

CHAPTER 1 : INTRODUCTION AND OVERVIEW

1.1 CHAIRMAN'S FOREWORD

The year under review saw the continued successful implementation of the financial turnaround strategy. The current year implementation focused on the following strategic imperatives.

- Migration of core functions and customer data base
- A real tariff increase of 3%
- Implementation of Operation Gcin'amanzi

The following core functions were successfully migrated in October 2004:

- Meter reading
- Billing
- Customer query resolution
- Data quality control
- New connections for account finalisation and issue of clearance certificates.

The Sandton customer data base was migrated in February 2005. 43 000 accounts were migrated.

Coupled with the tariff increase the migration resulted in a significant increase in payment levels and revenue.

Operation Gcin'amanzi was successfully implemented in Phiri and Superblocks 1 to 3. This is a multi-million Rand project to upgrade municipal water infrastructure and install prepayment meters in the Greater Soweto area.

The project was launched in August 2003 with the intention of reducing the severe water losses which amounts to about 7 billion litres of water a month. The project will be completed in June 2007. As a result of this intervention a marked reduction in bulk water purchases impacted positively on the cost of sales with a resultant increase in gross profit.

In addition to the above interventions prudent cost management led to an improvement in operating profit.

Performance monitoring as per balanced scorecard and the City of Johannesburg's Integrated Development Planning saw a marked improvement for the year under review.

Human capital development and transformation was adversely affected by the non-achievement of black economic empowerment targets particularly in the area of procurement of goods and services. The non-achievement was worsened by fronting. This area is a challenge for the Company and plans are already in place to address the matter.

Training and HIV/AIDS awareness programmes are on track. A Knowledge Attitude and Practice survey confirmed that the awareness programme had a major impact specifically on levels of knowledge whilst all areas indicated improvement. A voluntary counselling and testing programme was launched with success on 1 December 2004.

The following major projects were successfully completed :

- Upgrading of Alexandra water network
- Bruma outfall sewer augmentation
- Replacement of van Wyks rising main
- Installation of digester mixers (Goudkoppies Waste Water Treatment Works).

Projects that are ongoing include Operation Gcin'amanzi and the VIP programme.

Capital Expenditure against external funding provided by the City of Johannesburg excluding funding for Operation Gcin'amanzi was 98%.

Johannesburg Water has over the past year extended its public profile through a series of innovative and proactive campaigns and programmes. The recent customer satisfaction survey revealed yet again that public awareness of Johannesburg Water has increased significantly.

On a public education front Johannesburg Water's popular schools road show now reaches out to an average of 20 000 school learners each month. Johannesburg Water has produced a wide range of education material which complements our work with schools and learners. Various publications, ranging from water conservation tips to a comprehensive manual on water services in Johannesburg has also been produced and distributed to consumers through Johannesburg Water and the City of Johannesburg distribution points.

The Johannesburg Water Festival held in April 2005 attracted the participation of more than 100 different schools. Johannesburg Water is also in the process of establishing two community food gardening programmes, one at its Olifantsvlei Farms and another at the Northern Farms. This is part of the Company's corporate social investment programme and once fully operational will see the empowering of at least 100 community farmers on each of these projects.

Johannesburg Water has also intensified its communication efforts with regards to Operation Gcin'amanzi. This has been achieved through information manuals, outdoor advertising, the production of a bi-monthly newsletter to the community and also the development of a video which can be used by councillors to inform and engage with their constituencies.

The challenges facing Johannesburg Water are:

- Roll out of Operation Gcin'amanzi
- Black economic empowerment and transformation
- Water and sanitation national targets
- Infrastructure rehabilitation
- The development of a post "turnaround strategy" strategy.
- The development of a Post Jowam Strategy.

Executive management will implement and align management strategies in a manner that will optimally address the above challenges.

During the year under review the Board experienced four resignations which required significant commitment from the remaining members of the Board. Up to the appointment of the new directors in January 2005 I have to acknowledge the diligence of the directors in exercising their duties under trying circumstances. During this time the Company saw the beginning of the successes of the turnaround strategy.

The Board also saw the development of a risk policy and strategy which provides for risk to be managed by the Managing Director through his Executive Committee which reports into the Board.

The report of the external auditors has brought to the attention of the Directors and Management the issues that resulted in the disclaimer of audit opinion. Considerable progress has been made compared to the previous year, particularly by Johannesburg Water, on matters under the control of the company, including the completeness of revenue in respect of customers migrated from the City. The most significant items contributing to the report being disclaimed relate to the following:

- Controls were not in place to reconcile the properties reflected in the Geographic Information System (GIS), which is managed by the City, with users as recorded in the billing system. Completeness of revenue may be an issue.
- Debtors classified as indigents totaling R358,4 million were written off by the City of Johannesburg. Documentation to support the validity and accuracy of customers classified as indigent could not be made available by the City for audit purposes.
- Tests of detail revealed numerous unexplained differences in the ageing of debtors which may impact on the provision for impairment. The billing system is managed by the City.

