



Statement of Corporate Intent
For the three-year period commencing 1 July 2010



Watercare Services Limited

STATEMENT OF CORPORATE INTENT

FOR THE THREE YEAR PERIOD COMMENCING 1 JULY 2010

1. INTRODUCTION

Watercare Services Limited (Watercare) is required to prepare and deliver to its shareholders, no later than 30 June in each year, a Statement of Corporate Intent (SCI) for the three year period commencing 1 July.

The SCI is the public and legislative expression of Watercare's accountability to its shareholders. It is the contract between Watercare's Board of Directors and its shareholders, and it is against this document that the Board reports to the shareholders and is held accountable. The SCI identifies the nature of Watercare's business and its strategic and operational issues. It sets the expectations of Watercare by the shareholders, and provides a tangible record of Watercare's performance by setting performance targets against which the Company must report.

Integration of the Auckland Water and Wastewater Services Industry

The Auckland region is currently planning for Governance changes that will create a single Auckland Council resulting in the reorganisation of major local government services. On 1 November 2010 Watercare will replace the existing Local Network Operators (LNOs) and Council business units and become the integrated water and wastewater service provider for the region. The exception will be United Water which will manage the local networks and retailing under a franchise agreement while Watercare owns the assets and the franchise.

The timing of integration means that this SCI, as relevant to Watercare's existing operations and its current shareholders, will only cover a four month period from 1 July to 31 October 2010. For the remaining eight months to 30 June 2011 the company will have a new Shareholder, the Auckland Council. For practical reasons over the transition period, the existing Shareholders and the Auckland Transition Agency have agreed to Watercare basing the 2010 SCI on the existing SCI, with minor amendments to performance measures to reflect Watercare's responsibilities as the integrated operator from 1 November 2010.

In order to assess performance of the integrated business, retail performance measures have been included which are consistent with those currently used by the Local Network Operators. Reporting against these new measures will become effective from 1 November 2010 following integration.

Watercare will continue to submit quarterly performance reports to the Shareholder Representative Group until 31 October 2010 at which time the reports will be sent to the Auckland Council. Reporting against the current SCI will continue until a new Statement of Intent is agreed with the Auckland Council which is likely to take place in early 2011 and become effective from 1 July 2011.

2. BUSINESS PURPOSE

Watercare provides the majority of bulk water supply and wastewater services to the LNOs who then retail these services to the customers of the Auckland region. From 1 November 2010 the company will assume responsibility for the full range of regional water and wastewater services having absorbed the ownership and management of local networks and the retail functions from the LNOs.

Vision ^{note 1}

To continually strive for smart solutions that deliver high quality, reliable and efficient water and wastewater services to our customers while keeping our minimum price commitment.

This vision requires that Watercare:

- is a utility which prides itself on the quality of service delivered to its customers.
- balances investment with impact on pricing to ensure value for our customer's money.
- is a socially responsible company committed to meeting the public health, environmental and affordability needs of the community.

Values

Watercare's previous values of economic viability, sustainability, social responsibility and customer responsiveness remain inherent in the company's vision. However, new values have been developed that better reflect the types of behaviour and culture the company requires to deliver high quality services. These are:

Respectful We encourage our people to challenge each other and hold each other to account, but this must be done in a positive way. Similarly, we encourage each other to accept challenge positively. Respect does not require us to avoid the issues, but to deal with them in a fair and reasonable manner. Respect also applies to our relationships with our stakeholders, especially our customers and shareholder.

Efficient We recognise that our customers pay for our services without having a choice of alternative supplier. It is therefore essential that we spend their money wisely and are efficient in all our operations. We reward employees who find new efficient ways of achieving our business objectives.

Achieving Our Company has set itself high standards of performance in line with the expectations of our shareholder and the community. Our people need to be focussed on outputs, goals and targets. We reward people for achievement, encouraging them to be innovative so that the Company improves its performance.

Customer-focussed We recognise that our customers deserve a high quality, responsive service. We expect our people to place high priority on service delivery and meeting customers' needs. We do not allow our monopoly position to cause us to be slow and unresponsive and we

¹ Watercare is currently reviewing its Strategic Plan, including the vision and values, in preparation for integration and therefore the information presented may be subject to change.

recognise that it is part of our corporate social responsibility to deliver for the people we serve.

Honest We are transparent and ethical in all our business practices. We speak the truth to each other, our shareholder, our customers and community. We do not avoid difficult conversations but deal with things in an open and honest way. We encourage our people to speak the truth, not to cover up problems.

Commitment to Sustainability

Watercare has consistently recognised its responsibilities as a corporation and maintained a strong and consistent commitment to sustainability which goes beyond the specific legislative requirement of managing "...its business efficiently with a view to maintaining prices ...at minimum levels consistent with the effective conduct of that business and the maintenance of the long term integrity of its assets."

To limit disruption and maintain some continuity over the integration period, the 2010 SCI performance measures and reporting will continue to be structured around the six sustainability policies;

- *ENVIRONMENTAL CARE*: To minimise the adverse impact of the company's operations on the environment.
- *HEALTH, SAFETY and WELL-BEING*: To be an industry-best workplace.
- *STAKEHOLDER RELATIONSHIPS*: To be responsive to stakeholder requirements.
- *CUSTOMER SERVICE COMMITMENT*: To provide high quality products and meet customer service level requirements.
- *ASSET MANAGEMENT*: To manage and maintain the long-term integrity of assets.
- *ECONOMIC PERFORMANCE*: To manage the business efficiently at minimum prices.

