


NEW SOUTH WALES
GOVERNMENT TRADING ENTERPRISES

STATEMENT OF CORPORATE INTENT

ORGANISATION: **Hunter Water Corporation**

PERIOD: Commencing 1 July 2011

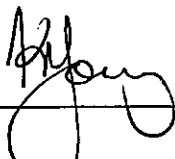
This Statement of Corporate Intent has been agreed between:



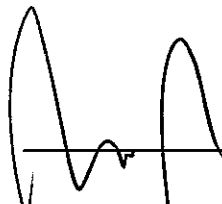
Ronald Robson
Chairman
Hunter Water Corporation
on behalf of the Board



Voting Shareholder
Barry O'Farrell
Premier of New South Wales
Minister for Western Sydney



Kevin Young
Chief Executive
Hunter Water Corporation



Voting Shareholder
Mike Baird
Treasurer

Board of Directors

Ronald Robson (Chairman)

Kevin Young (Managing Director)

Barbara Crossley

Richard Chappel

Gary Kennedy

Adrian Page

Jann Gardiner

Jeff Eather

Cristina Cifuentes

Hunter Water Corporation: Statement of Corporate Intent 2011/12

Hunter Water Corporation

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July 2011

Statement of Corporate Intent for the financial year ending 30 June 2012

Preamble

Hunter Water's operations are regulated by the NSW State Government on behalf of the community via a number of regulatory instruments:

- Water management and access licences issued by the NSW Office of Water (NOW) set conditions for access to natural surface and groundwater.
- Wastewater system licences issued by DECCW stipulate quality and quantity conditions for discharge from wastewater treatment works, as well as performance of wastewater networks.
- Customer service standards and other environmental commitments as specified in an Operating Licence issued by the Independent Pricing and Regulatory Tribunal (IPART) and administered by the Minister for Water.
- Prices are determined by IPART currently over a four-year price period.
- Water quality is managed through a Memorandum of Understanding (MOU) with the Department of Health.

These regulatory instruments each have their own accountability and reporting arrangements. The purpose of this Statement of Corporate Intent (SCI) is to report on the commercial aspects of Hunter Water's role, which are carried out in the context of the above regulatory arrangements.

1. Objectives of Hunter Water

Hunter Water's vision: "To be the leader in sustainable water services and utility solutions for our customers".

Hunter Water's mission: "To provide superior customer service and enhance the environment through operational excellence and a high performance culture by developing our people".

Hunter Water is committed to:

- thinking, working and living safely
- providing superior customer service
- delivering safe, highly reliable services
- creating a sustainable urban water future for the Hunter
- protecting people's health and enhancing the environment
- increasing our competitiveness and the value delivered to our community and our shareholders
- growing a vibrant workplace, achieving exceptional business outcomes.

2. Nature and scope of operations

Hunter Water Corporation is a State Owned Corporation (SOC), governed under the *State Owned Corporations Act 1989*. Hunter Water was corporatised in 1992 under the *Hunter Water Act 1991*. Prior to this, the Corporation was called the Hunter District Water Board, having its origins in the late 19th century.

The Corporation has two nominated shareholders, being the NSW State Government Treasurer and Premier of NSW. The Corporation is the parent entity in a group which includes a subsidiary – Hunter Water Australia (HWA). Each company is governed by an independent Board of Directors.

Hunter Water's primary purpose is to supply reliable and high quality water and wastewater services to the people of the lower Hunter region. Hunter Water's area of operation covers 5,366km² with a population of 533,874 in the local government areas of Cessnock, Dungog, Lake Macquarie, Maitland, Newcastle, Port Stephens and small parts of the Singleton and Great Lakes areas. As at 30 June 2010, there were 224,845 properties connected to Hunter Water's water network and 213,023 to the wastewater network.