- The continued non payment by consumer debtors in certain areas and the low payment levels in others could adversely impact on the ability of the company to provide services in the future. In terms of International Accounting Standard 36 a further provision for the impairment of assets may be required under such circumstances. The company is of the view that a further impairment is not required and has not increased the asset impairment requirement.

Discussions will be held with the City of Johannesburg to resolve the issues raised, where applicable. The limitation however, on the ability of the directors to exercise their fiduciary duties, as outlined in the Statement of Responsibilities, is of concern to the directors of Johannesburg Water.

In conclusion I wish to express my gratitude to the Board for their painstaking effort in designing and formulating the strategic direction of the entity and to Executive Management for ensuring the successful implementation of the strategy in 2004/2005.

Andries Tshabalala
Chairman

1.2 Overview of the Entity

Johannesburg Water (Pty) Ltd was incorporated on 21 November 2000 and commenced business on 1 January 2001.

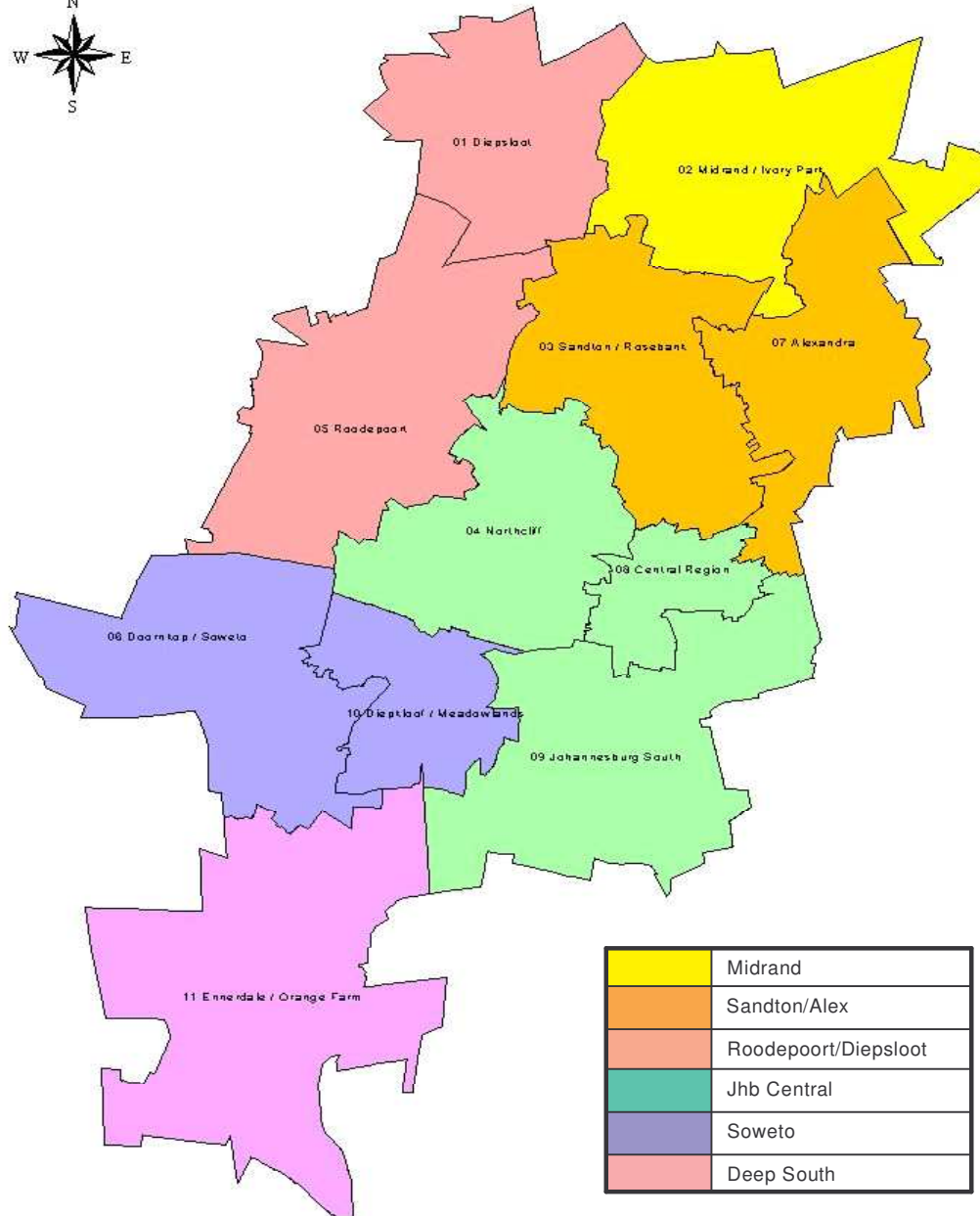
Johannesburg Water is a municipal entity wholly owned by the City of Johannesburg and is mandated to provide water and sanitation services to the residents of Johannesburg.