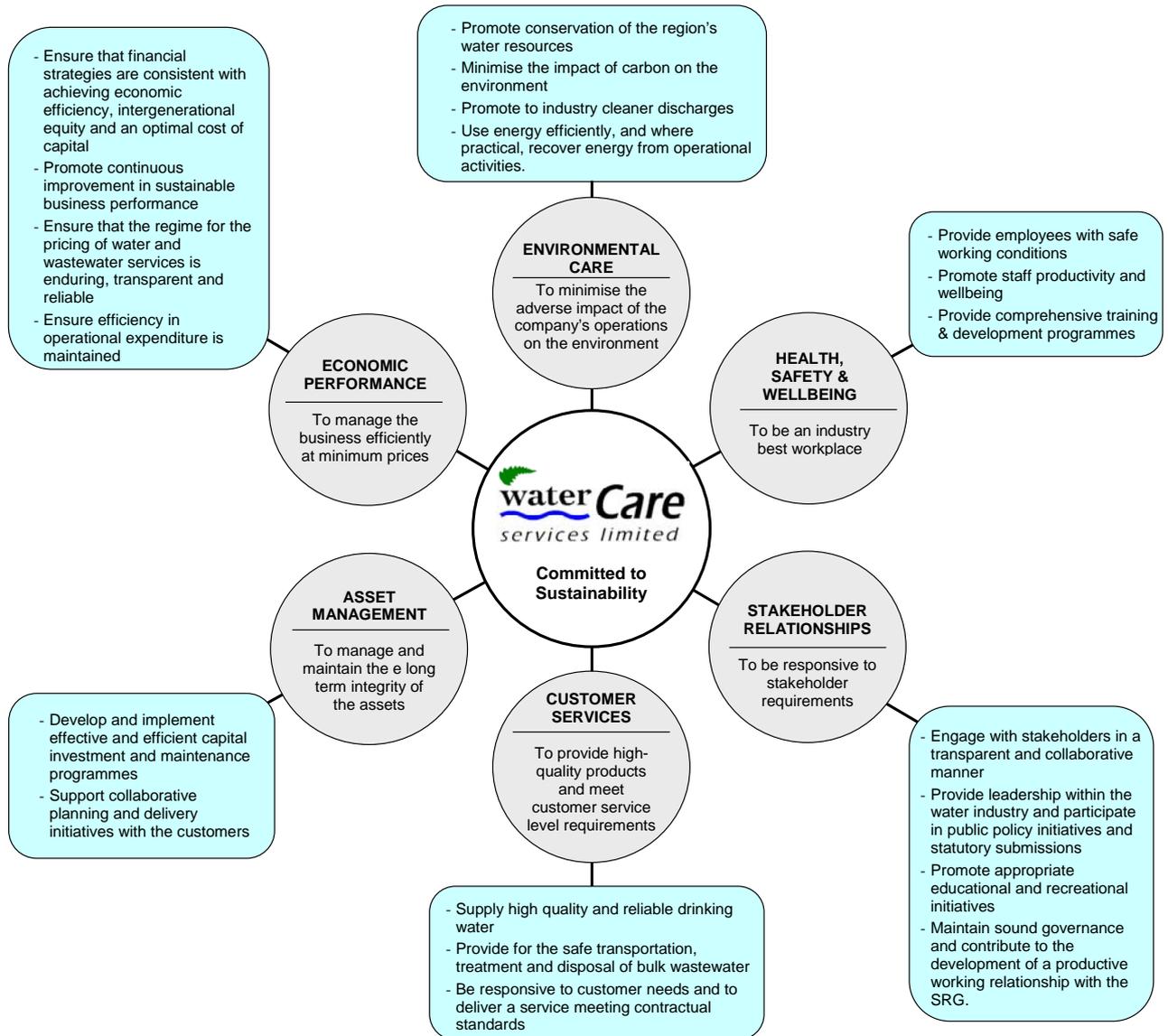
Watercare's commitment to sustainable business practice requires high levels of disclosure of plans, practices and operations. Also, Watercare's position as a monopoly service provider in the Auckland region obliges the company to retain stakeholders' confidence that it is performing optimally.

Each year Watercare publishes an Asset Management Plan to ensure the region's water and wastewater needs are met in a timely and cost-effective manner and support regional growth and planning strategies.

Watercare publicly reports achievement against a comprehensive set of objectives each year in its Annual Report. A range of 'sustainability performance rulers' will continue to be used in 2010/11 to provide a measure to compare current performance against prior years, and to assess improvement against objectives.

3. WATERCARE'S STRATEGIC PERFORMANCE OBJECTIVES

At a strategic level there are a number of performance objectives that the Shareholders Representative Group require Watercare to report performance against on a quarterly basis as detailed below.



In order to monitor performance of the integrated retail function and the new customer services role from 1 November 2010 the following performance objectives have also been included.