Hunter Water's water sources and capacity include Grahamstown Dam (190,000 ML¹ capacity), Chichester Dam (21,500 ML), Tomago Sandbeds (60,000 ML) and Anna Bay Sandbeds (16,000 ML). Water is delivered via an extensive network of some 4,886 kilometres of pipes, 85 reservoirs and 123 pumping stations. Bulk water is supplied to MidCoast Water for supply to North Karuah. Hunter Water also has the capacity to supply up to an average of 35 ML per day to the Central Coast (depending on Hunter Water's storage levels).

Wastewater is collected through 4,714 kilometres of pipes and 404 wastewater pumping stations, delivered for treatment at one of our 18 wastewater treatment plants, then recycled where possible.

Stormwater management in Hunter Water's area of operations is predominantly the responsibility of local councils, with the Corporation owning and operating only some assets in the Newcastle, Lake Macquarie and Cessnock local government areas.

The Corporation is structured across seven divisions: Infrastructure Delivery, System Operations, System Strategy and Sustainability, People and Change, Business Services, Business Strategy and Communication, and Customers and Commercial Development. This structure facilitates the efficient coordination of the Corporation's operations across key functional areas, based on the Corporation's Strategic Business Plan.

Hunter Water Australia (HWA), established in 1998, provides a range of specialist technical and operational services to water agencies, Councils and industry, primarily in Australia. HWA pursues commercial sales in the areas of water and wastewater treatment operations and consultancy, engineering consultancy, survey and asset mapping services, laboratory analysis and advice, and corrosion engineering consultancy. As well as successfully marketing its services to external parties, HWA is also a key supplier of services to Hunter Water, managing both the wastewater treatment works and water treatment plants of the Corporation.

¹ One mega litre (ML) equals one million litres

As a subsidiary of HWC, HWA is governed by a Board of Directors nominated by the parent Board and approved by the parent's Voting Shareholders. The HWA Board is responsible for oversight of the company's business operations and is accountable to the shareholder for ensuring compliance with shareholder approved policies and delegations. The subsidiary's business plan is approved by the parent Board, which receives regular reports on performance. HWA's Board is responsible for risk management across the company with the risk profile updated biannually for review by the Board. The risk profile is also reported to the parent's Audit and Risk Committee.

3. Strategic directions

Hunter Water's strategies are focussed on the key areas of our Strategic Business Plan: Customers, Environment, Operational Excellence and Performance Culture. The broad strategic directions for the Corporation over the next five year planning period are as follows:

- Our workforce is critical in delivering both operational and strategic objectives. Safety remains our number one priority and we will continue to work on developing the Corporation's safety culture. We aim to grow a vibrant workplace, achieving exceptional outcomes, successful partnerships and personal satisfaction, and the ongoing development of our workforce is a key focus for the Corporation.
- Customer service is explicitly recognised as both a corporate objective and a strategic response to changing industry paradigms, including the opening of the industry to competition. We recognise that providing quality, value for money services and supplies to our customers is critical to our business success. Following the NSW Government's decision not to proceed with Tillegra Dam in November last year, in collaboration with the NSW Office of Water, we will look at alternative options for securing our water future through the development of the Lower Hunter Water Plan. We will engage the community so that a decision can be reached for a solution which is likely to include more recycling, water efficiency and a new water supply.
- We will continue to build our sustainable decision-making capability. The way forward will be a new world of trade-offs to achieve the best result for the environment and customers. As nationally we move toward a price on carbon, we will ensure plans are in place to provide direction for the business in a future carbon constrained environment. We will continue to focus on energy efficiency to deliver environmental and cost benefits.
- To achieve the dual objectives of providing value for money services to our customers and appropriate returns to our shareholder we will drive continual improvements in our business efficiency and effectiveness through responsible cost control and a focus on business process improvement and new opportunities.

