment and vehicles.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006	2005	2006	2005
	R'000	Restated R'000	R'000	Restated R'000
12. INTANGIBLE ASSETS				
SOFTWARE				
Net book value 1 July 2005	3,730	4,979	3,730	4,979
Cost	28,025	27,655	28,025	27,655
Accumulated amortisation	(24,295)	(22,676)	(24,295)	(22,676)
Additions	1,423	370	1,423	370
Amortisation	(1,853)	(1,619)	(1,853)	(1,619)
Net book value 30 June 2006	3,300	3,730	3,300	3,730
Cost	29,448	28,025	29,448	28,025
Accumulated amortisation	(26,148)	(24,295)	(26,148)	(24,295)
In line with the adoption of IFRS (IAS 38), software has been reclassified from property, plant and equipment and is now disclosed as an intangible asset.				
The amortisation has been reclassified accordingly out of depreciation on the income statement for both the current year and the prior year. Refer to note 3.				
Total intangible assets	3,300	3,730	3,300	3,730

13. INVESTMENTS - FINANCIAL INSTRUMENTS

13.1. Capital market investments	92,977	413,740	92,977	413,740
Zero-coupon bonds	92,977	365,283	92,977	365,283
Other assets	48,457	48,457	48,457	48,457
Provision for impairment	(48,457)	-	(48,457)	-
13.2. Cash flow analysis of capital market investments	92,977	413,740	92,977	413,740
Capital investments - cost	32,576	197,564	32,576	197,564
Interest and premiums accrued	47,126	128,967	47,126	128,967
Mark-to-market adjustments	13,275	87,209	13,275	87,209
Interest and premiums have been accrued for where biannual coupon bonds and zero-coupon bonds have earned interest, but have not been received at year end.				
Capital market investments comprise investments in local listed bonds with credit ratings from A+ to AAA.				
13.3. Maturity profile:	92,977	413,740	92,977	413,740
1 - 5 years	92,977	118,442	92,977	118,442
6 - 10 years	-	295,298	-	295,298
13.4. Portfolio analysis:	92,977	413,740	92,977	413,740
Long-term investment	92,977	413,740	92,977	413,740
13.5. Fair value	92,977	420,934	92,977	420,934
Total investments - financial instruments	92,977	413,740	92,977	413,740

14. INVESTMENTS - SUBSIDIARIES AND ASSOCIATES

Investments in subsidiaries	-	-	-	-
Investments in associates	5,175	4,084	-	-
Cost	4,594	4,784	-	-
Share of post-acquisition reserves	581	-	-	-
Provision for write-down of investments	-	(700)	-	-
Loans to subsidiaries and associates	-	-	7,309	8,214
Msinsi Holdings (Pty) Ltd	-	-	2,260	4,003
Umgeni Water Services (Pty) Ltd	-	-	4,690	4,211
Associates	-	-	359	-
Total investments - subsidiaries and associates	5,175	4,084	7,309	8,214

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

14. INVESTMENTS - SUBSIDIARIES AND ASSOCIATES (continued)

Name	Principal activity	Place of incorporation	Proportion of ownership interest		Proportion of voting power held	
			2006 %	2005 %	2006 %	2005 %
Investments in subsidiaries						
Umgeni Water Services (Pty) Ltd	Analytical testing services	RSA	100%	100%	100%	100%
Msinsi Holdings (Pty) Ltd	Land and environmental management	RSA	100%	100%	100%	100%
Investments in special purpose entity						
Umgeni Water Share Incentive Trust	Employee retention	RSA	-	100%	-	100%

Both subsidiaries remained subsidiaries throughout the year.

The special purpose entity was wound up during the financial year.

Umgeni Water has subordinated its right to claim payment of debt of R10.6m (2005:R11.4m) owing by Umgeni Water Services (Pty) Ltd until the assets, fairly valued, exceed the liabilities.

Name of associates	Principal activity	Place of incorporation	Proportion of ownership interest		Proportion of voting power held	
			2006 %	2005 %	2006 %	2005 %
Investments in associates of Umgeni Water Services (Pty) Ltd						
Turngro Water Services (Pty) Ltd	Water treatment products	RSA	50%	50%	50%	50%
Watertite (Pty) Ltd	Water restriction technology	RSA	26%	26%	50%	50%
Durban Water Recycling (Pty) Ltd	Water recycling	RSA	18.5%	18.5%	18.5%	18.5%
Investment in associate of Msinsi Holdings (Pty) Ltd						
Powaprops 31 (Pty) Ltd	Investment	RSA	16.67%	16.67%	16.67%	16.67%