Sustainability Policy	Strategic Performance Objective	Performance Measure <i>Strategic initiatives and tactical targets</i>
<p>ENVIRONMENTAL CARE: To minimise the adverse impact of the company's operations on the environment.</p>	<ol style="list-style-type: none"> 1. To promote conservation of the region's water resources. 2. To promote to industry cleaner discharges 3. To minimise the impact of carbon on the environment. 4. To use energy efficiently and where appropriate recover energy from operational activities. 	<ul style="list-style-type: none"> - To develop and initiate implementation of a regional water efficiency and conservation plan for the integrated company by 30 June 2011. - To maintain regional unaccounted for water losses at less than 17.7 Million m³ (Applicable from 1 November 2010) - To achieve a 'Bb' grade as set-out in the 2003 NZWWA guidelines for the safe application of biosolids to land. - To achieve a 75% CO₂ equivalent reduction from 1990 levels for each of the next three years - To target 35% of energy needs sourced internally for each of the next three years.
<p>HEALTH , SAFETY and WELL-BEING: To be an industry best workplace.</p>	<ol style="list-style-type: none"> 5. To promote staff productivity and wellbeing. 6. To provide comprehensive training and development programmes. 7. To provide employees with safe working conditions. 	<ul style="list-style-type: none"> - To attain a lost-time injury frequency rate of less than or equal to 5 - To target an unplanned absenteeism rate of 2.5% - To target over 20 training hours per employee per year. - To target a ratio of less than 2.25 of external to internal appointments - To maintain the tertiary level ACC workplace management practices accreditation.

<p>STAKEHOLDER RELATIONSHIPS: To be responsive to stakeholder requirements.</p>	<p>8. To engage with stakeholders in a transparent and collaborative manner including the company's Maori, Environmental and Consumer Advisory Groups.</p> <p>9. To provide leadership within the water industry and participate in public policy initiatives and statutory submissions.</p> <p>10. To promote appropriate educational and recreational initiatives.</p> <p>11. To maintain sound governance and contribute to the development of a productive working relationship with the SRG.</p>	<ul style="list-style-type: none"> - To consult with all appropriate stakeholders in regard to key infrastructure projects. - To consult with relevant stakeholders in the development of the Regional Asset Management Plan, including major projects. - To obtain annual feedback from the company's advisory groups on the consultation process. - To report on the number of policy initiatives and key submissions made per annum. - To continue with the Rain Forest Express, the 'Adopt a Stream' and other educational programmes as appropriate. - To hold briefings with the SRG at least once every 6 months and undertake Council briefings as requested.
<p>CUSTOMER SERVICE COMMITMENT: To provide high quality products and meet customer service level requirements.</p>	<p>12. To supply high quality and reliable drinking water</p> <p>13. To provide for the safe transportation, treatment and disposal of bulk wastewater.</p> <p>14. To be responsive to customer needs and to deliver a service meeting contractual standards.</p>	<ul style="list-style-type: none"> - To maintain the public health grading of water treatment and networks of 'Aa'. - To ensure that demand can be met in a drought with a 1% probability of occurrence with 15% residual capacity in its reservoirs - To target no more than fifteen dry weather sewer overflows per 100km of wastewater pipe length per annum. ^{Note 2} - To achieve 100% compliance with the LNO contracts to 31 October 2010.

² The definition for a dry weather sewer overflow is as used by the Auckland Water Industry Operators Guide 2007/08. Details of this measure and appropriate targets will be reviewed with the Auckland Council.

<p>ASSET MANAGEMENT: To manage and maintain the long-term integrity of assets.</p>	<p>15. To develop and implement effective and efficient capital investment and maintenance programmes.</p> <p>16. To maintain a focus on integrated planning with the customers to secure long-term wastewater solutions and manage regional wet weather overflows.</p>	<ul style="list-style-type: none"> – To ensure that capital projects have robust business cases and are delivered to plan. – To continue with the implementation of the reliability centred maintenance (RCM) system on strategic assets. – To facilitate a process to agree regional environmental objectives, including the setting of wastewater overflow performance targets for each of the region’s key receiving water environments, within three years. – To progress planning associated with the Central Interceptor.
<p>ECONOMIC PERFORMANCE: To manage the business efficiently at minimum prices and to operate on a least-cost philosophy subject to fulfilling other environmental, social and legislative requirements.</p>	<p>17. To ensure that financial strategies are consistent with achieving economic efficiency, intergenerational equity and an optimal cost of capital.</p> <p>18. To ensure that the regime for the pricing of water and wastewater services is enduring, transparent and reliable.</p> <p>19. To promote continuous improvement in sustainable business performance.</p>	<ul style="list-style-type: none"> – To meet the requirements of the Auckland City Council (Auckland Council) Guarantee of Watercare’s debt. – To achieve a minimum funds flow from operations to interest cover of 2.5 times before any price adjustments. – The pricing methodology enables the revenue to be set to recover all costs and provide for an adequate level of debt servicing. – The pricing methodology established cannot be changed without Watercare providing the LNO customers with three-years advance notification of a change. <i>(Not applicable from 1 Nov 2010)</i> – To continue to use the Project Improve initiative as the vehicle to deliver continuous improvement in business performance.