4. Financial performance targets

Table 1: Annual financial performance targets (group, nominal \$)		2011/12 SCI	2012/13 Forecast	2013/14 Forecast
Total Income	\$m	288.3	316.0	365.4
Total Expenses	\$m	234.4	254.7	285.1
Earnings Before Interest & Taxes, Depreciation & Amortisation	\$m	161.7	184.4	229.1
Earnings Before Interest & Taxes	\$m	120.4	137.7	170.5
Operating Profit Before Income Tax Expense	\$m	53.9	61.2	80.3
Operating Profit After Income Tax Expense (NOPAT)	\$m	37.6	42.9	56.2
Target Dividend	\$m	26.4	30.0	39.3
Target Dividend Payout Ratio	%	70	70	70
Return on Average Assets	%	3.8	4.1	4.7
Return on Average Equity	%	2.1	2.3	3.0

Assumptions

- Modelling is based on the macro-economic forecast provided by NSW Treasury in February 2010.
- Pricing outcomes for 11/12 to 12/13 are based on the 2009 IPART Price Determination. Financial projections for future years are based on a real pre-tax rate of return of 7.4%.
- Target Dividend is based on 70% of NOPAT. The income tax rate assumed for the dividend calculation is 30% in accordance with NSW Treasury formula. The calculation of NOPAT for determining dividend distributions is normalised to exclude third party contributions received for expenditure on drought contingencies, and longer term water resource planning.
- Target dividend excludes the additional dividend requested by Treasury relating to the change in the government guarantee fee calculation methodology

5. Non-financial performance targets

Hunter Water operates in a highly-regulated environment with requirements to meet a broad range of performance standards set by regulatory agencies. These requirements all serve as performance targets for the Corporation and because of their regulatory nature, Hunter Water believes it must meet these targets in all but exceptional circumstances. In some cases, there are legislated penalties for non-compliance.

In full, these regulatory requirements are too numerous and complex to detail in this document - for example, the wastewater licensing process of the DECCW requires the monitoring of some 1400 parameters across 18 wastewater treatment plants. Table 2 provides a broad indication of the key regulatory requirements.

Other non-financial targets are:

- Safety – Hunter Water has extensive pipe systems located within public areas and the private property of customers. As most routine operations and maintenance activities take place in these areas, the safety of the community, contractors and Hunter Water’s employees is the number one priority. Hunter Water monitors its safety performance using the Serious Injury Frequency Rate (SIFR) as the primary indicator, which includes both lost time and medical injuries. Hunter Water also aims to achieve 100 per cent compliance with NSW government “*Working Together*” targets.

- Customer expectations – Hunter Water implemented a new customer reputation questionnaire in the second half of 2009/10 to improve the measurement of customer satisfaction with the services provided by Hunter Water. Key target measure as detailed in the Strategic Business Plan focus on honesty, reliability and overall customer satisfaction.

Table 2: Key regulatory requirements		
Instrument	Target area	Target
Operating Licence	Drinking water quality	<ul style="list-style-type: none"> • Meet Australian Drinking Water Guidelines as specified in licence
	Water supply	<ul style="list-style-type: none"> • Meet supply continuity and pressure standards specified in licence • Report to IPART on performance against environmental water quality requirements and water release requirements in licences issued by NOW
	Wastewater	<ul style="list-style-type: none"> • Meet sewer overflow standards set in licence • Report to IPART on performance with DECCW licence requirements for operation of wastewater treatment plants
	Customer and consumer obligations	<ul style="list-style-type: none"> • Meet requirements for community consultation and complaint management • Monitor customer service indicators
	Environmental management	<ul style="list-style-type: none"> • Prepare and implement an Integrated Water Resource Plan (H₂50) and report against progress annually. • Prepare and implement an Environmental Management Plan and report against progress annually. • Monitor environmental indicators and report status annually. • Produce Annual Catchment Report
DECCW wastewater system licences	Wastewater treatment works	<ul style="list-style-type: none"> • Meet individual treatment plant licence conditions on discharge quality, volume, load and pollution reduction programs
	Wastewater transport systems	<ul style="list-style-type: none"> • Meet system licence and pollution reduction program requirements
DECCW water management and access licences	Surface water extraction	<ul style="list-style-type: none"> • Meet Chichester Dam environmental flow conditions • Meet Seaham Weir operation and extraction conditions • Conduct surface water access studies as specified in licence
	Groundwater extraction	<ul style="list-style-type: none"> • Meet conditions on extraction from Tomago and Tomaree aquifers • Conduct aquifer monitoring to licence requirement • Conduct aquifer studies as specified in licence
MOU with NSW Health	Drinking water quality	<ul style="list-style-type: none"> • Provide monitoring and reporting information as required by Memorandum Of Understanding and Operating Licence • Meet emergency response requirements