Investments in associates of Umgeni Water Services (Pty) Ltd	Carrying amount		Directors' valuation		Loans to (from)	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000	2006 R'000	2005 R'000
Turngro Water Services (Pty) Ltd	359	-	359	-	-	-
Watertite (Pty) Ltd	-	-	-	-	-	-
Durban Water Recycling (Pty) Ltd	4,711	3,979	4,711	3,979	-	-
Investments in associates of Msinsi Holdings (Pty) Ltd						
Powaprops 31 (Pty) Ltd	105	105	105	105	-	-
Net Investment	5,175	4,084	5,175	4,084	-	-

Summarised financial information of associates:	2006 R'000	2005 R'000
Total non-current assets of associates	10,002	10,547
Total non-current liabilities of associates	10,014	9,614
Total current assets of associates	5,461	4,424
Total current liabilities of associates	895	1,537
Total capital and reserves	4,554	3,820
Total revenue of associates	7,026	7,003
Net profit for the year of associates	1,272	1,113

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
15. OTHER NON-CURRENT ASSETS				
15.1. Reticulation financial asset	326,949	-	326,949	-
Transferred from property, plant and equipment	369,942	-	369,942	-
Amortisation	(91,613)	-	(91,613)	-
Interest income	48,620	-	48,620	-
15.2. Long-term loans to municipalities	1,540	3,334	1,540	3,334
Carrying amount	2,771	4,872	2,771	4,872
Recognised as short-term portion	(1,231)	(1,538)	(1,231)	(1,538)
Settlement of the above loan is over 60 months without interest				
15.3. Biological assets	7,294	-	2,495	-
Additions - plantation	1,540	-	1,540	-
Fair value adjustment for the year - plantation	955	-	955	-
Fair value adjustment for the year - game stock	4,799	-	-	-
15.4. Fair value	335,783	3,334	330,984	3,334
Total other non-current assets	335,783	3,334	330,984	3,334
16. CURRENT INVESTMENTS				
16.1. Current investments	268,208	916,315	268,208	916,315
Money market investments	190,000	810,498	190,000	810,498
Other investments	78,208	105,817	78,208	105,817
16.2. Maturity profile	268,208	906,815	268,208	906,815
Overnight	268,208	109,896	268,208	109,896
1 to 7 days	-	-	-	-
8 to 30 days	-	-	-	-
31 to 180 days	-	777,395	-	777,395
181 to 365 days	-	19,524	-	19,524
16.3. Portfolio analysis	268,208	912,237	268,208	912,237
Current portion of long-term investment	-	32,922	-	32,922
Current portion of redemption portfolio	-	773,498	-	773,498
Other	268,208	105,817	268,208	105,817
16.4. Fair value	268,208	921,693	268,208	921,693
Total current investments	268,208	916,315	268,208	916,315
17. INVENTORIES				
Pipe inventories	459	1,652	459	1,652
Maintenance spares	2,443	2,605	2,443	2,605
Chemicals	1,990	1,815	1,990	1,815
Miscellaneous	2,048	2,099	1,978	2,040
Total inventories	6,940	8,171	6,870	8,112

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
18. TRADE AND OTHER RECEIVABLES				
Trade debtors	151,198	133,564	151,043	133,107
Sundry debtors	5,717	6,525	5,537	6,525
Less: provision for doubtful debts	(39,464)	(14,376)	(39,393)	(14,376)
Opening Balance	(14,376)	(19,384)	(14,376)	(19,324)
Utilised during the year	18	12,152	18	12,152
Provided for during the year (see note 7).	(25,106)	(7,144)	(25,035)	(7,204)
Trade debtors comprise bulk water and waste water sales to a widespread customer base of which eThekweni Municipality and Msunduzi - Pietermaritzburg Local Municipality comprise a significant proportion - 94.1% (2005: 94.6%) of sales.				
Trade debtors are granted credit terms of 30 days from date of invoice to settle outstanding debts. The average credit period, at financial year-end, is 44.6 days (2005: 39.1 days).				
Interest is charged on outstanding accounts at the prevailing prime interest rate.				
Credit risk related to debtors is monitored on a monthly basis and is adequately provided for. The directors are of the opinion that trade and other receivables approximate their fair value.				
Total trade and other receivables	117,451	125,713	117,187	125,256
19. INTEREST AND PREMIUM RECEIVABLE				
Interest and premiums have been accrued for where biannual coupon bonds and zero-coupon bonds have earned interest, but have not been received at year-end.				
Interest and premium receivable relating to current investments	1,335	301	1,335	301
Total interest and premium receivable	1,335	301	1,335	301
20. BANK AND CASH				
Cash and cash equivalents consist of:				
Bank and cash on hand	13,429	6,239	12,321	4,600
The balance comprises cash held by the group. The carrying amount of these assets approximate their fair value.				
The group's outstanding guarantees are disclosed under note 29.				
Total bank and cash	13,429	6,239	12,321	4,600
21. CAPITAL				
Capital consists primarily of contributions made by the Department of Water Affairs and Forestry.	442,847	442,847	442,847	442,847
Total capital	442,847	442,847	442,847	442,847