	20. To ensure efficiency in operational expenditure is maintained.	<ul style="list-style-type: none"> - To meet operational efficiency targets (excluding depreciation and interest) established in the December 2009 AMP as follows: 2011 - \$94.09 million - To report operational expenditure relative to budget for water, wastewater and capex.
--	--	---

<p><i>CUSTOMER SERVICES PERFORMANCE (Integrated business)</i></p> <p><i>Note: these objectives and measures will be effective from 1 November 2010 and will be reported quarterly to the Auckland Council).</i></p>	21. To maintain delivery of cost-effective services	<ul style="list-style-type: none"> - To maintain the average household bill at less than 1.5% of the average household income
	22. To maintain delivery of high quality water and wastewater services	<ul style="list-style-type: none"> - To achieve less than five water quality complaints per 1,000 customer connections
	23. To maintain good customer relationships	<ul style="list-style-type: none"> - To ensure 95% of all enquires are responded to in a meaningful way within 10 working days - To ensure greater than 95% of customers receive 3 days notice of planned shut-downs. - To achieve an average call centre operator connect time of <30 seconds - To monitor the effectiveness of customer communications over integration.
	24. To maintain service capacity	<ul style="list-style-type: none"> - To maintain a water interruption frequency of <10 per 1000 connections ^{note 3} - To maintain the frequency of sewer breaks and chokes (unplanned interruptions) at <10 interruptions per 1000 properties
	25. To restore service capacity	<ul style="list-style-type: none"> - To ensure that at least 90% of unplanned water shutdowns are restored within 5 hours

³ Rather than estimating the number of properties effected by interruptions a more accurate measure has been used which is the number of interruptions per 1000 connections. This measure is consistent with that used in the 2007/08 Auckland Water Industry Performance Report.

	26. To accurately measure and report future levels of customer service performance	<ul style="list-style-type: none"> - To ensure that at least 98% of wastewater blockages are responded to within one hour. - To develop a service level index relevant to the integrated business by 1 March 2011
<i>INTEGRATION OF REGIONAL WATER AND WASTEWATER SERVICES</i>	26. To successfully transition retail water and wastewater services to Watercare.	<ul style="list-style-type: none"> - To ensure all critical elements of Project One are achieved by 1 November 2010 ensuring a successful transition to an integrated water and wastewater services company. - To complete Project One within budget.

APPENDIX

This appendix contains background information on the nature and scope of Watercare's activities and on significant issues facing the business. It also contains other information disclosures required by the Local Government Act.

A. NATURE AND SCOPE OF ACTIVITIES

A.1 Background

Watercare was established in 1992 as a Local Authority Trading Enterprise (LATE) responsible for the provision of bulk water and wastewater services to the Auckland region. In 1998, ownership of the company was vested in the city and district councils of Auckland, Manukau, North Shore, Papakura, Rodney and Waitakere, having previously been owned by the Auckland Regional Services Trust. Since 1 July 2003 when the Local Government Act 2002 (LGA 2002) came into force, Watercare has been subject to dual legislative regimes;

- the Watercare specific provisions of the Local Government Act 1974 (LGA 1974), and
- the "Council Organisation" (CO) provisions of the LGA 2002.

Under the Watercare specific provisions of the LGA 1974 in section 707ZZZS Watercare is required to:

"manage its business efficiently with a view to maintaining prices for water and wastewater services at the minimum levels consistent with the effective conduct of that business and the maintenance of the long-term integrity of its assets".

Auckland Governance reform in 2009 confirmed Watercare's role as the provider of regional water and wastewater services and gave responsibility to the company for managing the transition from a wholesale to an integrated wholesale/retail business under the oversight of the Auckland Transition Agency. The final legislative process of the governance changes is the introduction of the Local Government (Auckland Law Reform) Bill (2009) which is currently undergoing Select Committee process. Under the Bill Watercare will retain its current status as a CO, including Watercare specific provisions of the LGA (1974), through to 1 July 2012 when it will become a Council Controlled Organisation (CCO) consistent with other large Council organisations. The details of the final Bill, which will include decisions on Watercare specific requirements (director appointment, minimum price obligation, sale of shares, assets etc.) are still subject to the outcome of the Select Committee process.

A.2 Governance

Shareholders

The six Auckland local authorities own shares in Watercare in the following proportions

- Auckland City 41.6%
- Manukau City 25.1%
- Waitakere City 16.7%
- North Shore City 11.5%
- Papakura District 3.7%
- Rodney District 1.4%

From 1 November 2010 the Auckland Council will become the sole Shareholder of Watercare.

Shareholder Representative Group

The owners of Watercare are represented, collectively, by the Watercare Shareholder Representative Group (SRG). Each of the six owners appoints two representatives to the SRG.

A Shareholders' Agreement, which was agreed between the six owners in 1998, sets out the role of the SRG and procedures for meetings of the group. In summary, the SRG;

- selects and appoints directors of Watercare
- approves Watercare's annual SCI
- considers the Asset Management Plans on behalf of the owners
- approves any major acquisition or transaction by the company on behalf of the owners
- reviews the performance of the Board
- liaises and consults on the company's financial performance

Decisions or actions on these points require the agreement of a representative of each of the shareholders collectively holding 75% or more of the shares in Watercare before they are binding on all shareholders.