6. Capital portfolio

Hunter Water assesses a range of social, regulatory, environmental and economic factors to ensure that capital invested in new assets and the replacement of ageing assets is in the best interests of the community.

Our objective is to provide sustainable water and wastewater services to our customers at minimum life cycle cost, whilst simultaneously meeting environmental and customer service standards in accordance with our regulatory framework.

In broad terms, the main drivers of forecast capital expenditure over the next four years of the SCI period (2011/12 to 2014/15) are:

- Growth – 51%,
- Regulatory/Statutory Standards – 27%,
- Business Decisions – 15%; and
- Government Programs – 7%.

As outcomes of these drivers, approximately 68% of the capital portfolio over the next four years is to be spent on new additional assets and 32% on the replacement of existing assets.

The main areas of expenditure over the four years will be on:

- the water supply system – 39% of the total Group capital portfolio;
- the wastewater system – 38%;
- corporate projects (including MARS) – 13%;
- recycled water projects – 9%; and
- the remaining 1% on HWA's capital portfolio.

Table 3 below displays the capital portfolio over the next four years by component, whilst Table 4 shows the split between key drivers, asset outcome and funding.

It is important to note that no allowance has been made at this stage for implementing outcomes of the Lower Hunter Water Plan following the decision not to proceed with Tillegra Dam.

The forecast capital expenditure for the four year period (2011/12 to 2014/15) for the parent entity in nominal terms is approximately \$912m, or \$871m in real 2011/12 terms.

Component		2011/12 SCI	2012/13 Forecast	2013/14 Forecast	2014/15 Forecast	Total
Water Supply	\$m	39.8	40.5	97.7	175.3	353.3
Wastewater Treatment	\$m	35.2	43.0	35.4	34.9	148.5
Wastewater Transport	\$m	38.5	38.8	51.5	75.5	204.3
Recycled Water	\$m	1.9	31.4	38.8	13.8	85.8
CTWSSP ¹	\$m	0.1	-	-	-	0.1
Other Corporate	\$m	16.7	26.9	46.6	29.8	120.0
Contingency		-	-	-	-	-
HWA	\$m	1.2	2.6	1.3	1.4	6.5
Total	\$m	133.2	183.2	271.2	330.7	918.4

¹ Country Towns Water Supply & Sewer Program

		2011/12 Forecast	2012/13 Forecast	2013/14 Forecast	2014/15 Forecast
Portfolio by key driver					
Growth	\$m	53.1	64.5	127.0	218.0
Regulatory / statutory standards	\$m	54.5	57.6	61.7	78.3
Business decisions	\$m	23.1	29.8	52.2	34.4
Government programs	\$m	2.6	31.3	30.3	-
Total	\$m	133.2	183.2	271.2	330.7
Portfolio by asset outcome					
Additional assets	\$m	80.3	127.1	182.8	238.0
Renewal of assets	\$m	52.9	56.1	88.4	92.7
Total	\$m	133.2	183.2	271.2	330.7
Portfolio by source of funds					
Budget funding	\$m	-	5.1	-	-
Borrowings	\$m	71.7	129.5	193.1	253.4
Other sources (includes internal funds) ⁽¹⁾	\$m	61.5	48.6	78.1	77.3
Total	\$m	133.2	183.2	271.2	330.7

Note: Disaggregation of expenditure is approximate only, due to the expenditures in many cases being for multiple purposes.