The entity supplies water and sanitation services to an area stretching from Orange Farm in the South, Midrand in the North, Roodepoort in the West and Alexander in the East. The entity operates in 6 regions with 10 network depots and 6 waste water treatment plants. The map overleaf indicates the operational area of Johannesburg Water.

The entity supplies some 600 000 domestic, commercial and industrial customers and serves an estimated consumer base of 3 million people.

The entity employs approximately 2 547 people and through a network of 9 000km of distribution pipes and over 100 reservoirs and water towers, reticulates water to consumers. Johannesburg Water also collects waste water through a 8 500km network. Water purchases amounts to 1 240 MI/day from Rand Water and 980 MI/day of sewage is treated.

Johannesburg Water Regions



1.3 Executive Summary

Johannesburg Water's Turnaround Strategy has the following main thrusts:

- Upgrading of infrastructure to reduce the level of unaccounted for water.
- Installation of prepayment meters to improve payment levels.
- Implementation of various interventions to improve the billing rate and payment levels including:
 - Migration of core functions from the City of Johannesburg
 - Migration of customers from the City of Johannesburg
 - Data Clean-up
 - Customer Services

Strategy implementation focuses on four strategic priorities:

- Financial Sustainability
- Service Delivery
- Human Capital Development and Transformation
- Governance

The continued implementation of the Turnaround Strategy progressed successfully with a significant positive impact on the financial results of the Company.

The upgrading of infrastructure and installation of prepayment meters as part of Operation Gcin'amanzi progressed well with the resultant reduction in water purchases.

The migration of customers resulted in an increase in payment levels and the process of data cleaning was completed. The migrations of the West and East customer database were scheduled for August and October 2005 respectively. Discussions are currently being held with the City in this regard.

Financial sustainability targets were exceeded. Revenue increased and profit before tax for the year ended June 2005 was R156 million compared to a loss of R118 million for the previous year.

The attainment of service level targets resulted in improved customer responsiveness. Water quality and environmental compliance was in line with specifications.

The process and programme of ensuring access to basic sanitation was expedited with the installation of 5 000 ventilated improved pit latrines.

There was an increase in the employment equity percentages for the top three management levels compared to the previous year. The Black Economic Empowerment targets relating to procurement were not met and strategic interventions are now in place to address the issue.

Ten contracts each exceeding R4 million in value were initiated at a total cost of R229 million.

1.4 VISION AND MISSION

VISION

To become the leading water utility in South Africa.

MISSION

To provide all residents of Johannesburg with access to quality water and sanitation, Johannesburg Water will

- Deliver a sustainable, affordable and cost effective service
- Upgrade services in low income areas
- Create a customer focused culture
- Build capacity through the development of our employees
- Protection of the environment

1.5 STATEMENT OF RESPONSIBILITIES

The directors are responsible for the preparation, integrity and fair presentation of the annual financial statements of Johannesburg Water. The annual financial statements presented on pages 35 to 76 have been prepared in accordance with Statements of Generally Accepted Accounting Practice in South Africa, and include amounts based on judgement and estimates made by management. The directors also reviewed the other information included in the annual report and are responsible for both its accuracy and its consistency with the annual financial statements.

The City manages customers representing approximately 60% of the service revenue of Johannesburg Water. The Company is dependent on the City for the following functions relating to those customers managed by the City:

- Billing (excluding migrated core functions)
- Cash collection
- Debtors

The following concerns relating to issues under the control of the City were identified:

- Controls were not in place to reconcile the properties reflected in the Geographic Information System (GIS), which is managed by the City, with users as recorded in the billing system. Completeness of revenue may be an issue.

- Debtors classified as indigents totaling R358,4 million were written off by the City of Johannesburg. Documentation to support the validity and accuracy of customers classified as indigent could not be made available by the City for audit purposes.
- Tests of detail revealed numerous unexplained differences in the ageing of debtors which may impact on the provision for impairment. The billing system is managed by the City.
- The continued non payment by consumer debtors in certain areas and the low payment levels in others could adversely impact on the ability of the company to provide services in the future. In terms of International Accounting Standard 36 a further provision for the impairment of assets may be required under such circumstances. The company is of the view that a further impairment is not required and has not increased the asset impairment requirement. Notwithstanding this the payment level for Johannesburg Water exceeds 100% and the payment level achieved for Customers managed by the City requires attention.

The significance of the amounts involved has resulted in a disclaimer of audit opinion by the Auditor-General, on the annual financial statements. The issues above are under the direct management of the City and beyond the control of the management or the directors of the Company.

The annual financial statements have been audited by the Office of the Auditor General, who had access to all available records and related data, including minutes of all meetings of the Board of Directors and Committees of the Board. The directors believe that all representations made by Johannesburg Water to the Office of the Auditor General during their audit are valid and appropriate.

The Annual Financial Statements were approved by the Board of Directors on 12 January 2006 and signed on its behalf by:

.....
DIRECTOR
(ACCOUNTING OFFICER)

.....
DIRECTOR