The directors and senior executives meet the SRG quarterly to brief them on company operations.

From 1 November 2010 Watercare will be owned by a new shareholder, the Auckland Council. The functional details of the new relationship with the Auckland Council will be determined in due course.

Board of Directors

Watercare has an independent board of directors. The LGA 1974 and the Local Government (Auckland Law Reform) Bill stipulate that no person who is a member or an employee of a local authority may hold office as a director of Watercare.

Watercare's Constitution requires the directors manage the company in line with the annual SCI. Through the SCI, the directors are accountable to the owner(s), who are, in turn accountable to residents and ratepayers of the Auckland region.

Practically the directors determine the overall direction of the company in light of the objectives set out in the SCI and the statutory requirements for the company in the LGA. The directors make major decisions, including decisions on major new capital investment and on major business initiatives, in line with those objectives.

The directors are responsible for monitoring the performance of the company, and for monitoring the performance of the Chief Executive who has responsibility for managing the company on a day-to-day basis.

A.3 Business Overview

(a) Water Services

Watercare collects and treats raw water from the Hunua and Waitakere Ranges, the Waikato River and from groundwater sources at Onehunga and supplies the LNOs with potable water at contractually defined standards of quality and storage security. Water demand for the 12 months ending June 2009 averaged 358,690 m³ per day and was reticulated by the LNOs to over 1,258,000 consumers.

From 1 November Watercare will assume responsibility for all the assets and operational activities associated with water catchment, treatment, storage and distribution of water to meet the requirements of Auckland's business and household customers. The exception will be United Water who will continue to retail water under a franchise agreement with Watercare owning the assets and the franchise and supplying bulk water for retail delivery.

(b) Wastewater Services

Watercare collects wastewater up to specified maximum flow rates, from Herald Island to Papakura. The Company's system services four LNOs, (Metro Water, Waitakere City Council, Manukau Water and United Water), over 600 trade waste customers and ultimately over 975,000 consumers.

Approximately 342,410 m³ per day of wastewater is received from the LNOs' systems and treated at the Mangere Wastewater Treatment Plant (WTP). Discharges from the treatment plant to the environment are controlled in accordance with resource consents granted by the ARC pursuant to the Resource Management Act 1991 (RMA).

Integration will significantly expand Watercare's wastewater network as it takes over responsibility for the region's second largest Wastewater Treatment Plant at Rosedale, smaller regional treatment plants, local networks and the retail delivery of wastewater services to customers of the Auckland region. United water will continue to provide retail wastewater services in the same way it does for water.

(c) Laboratory Services

Watercare operates one of the largest water, wastewater and environmental laboratories in New Zealand. The analytical laboratory provides sampling, on site monitoring, analytical and scientific services. In addition, the air quality department provides ambient air and point source emission and odour monitoring. The laboratory services a wide range of clients both internally and nationwide. The Laboratory will continue to deliver sampling, monitoring and testing services following integration.

(d) Watercare's Organisational Structure

In preparation for integration, the company structure has been reorganised around four key functional areas as follows:

Infrastructure: Responsible for asset planning, asset development, project management and delivery of new assets.

Operations: Responsible for water collection and treatment operations, wastewater treatment and network operations, maintenance planning, monitoring and prevention of wastewater overflows and risk management.

Customer Service: Responsible for managing and monitoring the delivery of customer services including meter reading, bill collection, the call centre and major accounts management.

Finance: Responsible for financial reporting, accounting and treasury management. The finance group will also be responsible for information systems management, asset information management and procurement and property management.

B. SIGNIFICANT ISSUES

B.1 Integration of the Water and Wastewater Services

The successful integration of the regional water and wastewater services industry represents a major undertaking for Watercare. The integration of six LNOs, including their diverse functions and assets, presents many challenges and risks. In response, Watercare established 'Project One' consisting of Watercare and LNO subject matter experts to plan for and implement the changes. The Project One team is focused on achieving a smooth transition which will cause minimal disruption for retail customers. Project one continues to progress well and is now in an implementation phase focusing on three major work streams, customer, operations and corporate. Teams are also working on information systems, communications, people and legal and governance.

B.2 Operating Environment

A key issue facing Watercare over the longer term is the strong growth of the Auckland region as outlined in the Regional Growth Strategy. This growth will result in an increasing demand for water supply and wastewater services.

Efficient use of existing resources and infrastructure through demand management, inflow and infiltration control as well as enhancement, expansion or replacement of existing infrastructure will continue to be required to meet growing demand.

At the same time, the requirement for reduced environmental impacts, formalised through resource consents issued under the Resource Management Act, will place increasing demands on the operational performance of existing infrastructure.

From 1 November integration will offer new opportunities to improve the region's efficiency in the long-term planning and delivery of water and wastewater services. The Three Waters Strategic Plan, completed in December 2008, was an important step in the identification of future regional infrastructure. Work will continue to build on the three waters foundation to maximise the potential of integrated regional planning to deliver sustainable, cost effective outcomes.