(1) Other Sources includes net profit after tax & dividends, third party and developer contributions, and Community Service Obligation (CSO) receipts.

Why are we making this investment?

- To conserve and secure our drinking water supply for the future, taking into account the uncertainties associated with climate change
- To provide capacity for a growing Lower Hunter population
- To meet environmental and customer service standards under our regulatory framework
- To reduce operating, maintenance and risk costs, and minimise the life cycle cost of our assets
- To reduce adverse impacts on our customers and the environment from our wastewater transport assets in wet weather
- To support business improvement initiatives eg better Information and Communication Technology (ICT) services

7. Accounting policies

In the preparation of its financial reports, Hunter Water complies with the *Public Finance and Audit Act 2010*, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board.

The financial statements also incorporate financial reporting requirements specified in the *Public Finance and Audit Regulation 2010*, and the relevant Treasurer's directions.

8. Social programs and non-commercial activities

Customer assistance programs

▪ *Community Service Obligations*

The Community Service Obligations (CSO) for which compensation is sought in 2011/12, in accordance with Treasury and other commitments, is outlined in Table 5 below.

Table 5: Annual CSO (nominal \$)		2011/12 SCI	2012/13 Forecast	2013/14 Forecast	2014/15 Forecast
Concessions to eligible pensioners who hold the appropriate Centrelink or Veterans Affairs Concession card and are the owner and occupier of the property to which the concession applies.	\$m	10.84	11.61	14.10	15.68
Exempt Properties (charities, public benevolent institutions etc).	\$m	1.56	1.66	1.98	2.17

Note: Modelling is based on the macro-economic forecast provided by NSW Treasury in February 2010.

▪ *Eligible pensioners*

Eligible pensioners receive a rebate of fixed and usage charges up to an estimated maximum of \$239 for the 2011/12 year for water/sewer properties, and \$119.50 for water only properties. In addition, the estimated annual Environmental Improvement Charge (EIC, \$34.81 from July 2011, in 2011/12 terms) is also waived. The eligible pensioner rebate is fully funded by the Government.

In 2009 after reviewing issues of affordability, the NSW Government further agreed that the pensioner rebates increase over the price path period. The rebate will increase to \$250 in 2012/13 (in 2011/12 terms). The rebate has been calculated as 26 per cent of the average customer's water and sewer bill, consuming 200 kL of water per year.

- *Exemption Eligibility*

Customers termed "Exempt" are historically non-profit properties owned or occupied by religious bodies, public benevolent institutions or charities. Commercially owned and operated premises do not qualify for exempt status. Exempt concessions are granted in three ways:

- a) Reduction of Fixed Service Charges
- b) Waiving of the EIC
- c) Provision of a Usage Allowance in certain circumstances (nursing homes / hostels with exempt status).

This rebate is fully funded by the Government.

- *Kidney dialysis customers*

Hunter Water recognises that certain customers require additional water to maintain their health because they are dialysis patients and are able to dialyse from their own homes. These customers are offered financial support in the form of the dialysis rebate. This rebate is fully funded by the Government and included in the Exempt Properties CSO in Table 5 above. The Renal Unit of Hunter New England Area Health provides Hunter Water with the details of customers who are required to dialyse at their own home.

The rebate provides a free "water allowance" of 250 kilolitres per year. The rebate is split and applied to each account.

Backlog sewer programs

- *Priority Sewerage Program*

The Government established the Priority Sewerage Program (PSP) for providing backlog sewerage services to un-sewered townships in the areas of operation of Sydney Water, Hunter Water, Gosford City Council and Wyong Shire Council.

The current program in the Hunter was based on environmental and health need priorities set by the then Environment Protection Authority (now the Department of Environment Climate Change and Water) to evaluate and prioritise townships for backlog sewer services. Following this assessment, Hunter Water examined the technical and financial considerations and recommended a program to the Government.