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
22. LONG-TERM LIABILITIES				
22.1 Capital market liabilities				
Long-term interest-bearing debt consists of:	2,168,572	2,140,595	2,168,572	2,140,595
Locally registered stock including finance leases	2,384,984	3,378,475	2,384,984	3,378,475
Loan discount - long term	(86,156)	(132,701)	(86,156)	(132,701)
Less: nominal amounts due within 12 months (see note 26)	(130,256)	(1,105,179)	(130,256)	(1,105,179)
- Net amount	(113,030)	(1,084,396)	(113,030)	(1,084,396)
- Loan discount - short-term	(17,226)	(20,783)	(17,226)	(20,783)
22.2 Maturity profile	2,168,572	2,140,595	2,168,572	2,140,595
1 - 5 years	1,407,070	1,508,886	1,407,070	1,508,886
6 - 10 years	558,145	380,997	558,145	380,997
> 10 years	203,357	250,712	203,357	250,712
22.3 Nominal value reconciliation	2,168,572	2,140,595	2,168,572	2,140,595
Individual loan stock - as per annexure 1	2,237,502	2,252,513	2,237,502	2,252,513
Loan discount	(68,930)	(111,918)	(68,930)	(111,918)
22.4 Fair value	2,356,384	2,668,566	2,356,384	2,668,566
Interest rates for the loans are disclosed in annexure 1 and 2.				
Umgeni Water has a financial structure that underlies loan 56 and in terms of the final settlement thereof, it has made a deposit with and ceded it in favour of Rand Merchant Bank, for future settlement and with right of set-off against an equal liability. Accordingly these assets and liabilities have been offset and are not reflected in the annual financial statements.				
Total long-term liabilities	2,168,572	2,140,595	2,168,572	2,140,595

Borrowing limits

Umgeni Water has the following approval from the Minister of Water Affairs and Forestry and the Minister of Finance:

Approved	3,500,000	5,200,000
Utilised on 30 June	(2,372,504)	(3,489,038)
- long-term liabilities (refer annexure 1)	(2,237,502)	(2,252,513)
- short-term funding (refer annexure 2)	(133,416)	(1,235,179)
- collateral and guarantees (refer note 29)	(1,586)	(1,346)
Unutilised borrowing limits	1,127,496	1,710,962

Liquidity risk:

This is the risk that the organisation could encounter difficulty in raising funds to meet its commitments.

Liquidity risk is minimised through the use of:

- a redemption portfolio to meet the UG65 maturity in June 2010;
- short-term funding facilities to meet ongoing cash requirements; and
- actively seeking longer dated debt to minimise the risks inherent in utilising short-term debt.

Credit risk:

This is the risk of the organisation being exposed to counter-party failure.

This risk is minimised as follows:

- Transactions are conducted only with counter-parties, and issuers who satisfy soundly based, and acceptable, assessment processes, and only after formal limits have been set;
- Credit limits are set for individual legal entities in terms of predetermined Credit Limit Guidelines;
- Where available and credible, formal credit ratings are utilised in the credit evaluation process;
- In order to reduce credit risk further, same day settlement limits are set wherever possible. In addition strict settlement procedures are set and adhered to. This especially applies for counterparties not registered as financial institutions; and
- Continued monitoring of the credit quality of counterparties is essential. A rating review takes place at least annually.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

22. LONG-TERM LIABILITIES (continued)

Interest rate risk:

This is the risk that adverse changes in interest rates will have a negative impact on net income.

Umgeni Water's interest rate risk is concentrated in its UG65 bond, and is most prevalent on maturity in 2010, when replacement debt will need to be raised.

This risk is minimised by:

- Raising longer-term finance;
- Only utilising rand-denominated debt; and
- Utilising appropriate interest rate hedging instruments.

Interest rate exposures

Umgeni Water's optimal debt structure is 70% fixed to 30% floating interest rate.