As a matter of continuous improvement, Watercare is currently working on the delivery of an Integrated Asset Planning Framework to formalise and improve the efficiency of the asset planning process. The development of a new Regional AMP in 2010 that considers regional asset management priorities in an integrated fashion will be an important step in this planning process.

B.3 Water Supply

As the region grows and demand for water increases the reliance on the existing aging network increases raising the potential for supply risks. The Hunua No. 4 water main which is currently being designed will provide additional capacity from the southern supply zone to meet growth requirements in the north and reduce the risks associated with reliance on the existing water supply network. Over the next year Watercare will continue to focus on completing the route design and obtaining designations and resource consents for the new water main and associated works.

Watercare works closely with the Ministry of Health and the Ministry for the Environment to ensure water quality standards development are appropriate from a public health and affordability viewpoint. This relationship will continue following integration.

B.4 Wastewater Collection, Treatment and Disposal

Under the provisions of the Resource Management Act (RMA), Watercare is obliged to secure resource consents for discharges associated with the operation of the bulk wastewater collection systems.

Applications to renew the existing wastewater discharge consents were submitted in March 2001 to permit the continued operation of the wastewater collection system in compliance with the RMA. Further consents were sought in 2008 to use biosolids to rehabilitate a quarry on Puketutu Island, providing an opportunity for the development of a regional park in the process. Although Watercare was unsuccessful in securing the designation and resource consents, appeals have been lodged and the company is committed to working with local groups to find a workable solution.

As an integrated company, Watercare will continue to review existing network models, catchment studies and the development of harbour and stream quality models to quantify the effects of wastewater overflows. The principal objective of the project is to ensure that overflow mitigation works are regionally optimised, fully accounting for the economic, environmental and social impacts. Such planning remains crucial to optimising the development and operation of new infrastructure such as Project Hobson and the central interceptor.

Planning and design stages are underway for the central interceptor, a sewage conveyance and storage tunnel identified through the Three Waters joint planning process as the preferred solution to address the need for additional trunk sewer capacity to central Auckland. The new central interceptor will collect wastewater flows from parts of central Auckland and Waitakere City and transfer them to the existing Mangere Wastewater Treatment Plant.

B.5 Trade Waste

Trade Wastes are controlled and charged for under a framework established by the Auckland Metropolitan Drainage Act (AMDA) and by the supporting Trade Wastes Bylaw as amended by Watercare.

With integration, the AMDA will be repealed. However, the clauses supporting the Bylaw, under which Watercare manages trade wastes, and the bylaw itself will continue for a further five years. It is envisaged that Watercare will also assume the rights and responsibilities of the North Shore City Council, Rodney District Council and the Franklin District Council trade waste bylaws. This will enable Watercare to continue managing trade waste discharges until the promulgation of a new regional trade waste bylaw under the LGA 2000 by the new Auckland Council. However, an amendment will be sought to the ARC Trade Waste Bylaw 1991 to be completed by 1 November 2010. The amendment is required to minimise the extent of changes to the level of trade waste charges customers will experience following integration.

Watercare will continue to review its Trade Wastes control programmes and implement changes as required to ensure that management of Trade Wastes is aligned to WTP processes and its resource consent requirements. Watercare is committed to consulting all stakeholders to ensure that any changes meet the needs of all concerned.

B.6 Customer Contracts

The existing bulk water contracts will continue until 31 October 2010 when Watercare will become responsible for retailing water direct to customers of the Auckland region. The existing wastewater contracts, which expire on 30 June 2010, will be rolled over to 31 October.

The exception is United Water which will continue to operate and retail water and wastewater services under its existing franchise agreement. This agreement requires Watercare to provide bulk water and wastewater services and the existing contracts will continue and be renegotiated upon expiry.

As a result of integration, Watercare also proposes to gradually standardise the terms and conditions of the retail contracts wherever possible.

B.7 Funding

Watercare is investing in a significant capital works programme that will ensure Auckland continues to receive a secure high quality water supply and safe wastewater collection, treatment and disposal.

Watercare's financial strategies are developed to ensure they are consistent with the goals of achieving economic efficiency, intergenerational equity and optimal cost of capital.

To achieve Watercare's financial goals the company must maintain an appropriate balance between revenue and debt funding and must be able to raise the necessary debt from a wide variety of sources and at attractive interest rates. In July 2008 Watercare established a debt guarantee facility with Auckland City Council backed by the remaining shareholders. The guarantee facility allows Watercare to use the strong credit rating of Auckland City to become more highly geared and deliver lower price increases than would otherwise have been possible.

Watercare is currently achieving an 'AA-' rating on debt from Standard & Poor's as a result of the guarantee facility which has allowed the company to borrow funds at more favourable rates.

Following integration, the debt guarantee will continue to exist with the new Shareholder, the Auckland Council. Watercare will continue to use the guarantee facility to raise debt in circumstances where justified by lower costs.

C. OTHER INFORMATION

C.1 Shareholders' Funds

	2009/10
Consolidated Shareholders' Funds to Total Assets	58.79
Consolidated Shareholders' Funds to Total Assets (historic cost)	28.57

Note:

1. Consolidated Shareholders' Funds are defined as Issued and Paid Up Capital, Revaluation Reserve and Retained Earnings.