Five villages in the Hunter – Fern Bay, Kitchener, Lochinvar, Millfield and Ellalong – were approved by Government for servicing under the PSP between 2002 and 2004. Funding via CSO subsidies was received in 2004/05 to 2007/08. Works on these projects have now been completed.

- *Country Towns Water Supply and Sewer Program*

The Government committed a funding contribution in the 2007 State Budget to provide sewer services to Clarence Town under the Country Towns Water Supply and Sewer Program (CTWSSP). This funding commitment was originally made to Dungog Shire Council but was transferred to Hunter Water in July 2008 when Dungog Council's water and sewer operations were transferred to Hunter Water.

Funding assistance under the CTWSSP for both the reticulation and treatment plant components of the Clarence Town scheme have been approved by the Minister for Water. The Minister has advised that actual assistance payments will not be made until after July 2012.

The timing of funding receipts outlined in Table 6 below reflects the expected expenditures on both the reticulation and treatment components.

Grant Due	Scheme	Capital Expenditure	Country Towns Water Supply and Sewer Program Grant From Treasury	Scheme Completion
2012/13	Clarence Town Reticulation	\$4.250m	\$2.529m	2010/11
2012/13	Clarence Town Treatment	\$4.336m	\$2.580m	2010/11
Total		\$8.587m	\$5.109m	

Government directives

(under Section 20p of the State Owned Corporations Act 1989)

Following the decision to terminate the Government directive of the Tillegra Dam project under section 20P of the State Owned Corporations Act 1989, only one project, the Kooragang Island Recycled Water Scheme, remains. Projected expenditure on this scheme is shown in Table 14 'Major Project Listing' in the Strategic Business Plan.

9. Financial asset and liability management

Hunter Water's objectives in financial asset and liability management are in accordance with NSW Treasury management policies to achieve an optimum cost of funds within defined risk parameters, including the identification of a Risk Neutral Benchmark. Hunter Water's debt portfolio is held with NSW Treasury Corporation (TCorp).

In respect of the Financial Asset Portfolio, funds are invested through an 11am Deposit Account held with NSW TCorp.

To allow flexibility in managing daily working capital requirements, an overdraft facility of \$10m (called a "Come and Go" facility) is in place with TCorp. This facility is accessed as required to fund any short term working capital requirements.

TCorp is contracted by Hunter Water to manage its Financial Asset and Liability Portfolios. As at 1 December 2010 TCorp have taken on a more active role with Hunter Water Corporation in a strategic advisory and management role. One of their key principles is to

source the cheapest cost of debt and minimise risk by better matching our debt maturity to the business's underlying assets.

Hunter Water's current investment powers are in accordance with Part II of the *Public Authorities (Financial Arrangements) Act 1987*.

On the basis of expected future capital works, \$411m of new borrowings may be required over the coming three year period of this SCI. This is below the net increase of \$694m flagged in last year's SCI over the same period. The large decrease in expected borrowings is due to the cancellation of the Tillegra Dam project.

Hunter Water will seek approval for a maximum Global Borrowing Limit of \$925m for 2011/12 from the Treasurer. TCorp will provide advice on appropriate structures and ongoing strategies for the portfolio. Future limits will be revised on an annual basis in line with debt levels flagged in the SCI process.

Key indicators are shown in Table 7 below.

Table 7: Key indicators (group, nominal \$)	2010/11 Budget / benchmark	2011/12 Budget/benchmark
Total interest cost	\$42.5m	\$51.3m
Average yield cost	6.0%	5.95%
Total Government guarantee fee	\$17.6m	\$15.7m
Modified duration of benchmark portfolio		
- Existing Nominal debt	N/A	N/A
- New nominal debt (target range 70-100% of total portfolio)	6.25 years	6.25 years
- Inflation-linked debt (target range 0-15% of total portfolio)	12.8 years	12.8 years
- Floating rate debt (target range 0-15% of total portfolio)	0.25 years	0.25 years
Total investment income	\$0.4m	\$0.5m
Rate of return on cash	3.70%	4.70%

10. Risk management and internal control overview and impacts

Risk management is taking on increasing importance in the rapidly changing commercial business world. The historical concentration on assessment of safety and financial risk is no longer sufficient to meet the needs of evolving companies and, with the impending emergence of competition and increasing research on potential effects of climate change within the water industry, we have a clear imperative to determine a risk management methodology which will address all of our corporate needs.