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
23. OTHER NON-CURRENT LIABILITIES				
Retirement benefit - medical aid	76,373	68,945	76,373	68,945
Opening balance	68,945	44,354	68,945	44,354
Provided for during the year	9,431	26,474	9,431	26,474
Utilised during the year	(2,003)	(1,883)	(2,003)	(1,883)
The retirement benefit medical aid is the value of the past service liabilities at financial year end and is based on an actuarial valuation. (Refer to note 30.3 for additional information)				
Retirement benefit - defined benefit plan				
Provision against under funded position (Refer to note 30.2 for additional information)	21,543	11,120	21,543	11,120
Total other non-current liabilities	97,916	80,065	97,916	80,065
24. ACCOUNTS PAYABLE				
Accounts payable	88,373	89,620	86,171	108,996
Accruals	66,476	78,319	66,476	78,319
Accounts payable comprise amounts outstanding for trade purchases and ongoing costs.				
The Board consider that the carrying amount of trade and other payables approximate their fair value.				
Total accounts payable	154,849	167,939	152,647	187,315

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

25. PROVISIONS	Leave pay R'000	Legal fees R'000	Bonus R'000	Other R'000	Total 2006 R'000	Total 2005 R'000
Group						
Opening balance	14,006	-	11,840	1,184	27,030	20,720
Provided for during the year	2,344	6,145	7,179	(92)	15,576	20,173
Utilised during the year	(1,319)	-	(11,248)	(670)	(13,237)	(13,863)
Closing balance	15,031	6,145	7,771	422	29,369	27,030
Parent						
Opening balance	13,226	-	11,840	767	25,833	19,295
Provided for during the year	2,253	6,145	7,179	(97)	15,480	20,173
Utilised during the year	(1,319)	-	(11,248)	(670)	(13,237)	(13,635)
Closing balance	14,160	6,145	7,771	-	28,076	25,833

The leave pay provision is based on the number of days leave due to employees at financial year end times their cost to company per day.

The provision for bonus is raised to recognise the performance bonus provision, which is payable at the boards discretion in line with the Performance Management Scheme.

Legal fees are raised to the extent that it is probable Umgeni Water will be required to honour obligations.

All provisions are raised in the ordinary course of business and no material unutilised provisions were written back.

26. SHORT-TERM FUNDING	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
Short-term interest bearing debt consist of:	116,190	1,214,396	116,190	1,214,396
Term deals	-	80,000	-	80,000
Call funding	3,160	50,000	3,160	50,000
Current portion of long-term liabilities	113,030	1,084,396	113,030	1,084,396
Nominal value reconciliation	116,190	1,214,396	116,190	1,214,396
Individual loan stock - as per annexure 2	133,416	1,235,179	133,416	1,235,179
Current portion of loan discount (see note 22 above)	(17,226)	(20,783)	(17,226)	(20,783)
Fair value	151,692	1,274,552	151,692	1,274,552
Total short-term funding	116,190	1,214,396	116,190	1,214,396

27. CAPITAL COMMITMENTS

Commitments in respect of capital expenditure				
- contracted for but not provided for in the annual financial statements	65,122	41,292	63,733	41,292
- authorised but not contracted for	173,763	228,659	170,051	228,659
The proposed capital expenditure will be financed through internally generated funds.				
The expenditure is substantially for the augmentation and upgrades to pipelines				
Total capital commitments	238,885	269,951	233,784	269,951

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
28. OPERATING LEASE ARRANGEMENTS				
At the balance sheet date, the group had no outstanding commitments under non-cancellable operating leases.				
The group as the lessor - rental income				
The group owns a number of properties from which rental income of R2.0m (2005: R1.7m) is earned.				
At the balance sheet date, the group had contracted with tenants for the following future minimum lease payments.				
0 - 1 year	507	261	507	261
1 - 5 years	343	206	343	206
> 5 years	164	55	164	55
	-	-	-	-
Total operating lease arrangements	507	261	507	261
29. CONTINGENT LIABILITIES				
Collateral				
Collateral security has been given to certain financial institutions in respect of mortgage loans advanced to employees under the home ownership scheme.	920	680	920	680
Guarantees				
Guarantees have been given by certain financial institutions in respect of payments to utility service providers.	666	666	666	666
Total contingent liabilities	1,586	1,346	1,586	1,346
30. RETIREMENT BENEFIT PLANS				
All the Umgeni Water retirement benefit plans are governed by the Pension Funds Act No. 24 of 1956. All full-time employees are compelled to belong to either the defined benefit or the defined contribution plan.				
30.1 Defined contribution plan				
The total cost charged to income represents the group's portion of the contribution payable to this scheme. At reporting date all amounts due and payable to this scheme had been paid.	4,541	3,075	3,488	3,075
30.2 Defined benefit plan				
The scheme is actuarially valued at three-year intervals. The effective date of the most recent valuation is 30 June 2006.				
The amount included in the balance sheet arising from Umgeni Water's obligation in respect of the defined benefit plan is as follows:				
The net under funded position of the plan at financial year-end is as follows and is based on the actuarial valuations done on 30 June 2006:				
Defined benefit obligation			300,620	189,429
Assets at fair value			(195,782)	(184,101)
Under funded status			104,838	5,328
Unrecognised actuarial losses			(83,295)	5,792
Net liability			21,543	11,120