2. Total Assets are defined as Net Book Value of Current Assets, Investments and Fixed Assets as disclosed in the Company's Statement of Financial Position.
3. The ratio of Consolidated Shareholders' Funds excluding the revaluation reserve to Total Assets less the revaluation reserve is referred to as the historic cost basis.
4. No ratios are provided for 2010/11 and 2011/12 financial years as forecasting for the integrated company has not been completed.

C.2 Accounting Policies

Watercare's financial statements are prepared in accordance with the New Zealand International Financial Reporting Standards.

C.3 Application of Surplus Funds

Watercare is prohibited by legislation from paying a dividend.

Watercare annually reviews any water and wastewater surpluses and considers if the return of such surpluses to the customers is commercially prudent.

Watercare has developed a Pricing Adjustment Mechanism that allows for prices to customers to be reduced in circumstances where in aggregate, the company's performance in the year is significantly better than anticipated. The pricing adjustment in these exceptional circumstances will be made in the year it occurs.

C.4 Information to be provided to the Shareholder(s)

Watercare will meet the requirements of the LGA 1974 and LGA 2002⁴, the Companies Act 1993 and the reasonable requirements of the Shareholder(s). In particular, the following information will be provided:

- *Annual Statement of Corporate Intent (SCI)*

Watercare will provide a draft and final SCI in accordance with the LGA. The Directors will include any other information they consider appropriate.

The draft SCI will be provided to the Company's shareholder on or before 1 March each year and the final SCI by 30 June each year in terms of the LGA 2002 and Watercare specific provisions in the LGA 1974.

- *Asset Management Plan*

In accordance with ss707ZZZS(1)(k) and (m) of the LGA 1974, Watercare will provide an indicative Asset Management Plan to each shareholder at least four months before the end of the financial year, will consider written submissions made by each shareholder on that plan and will include in the SCI a summary of Watercare's proposals in respect of the submissions.

An assessment of the costs and benefits of significant proposed projects and their alternatives, including the impact of demand management and efficient pricing, and the commercial and operational risks of not proceeding with the project, deferring it or bringing it forward will be included in the Asset Management Plan.

⁴ Watercare will also be required to meet requirements of the Local Government (Auckland Law Reform) Bill when enacted by Parliament.

- *Funding Plan*

In accordance with ss707ZZZS(1)(l) and (m) of the LGA 1974, Watercare will provide an indicative Funding Plan to the shareholder at least four months before the end of each financial year, will consider written submissions made by each shareholder on that plan and will include in the SCI a summary of Watercare's proposals in respect of the submissions.

- *Management Reports*

Management reports will be provided within one month of the end of the September and March quarters and within two months of the end of the December and June quarters, including:

- The unaudited Statement of Financial Position as at the end of the preceding quarter, and the Statement of Financial Performance, Statement of Cash Flows and a capital expenditure summary for the year to date and the preceding quarter. These statements will include comparative budget data and variances.
- A commentary upon significant matters that occurred in the previous quarter including comments on financial results and significant matters expected in the next quarter.
- The return on equity for the preceding quarter and year to date.
- Particulars of any assets sold during the preceding quarter where the aggregate value of associated assets exceeds \$1 million.
- Reasons for, and impacts of variance from the capital expenditure programme which was identified in the Asset Management Plan.
- A commentary on significant capital projects in progress.
- A commentary on material changes, if any, in capital expenditure from that reported in the AMP.
- A commentary on significant customer service and management issues.
- A report on the achievement of the SCI performance targets.
- Any reasonable request for information.

The statutory obligations to provide shareholders with a half-year and a full year report on operations will be met by the management reports for the December and June quarters respectively.

- *Annual Report*

Watercare will produce an Annual Report that covers sustainability performance together with the audited financial and service performance statements.

The report will be provided within three months of the end of the financial year in accordance with the LGA, and will meet the reporting requirements of the Companies Act and the Financial Reporting Act. It will comply with New Zealand International Financial Reporting Standards and will include any other information the Directors consider appropriate.

- *Shareholder Consultation*

Watercare will maintain an ongoing dialogue with the shareholder(s), to ensure they are aware of major issues facing Watercare and are satisfied that Watercare is meeting its business and performance targets.

In particular Watercare will keep its shareholder(s) informed of any submissions it makes on significant areas of legislative change.

C.5 Procedure for the acquisition of shares

The Directors will consider all share investment proposals.

Any decision to invest in or divest shares in another company or to enter into a joint venture relationship or participation arrangement through equity or operating agreements will be made by the Directors in accordance with Watercare's constitution. The shareholders will be consulted in the event that an investment or divestment of this nature will create a significant increase in risk exposure.

C.6 Events requiring Shareholder approval

Shareholder approval will be obtained prior to Watercare entering any business activity that significantly changes or is outside the nature and scope of Watercare's current activities.

C.7 Activities for which the Company seeks compensation from any Local Authority

Watercare maintains commercial arrangements with the Auckland Territorial Authorities for functions, duties or services that Watercare is required to undertake. These include supply of water, collection of wastewater and trade wastes functions. However these negotiations will be without prejudice to Watercare's rights at law to impose reasonable charges for the supply of its services.

C.8 Directors' estimate of the Commercial Value of the Shareholders' Investment

The inclusion of an estimate of commercial value is a statutory requirement.