Hunter Water has responded proactively to this imperative and considerable effort has been expended on the development of an Enterprise Risk Management Framework for progressive implementation across the entire Corporation. This Framework is consistent with

ISO 31000 and provides a transparent and consistent approach to risk management, as well as standardised documentation and terminology. A suite of tools has been developed to enable assessment comparability across Divisional boundaries and a staged implementation plan developed to ensure the knowledge transfer process is managed effectively.

The framework is designed to integrate risk management into every component of Hunter Water's activities. It commences with a structured analysis of the corporate Strategic Business Plan by the senior management team and Board of Directors. It continues this corporate focus by analysing key areas such as fraud and environmental sustainability, and plans are currently underway to further integrate our strategic risk management approach into our asset management framework.

As part of its ongoing risk identification, assessment and management activities, Hunter Water continues to actively establish, refine and review controls which reduce the impact and likelihood of adverse events. There are some key risks, which if not closely managed, could affect shareholder value, and various controls and management strategies have been established to mitigate these risks. Details of those risks assessed as high, after taking all existing controls into account, are outlined in Table 8 below.

Information gathered during the risk assessment process enables a 5-year Internal Audit Plan to be customised to the risk based requirements of Hunter Water. Detailed examination of the potential risks and the effectiveness of existing controls provides invaluable information utilised to target specific vulnerabilities within the organisation. Prioritisation of audits within the plan is based upon:

- the controlled level of risk agreed upon by the senior management team in their annual risk assessment of the business's strategic objectives;
- the inherent risk level comparative to the controlled level of risk, to take into account the relative importance of internal controls;
- the results of the Corporation's biennial Fraud Risk Assessment; and
- other considerations, such as the extent of external monitoring (e.g. by Regulators) and the date and result of prior audits.

The Plan is updated annually and approved by the Board's Audit and Risk Sub-committee. Progress against the Plan is reported to the Committee's quarterly meetings. Audit reports are prepared for all internal audits conducted. Reports include an overall assessment of the control system subject to review. Each issue raised is assigned a risk rating of high, medium or low. Recommendations for improvement are discussed with relevant management and agreed audit actions are recorded in final reports which are tabled at the Audit and Risk Committee. Progress against these actions is monitored by the Audit and Risk Management Team and reported quarterly to the Audit and Risk Committee.

The responsibilities and role of the Audit and Risk Committee are documented in the Committee's Charter, which is compliant with Treasury policy TPP 09-5 *Internal Audit and Risk Management for the NSW Public Sector*. The Charter sets out the Committee's authority, as delegated by the Board. The Committee reviews the Charter annually with any changes approved by the Board. As required by the Charter, the Committee consists solely of independent directors appointed by the Board's Corporate Governance Subcommittee. The Chairman may not be the Chairman of the Board. The Audit and Risk Management Team functionally reports to the Chairman of the Audit and Risk Committee and the

Chairman participates in the selection of the Team's Manager whose performance is reviewed annually by the Committee.

Under its Charter, the Audit and Risk Committee's purpose is to assist the Board in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control, the risk management framework and risk profile, the audit process, and the Corporation's process for monitoring compliance with laws, regulations and Corporation policy. The Committee also has oversight over the Corporation's Fraud and Corruption Control Strategy.