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

	Group		Parent	
	2006 R'000	2005 R'000	2006 R'000	2005 R'000
30. RETIREMENT BENEFIT PLANS (continued)				
30.2 Defined benefit plan (continued)				
Current service cost			18,977	18,054
Interest on obligation			17,037	15,777
Expected return on plan assets			(14,728)	(13,577)
Total included in staff costs			21,286	20,254
Movement in the net liability recognised in the balance sheet are as follows:				
Net liability at start of year			11,120	2,400
Net expense recognised in the income statement			21,286	20,254
Company contributions			(10,863)	(11,534)
Net liability at end of year			21,543	11,120
Key assumptions used in the actuarial valuation:				
Discount rate			9.0%	8.5%
Expected return on plan assets			10.0%	8.5%
Expected rate of salary increases			6.75%	5.5%
Future pension increase			3.83%	2.67%
30.3 Retirement medical aid				
During the financial year, the group recognised its full past service liability and reflected this in other non-current liabilities (see note 23).				
Employees who joined Umgeni Water after 28 February 2002 can not elect to join this scheme.				
The movement in the reserve is as follows				
Opening balance			68,945	44,354
Actual contributions paid			(2,003)	(1,883)
Charged to the income statement			9,431	26,474
			76,373	68,945
Key assumptions used in the actuarial valuation performed on 31 December 2004:				
Discount rate			9.5%	9.5%
Expected rate of increase in medical indices			7.5%	7.5%
The year of the next actuarial valuation is 31 December 2007.				

31. RELATED PARTIES

Umgeni Water, its subsidiaries and other public entities enter into various sale, purchase and service transactions in the ordinary course of business. Material related party transactions are as follows:

Trading transactions

Management fee paid to Msinsi	-	-	13,595	12,096
Interest charged on Msinsi Holdings	-	-	216	396
Purchases from Msinsi Holdings	-	-	1,612	1,063
Management fee paid to TCTA	385	2,000	385	2,000
Raw water purchases from DWAF	69,318	65,509	69,318	65,509

Compensation of key management personnel

Compensation of directors and other members of key management personnel during the year is reflected under note 33.

The remuneration of directors and key executives is determined by the remuneration committee having regards to the performance of the individuals and market trends.

32. FINANCIAL REPORT

Included in the Financial Report is the information required in terms of the 4th schedule of the Companies Act No 61 of 1973 as well as Umgeni Water's approach to financial risk management, fraud and error.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (continued)

For the year ended 30 June 2006

33. DIRECTORS AND EXECUTIVE MANAGEMENT EMOLUMENTS

	2006 R'000 Fees for services	2006 R'000 Basic salary	2006 R'000 Bonuses	2006 R'000 Expense allowances	2006 R'000 Other benefits	2006 R'000 Pension contributions	2006 R'000 Total	2005 R'000 Total
Non-executive board members								
Mr NA Gasa (Chair) ^{N1}	208	-	-	6	-	-	214	38
Mr V Gounden (Vice Chair)	71	-	-	3	-	-	74	35
Ms N Afolayan	119	-	-	5	-	-	124	58
Mr SM Dlamini	78	-	-	5	-	-	83	49
Mr JS de Kock	7	-	-	-	-	-	7	45
Dr R Makote ^{N1,2}	9	-	-	-	-	-	9	-
Ms TC Shezi ^{N2}	71	-	-	3	-	-	74	-
Mr NJ Dlamini ^{N2}	106	-	-	11	-	-	117	-
Mr BB Mathebula ^{N2}	81	-	-	1	-	-	82	-
Mr ZJ Dube ^{N2}	98	-	-	5	-	-	103	-
Mr NA Macleod ^{N2}	65	-	-	-	-	-	65	-
Ms R Manning ^{N2}	73	-	-	2	-	-	75	-
Ms RM Lesoma	97	-	-	4	-	-	101	55
Mr MH Buthelezi ^{N2}	94	-	-	4	-	-	98	-
Ms J Armstrong ^{N2}	97	-	-	2	-	-	99	-
Ms N Medupe ^{N2}	83	-	-	1	-	-	84	-
Mr M Fitzsimons ^{N3}	-	-	-	-	-	-	-	69
Mr PN Ngcobo ^{N3}	-	-	-	-	-	-	-	55
Prof. O Latiff ^{N3}	-	-	-	-	-	-	-	40
Mr GM Anderson ^{N3}	-	-	-	-	-	-	-	96
Mr WJ Barnsley ^{N3}	-	-	-	-	-	-	-	125
Ms NR Bhengu ^{N3}	-	-	-	-	-	-	-	77
Mr S Meyiwa	-	-	-	-	-	-	-	66
Mr EB Bizzell (Deceased 2005)	-	-	-	-	-	-	-	36
Total non-executive board members	1,357	-	-	52	-	-	1,409	844
Executive board member								
Ms G Moloi (CEO) ^{N4}	-	518	255	161	158	139	1,231	1,390
Total - parent	1,357	518	255	213	158	139	2,640	2,234
Msinsi Holdings (Pty) Ltd								
Total non-executive board members	23	-	-	-	-	-	23	-
Mr T Moyo (MD) ^{N6}	-	454	37	122	46	77	736	827
Total - subsidiaries	23	454	37	122	46	77	759	827
Total - Group	1,380	972	292	335	204	216	3,399	3,061
Exco members								
Ms P Maposhe ^{N5}	-	476	141	75	9	78	779	1,030
Mr P Jonas	-	655	142	117	33	112	1,059	982
Mr M Msiwa (act.CEO) ^{N4}	-	693	141	142	24	117	1,117	1,068
Ms M Gevers	-	732	150	144	-	119	1,145	1,023
Ms M Venter-Hillebrand	-	-	-	-	-	-	-	951
Total - Exco	-	2,556	574	478	66	426	4,100	5,054