Watercare is however prohibited by the LGA from being privatised. Legislative restrictions prevent Watercare's shareholder(s) from selling their shares and prevent Watercare from paying dividends to its shareholder(s).

The book value of the shareholders' investment at 30 June 2009 was \$1,451m based on the accounts maintained by Watercare in accordance with the stated accounting policies. The Directors may from time to time requisition an independent valuation of the shareholder investment.

C.9 Asset Management Plans and Funding Plans

The Asset Management Plan (AMP) for the financial year ending June 2011 was issued to Shareholders on 1 December 2009. No comments were received from Shareholders on the AMP. However, Watercare responded to several minor comments received from the OWG in January 2010.

Watercare's Funding Plan for the 2010/2011 financial year was issued to the shareholders on 26 February 2010.

The Shareholder comments on the SCI and the Funding Plan were received as resolutions from the 21 April Shareholder Representative Group Meeting.

Key matters raised, including Watercare's response is included in the table below.

	SRG Resolution	Watercare Response
A	Receives the comments tabled at the meeting from shareholding councils.	Noted
B	Comments in respect of Watercare Services Limited's 2010 Funding Plan that the SRG supports Watercare's prudent approach to budgeting for 2009/2010 and for 2010/2011 which has allowed the operational costs of transition (\$4.0 million for 2009/2010 and \$4.2 million for 2010/2011) to be absorbed without adding to already substantial price increases.	Noted
C	Comments in respect of Watercare Services Limited's 2010 Funding Plan that the SRG expects that Watercare will achieve actual financial results closer to budget, in future years following transition, which will ensure that prices are kept to the minimum.	Rather than meeting budget, Watercare managers are always encouraged to do better than budget. However, achieving an outcome where actual results are closer to budget is often difficult due to the time between preparation of the funding plan (Jan/Feb) and the completion of the financial year (June of the following year). Furthermore, any over or under performance is taken into account when developing the next year's funding plan.
D	Asks Watercare Services Limited whether there has been any risk to security of supply and/or regulatory compliance from Watercare under spending its capital expenditure budget since 2007/2008 and absorbing \$23.2 million of transition related capital expenditure, within its asset management plan which has been subject to independent review.	Watercare has worked hard to assimilate the costs of integration without compromising risks to security of supply or regulatory compliance. The majority of changes have come through a concerted effort to review the timing of capital and operational expenditure while still maintaining appropriate levels of risk across the region. The closer cooperation between Watercare and the LNOs and the commitment to focus on regional solutions has also helped with prioritisation and timing of capital expenditure.
E	Comments in respect of Watercare Services Limited's 2010 Funding Plan, that the SRG suggests that future funding plans prepared by Watercare as the region's integrated water and wastewater provider,	Refer E(i) to E(v) below

	owned by the Auckland Council:	
E (i)	show both wholesale and retail prices (as proposed by Watercare), rather than a single water price and a single wastewater price, as this will help ensure transparency of pricing;	A wholesale price will be shown for United Water which will continue to operate under their existing franchise agreement.
E (ii)	include the rate of inflation of Watercare's own inputs, instead of the consumer price index, in order to improve the transparency of price changes;	Watercare's pricing methodology enables revenue to be set to recover all costs. Inflation, growth and other factors are included in the method. Separating out drivers in more detail is a difficult exercise and does not necessarily achieve greater accuracy or transparency. Watercare discussed the complexities of this issue with the OWG and has agreed to work with the Auckland Council regarding transparency of the pricing methodology.
E (iii)	include more detail of how Watercare calculates its trade waste and laboratory prices, including an explanation of the projected changes in these prices and the factors driving price changes, to enable more scrutiny of this funding;	<p>It is inappropriate to provide more detail on how Watercare calculates laboratory charges because of commercial sensitivities.</p> <p>Trade waste charging is a complex cost recovery process involving a number of assumptions and calculations. However, trade waste customers do not subsidise other wastewater service customers.</p> <p>As a regional service provider Watercare is committed to fair and equitable delivery of services and charges. General statements will be included in future funding plans to explain how the pricing of Laboratory Services and trade waste charging is determined.</p>
E (iv)	set a budget that ensures the funds from operations to interest cover ratio is 2.5 rather than allowing it to remain above that ratio, and	<p>The Funding Plan is prepared based on the AMP and targeting an FFO of 2.5 times cover without any significant accounting loss.</p> <p>Consideration is also given to smoothing price changes from year to year. Budgeting follows production of the Funding Plan. At times the FFO achieved may be higher than the target as managers strive to better budgets and performance targets.</p> <p>Any over performance that results in less debt is taken into account when developing the Funding Plan and</p>

		budget for the following year.
E (v)	include operating and capital expenditure budgets for year one of the funding plan.	The Funding Plan is prepared based on the Asset Management Plan. Detailed budgeting does not take place until after the funding plan has been prepared. The best indication of the year 1 budget would be provided from year 1 of the AMP. It is not proposed to include this information in future Funding Plans.

C.10 Disposal of Assets

The Company will consult with the shareholder(s) prior to the disposal of any part of its undertakings, which, in any one-year, exceed in aggregate 5% of the current book value of its assets.