There are no share option schemes within the group.

^{N1} Dr R Mokate resigned from the board on 27 July 2005 and was replaced as the Chair by Mr NA Gasa, the effective date was 1 August 2005.

^{N2} Appointed 1 July 2005.

^{N3} Retirement due to expiry of term - 30 June 2005.

^{N4} Ms Moloi's resignation was effective from 31 March 2006, and Mr Msiwa was the Acting CEO from 1 April 2006, and was appointed CEO on 1 September 2006.

^{N5} Resigned 31 January 2006.

^{N6} Resigned 18 August 2006.

ANNEXURES 1 AND 2 - SCHEDULES OF LIABILITIES

ANNEXURE 1 : LONG-TERM LIABILITIES

Loan	Fixed or floating interest rate	Authorised nominal value	NACM 2006	NACM 2005	Year of maturity	Issued nominal value 2006	Issued nominal value 2005
		R'000	%	%		R'000	R'000
27	Fixed	39,939	14.55	14.55	2012	25,269	28,076
30	Fixed	5,214	16.52	16.52	2013	3,336	3,638
37	Fixed	4,006	16.80	16.80	2009	1,416	1,837
47	Fixed	33,665	9.80	9.80	2017	25,654	27,023
54	Fixed	200,000	11.60	18.28	2013	71,869	82,915
56	Fixed	200,000	12.44	12.44	2014	16,229	16,229
65	Fixed	1,900,000	15.50	15.50	2010	1,003,262	1,303,262
71 Sub 1 and 2	Floating	750,000	8.83	9.11	2019	600,000	650,000
71 Sub 3	Fixed	161,000	10.95	10.95	2019	128,800	139,533
72	Fixed	50,000	4.95		2021	46,667	-
73	Fixed	350,000	8.16		2016	315,000	-
Total issued nominal value						2,237,502	2,252,513

ANNEXURE 2 : SHORT-TERM FUNDING

Loan	Fixed or floating interest rate	Authorised nominal value	NACM 2006	NACM 2005	Year of maturity	Issued nominal value 2006	Issued nominal value 2005
		R'000	%	%		R'000	R'000
1	Fixed	7,209	6.73	6.73	2005	-	711
27	Fixed	39,939	14.55	14.55	2012	2,807	2,429
30	Fixed	5,214	16.52	16.52	2013	301	256
37	Fixed	4,006	16.80	16.80	2009	421	356
47	Fixed	33,665	9.80	9.80	2017	1,369	1,273
54	Fixed	200,000	11.60	18.28	2013	26,292	18,507
55	Fixed	1,600,000	14.70	15.20	2005	-	834,843
56	Fixed	200,000	12.44	12.44	2014	-	36,071
70	Fixed	150,000	10.16	10.25	2006	-	150,000
71 Sub 1 and 2	Floating	750,000	8.83	9.11	2019	50,000	50,000
71 Sub 3	Fixed	161,000	10.95	10.95	2019	10,733	10,733
72	Fixed	50,000	4.95		2021	3,333	-
73	Fixed	350,000	8.16		2016	35,000	-
Call liabilities	Floating					3,160	50,000
Term deals	Floating					-	80,000
Total issued nominal value						133,416	1,235,179

NOTE:

- There are no outstanding interest commitments with regard to the above loans.
- Loan 71 has three sub-loans, the first two were drawn as floating-rate loans, the third as a fixed-rate loan. This is in line with Umgeni Water's optimal debt structure.
- Loan 72 and 73 were raised during the current financial year and both are fixed interest rate amortising loans.

FIVE-YEAR FINANCIAL REVIEW

	2006	2005	2004	2003	2002
	R'000	Restated R'000	R'000	R'000	R'000
Financial position					
Capital and reserves	390,171	327,661	288,698	362,351	337,365
Net interest-bearing debt	1,923,577	2,024,936	2,340,278	2,460,308	2,338,110
Assets - excluding financial assets	2,635,891	2,698,718	2,843,735	2,976,044	2,946,341
Operations					
Revenue	1,084,544	1,008,352	912,895	835,586	745,632
Cost of sales	(112,825)	(96,656)	(82,516)	(69,579)	(62,686)
Other income	26,057	8,137	630	877	(2,317)
Operating and administration expenses	(575,832)	(530,581)	(397,396)	(440,549)	(378,397)
Profit from operations	421,944	389,252	433,613	326,335	302,232
Net finance costs	(283,741)	(346,469)	(470,674)	(399,214)	(326,997)
Profit (loss) before taxation	138,203	42,783	(37,061)	(72,879)	(24,765)
Taxation	(640)	(2,175)	(125)	1,005	-
Profit (loss) for the year	137,563	40,608	(37,186)	(71,874)	(24,765)

Cash flow

Net cash from operating activities	644,654	630,412	536,908	401,827	421,910
Net cash (used in) from investing activities	(80,645)	(4,834)	54,601	(96,106)	(118,749)
Net cash generated	564,009	625,578	591,509	305,721	303,161
Net cash used in financing activities	(556,819)	(625,560)	(592,015)	(317,441)	(314,006)
Net (decrease) increase for the year	(7,190)	(18)	506	11,720	10,845
Net cash utilised	(564,009)	(625,578)	(591,509)	(305,721)	(303,161)

	2006	2005	2004	2003	2002	Annual trend growth rate 5-year average	2006-2005 Growth rate
Financial indicators/ratios							
Water sold (ML)	361,438	352,634	340,190	329,370	315,370	2.52%	2.50%
Total gross income (R'000)	1,084,544	1,008,352	912,895	835,586	745,632	11.25%	7.56%
Bulk water tariff (R'000/ML)	2.698	2.579	2.442	2.261	2.112	8.47%	4.63%
Operating indicators/ratios							
Profit from operations (R'000/ML sold)	1.167	1.104	1.273	0.988	0.958	14.87%	5.71%
Total expenditure (R'000/ML sold)	2.690	2.761	2.792	2.789	2.443	0.42%	-2.57%
Operating costs (R'000/ML sold)	1.593	1.505	1.168	1.338	1.200	13.34%	5.85%
Cost of sales (R'000/ML sold)	0.312	0.274	0.243	0.211	0.199	-1.11%	13.87%
Net finance costs (R'000/ML sold)	0.785	0.983	1.384	1.212	1.037	-4.42%	-20.14%
Personnel costs							
Manpower (R'000/ML sold)	0.599	0.671	0.524	0.553	0.433	9.29%	-10.73%
Training and development (R'000/ML sold)	0.024	0.019	0.011	0.019	0.019	12.50%	26.32%
Personnel (ML sold per employee)	398	391	380	286	274	9.46%	1.82%
Number of employees as at year-end	908	902	896	937	1,150	-5.60%	0.67%
Ratios							
Working ratio	0.489	0.536	0.526	0.611	0.592	-5.97%	-8.77%
Rate of return on assets	16.01%	14.42%	15.90%	11.43%	10.26%	21.11%	11.11%
Gross profit margin ratio	89.60%	90.41%	90.96%	91.67%	91.59%	2.96%	-0.88%
Current ratio	1.197	0.714	0.896	0.747	0.807	23.87%	67.65%
Debt-service ratio (interest cover)	1.487	1.123	0.920	0.815	0.924	22.38%	32.41%
Net debt-equity ratio	4.930	6.180	8.457	6.947	6.180	24.74%	-20.23%
Trade debtors collection period (days)	44.636	42.410	39.139	39.100	48.863	1.83%	5.25%
Trade debtors collection period after provision (days)	32.986	37.845	32.341	35.934	38.158	1.79%	-12.84%
Net debt to asset ratio	0.730	0.750	0.823	0.827	0.794	1.81%	-2.67%

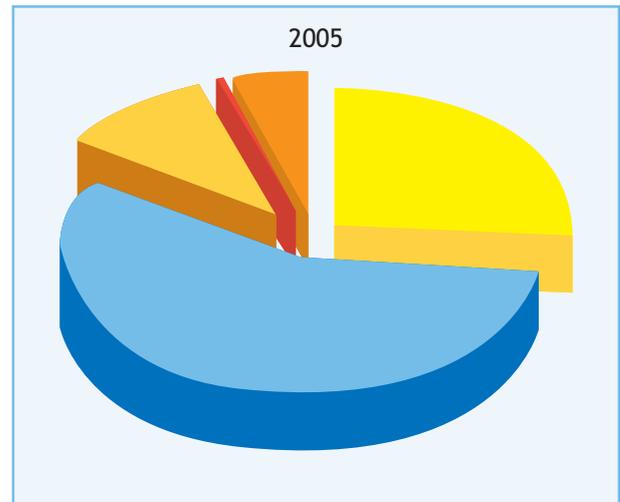
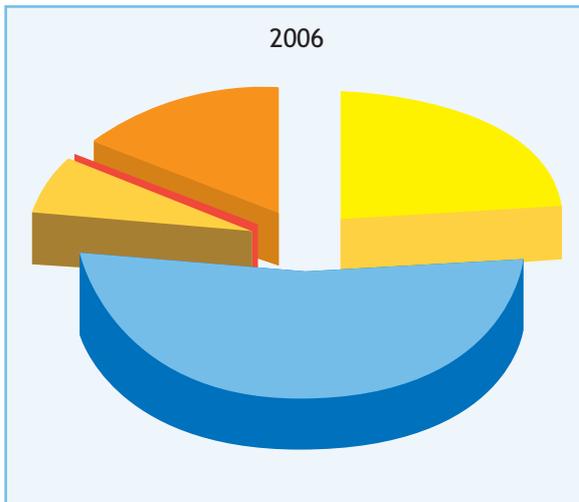
Definitions of ratios

Working ratio	Operating costs, exclusive of depreciation and amortisation, divided by operating revenue.
Rate return on assets	Profit from operations divided by total property, plant and equipment.
Current ratio	Current assets divided by current liabilities.
Debt-service ratio (interest cover)	Profit from operations divided by net finance costs.
Net debt-equity ratio	Net interest-bearing debt divided by capital and reserves.
Net debt to asset ratio	Net interest-bearing debt divided by fixed assets.

VALUE-ADDED STATEMENT

	2006	2005
	R'000	Restated R'000
Gross revenue	1,084,544	1,008,352
Paid to suppliers for materials & services	(387,158)	(321,065)
Value added	697,386	687,287
Interest income	190,165	121,618
Total wealth created	887,551	808,905

Salaries, wages and other benefits	210,497	213,176
Providers of capital	473,906	468,087
Depreciation	64,945	84,859
South Africa Revenue Services	640	2,175
Profit for the year	137,563	40,608
Total wealth distributed	887,551	808,905



ACRONYMS

ABET	Adult Basic Education and Training
AEP	Assisted Education Programme
ASGISA	Accelerated and Shared Growth Initiative for South Africa
BEE	Black Economic Empowerment
CAPEX	Capital Expenditure
CEO	Chief Executive Officer
CIDB	Construction Industry Development Board
CPIX	Consumer Price Index
CPLD	Certificate Programme in Leadership Development
CSI	Corporate Social Investment
DLGTA	Department of Local Government and Traditional Affairs
DBSA	Development Bank of Southern Africa
DPLG	Department of Provincial and Local Government
DWAF	Department of Water Affairs and Forestry
EIA	Environmental Impact Assessment
EXCO	Executive Management Committee
GDP	Gross Domestic Product
GM	General Manager
GRI	Global Reporting Initiative
IAS	International Accounting Standards
IDP	Integrated Development Planning
IFRS	International Financial Reporting Standards
ISO	International Organisation for Standardisation
KZN	KwaZulu-Natal
MOU	Memorandum of Understanding
NEHAWU	National Education and Allied Worker's Union
NEMA	National Environmental Management Act
NOSA	National Occupational Safety Association
NQF	National Qualification Framework
NTU	Nephelometric Turbidity Unit
OHASA	Occupational Health and Safety Act
PFMA	Public Finance Management Act 1 of 1999
RAWSP	Rural Water and Sanitation Plan
SAAWU	South African Association of Water Utilities
SABS	South African Bureau of Standards
SALGA	South African Local Government Association
SANS	South African National Standard
SCA	South Coast Augmentation
SCM	Supply Chain Management
SCP	South Coast Bulk Pipeline
SETA	Sector Education and Training Authority
SHEQ	Safety, Health, Environment and Quality
WISA	Water Institute of Southern Africa
WSA	Water Service Authority
WSDP	Water Services Development Plan
WW	Water Works
WWW	Wastewater Works

Further copies of this report are available on request from:
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