Risk	Description	Risk indicator/ target	Potential impact on SCI targets	Risk management action, responsibility and time frames	Target level for indicator
Recycled water distribution	A significant segment of the recycled water user market is lost and is unable to be replaced in a timely manner. Decreased levels of recycled water demand then result in increased discharge of effluent to the environment and underutilisation of major recycled water infrastructure.	<ul style="list-style-type: none"> • Volume of recycled water used per annum 	<ul style="list-style-type: none"> • Reduced revenue • Increased capital expenditure 	<ul style="list-style-type: none"> • Conduct a commercial risk assessment of critical recycled water users – Manager Product Development – 30/12/2011 	<ul style="list-style-type: none"> • 4GL of recycled water used p.a.
Source infrastructure reliability	Source infrastructure experiences a significant breach resulting in the unplanned expulsion of considerable volumes of water.	<ul style="list-style-type: none"> • % of prescribed dam inspections completed 	<ul style="list-style-type: none"> • Increased operating costs, reducing operating profit • Increased capital expenditure 	<ul style="list-style-type: none"> • Review maintenance strategies for top 5 asset classes - Manager Asset Management - 30/12/2011. • Develop asset risk profile - Manager Asset Management - 30/12/2011. 	<ul style="list-style-type: none"> • 100% of prescribed dam inspections completed p.a.
Safety in the workplace	Unsafe work environment or practices result in escalated levels of injury.	<ul style="list-style-type: none"> • Number of Lost Time Injuries (LTI) • Number of Medical Treatment Injuries (MTI) • Number of First Aid Injuries (FAI) 	<ul style="list-style-type: none"> • Increased operating costs, reducing operating profit 	<ul style="list-style-type: none"> • Review OHS Strategy – Manager, OHS - 30/06/2011. 	<ul style="list-style-type: none"> • 0 LTI • 50% reduction in MTI • 20% reduction in FAI

Table 8: Major risks and actions

Risk	Description	Risk indicator/ target	Potential impact on SCI targets	Risk management action, responsibility and time frames	Target level for indicator
Imbalance in water supply/demand	Yield from existing water supply sources is insufficient to meet demand resulting in the introduction of restrictions and commissioning of interim supply source	<ul style="list-style-type: none"> Water demand vs sustainable yield 	<ul style="list-style-type: none"> Increased operating costs, reducing operating profit Increased capital expenditure Reduced revenue 	<ul style="list-style-type: none"> Develop the Lower Hunter Water Plan – GM SSS – 31/12/2013 Revise the Drought Management Plan – Manager Water Resources – 31/03/2012 	<ul style="list-style-type: none"> In balance

Table 9: Key audit actions and their implementation

Key audit action	Risk addressed	Completion deadline	Status of audit action and comment on progress
Upgrade the risk management procedure in the OHSMS to more comprehensively include all related tools and forms	Safety in the workplace	30 June 2011	This is on track to be completed by the due date.
Update the risk management training requirements to ensure consistency with the upgraded procedure	Safety in the workplace	30 June 2011	This is on track to be completed by the due date.
Compile a comprehensive risk profile of safety issues	Safety in the workplace	31 December 2011	This is on track to be completed by the due date.
Develop procedures for pump station inspections	Safety in the workplace	30 June 2011	A set of draft procedures is available. It is anticipated that these will be finalised by the end of the 2010-11 financial year.

Key audit actions are considered to be those assessed as being of high risk.

11. Statement addressing shareholder issues

Hunter Water meets with Treasury representatives on a bi-monthly basis to discuss progress against the SCI commitments and any other strategic issues as they arise.

In addition to the quarterly progress reporting, Hunter Water provides monthly reports to Treasury on key financial indicators, including commentary on key variances.

12. Quarterly and half yearly reports

Hunter Water Corporation's Board of Directors acknowledges quarterly and half yearly reporting obligations. A half yearly report will be submitted to the Treasurer one month after the end of the first six months of the financial year, containing a report on operational performance against obligations set by Hunter Water's Operating Licence, as well as an Income Statement, Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, and Statement of Cash Flows.

The financial statements contained within the half-yearly report are unaudited General Purpose Reports prepared in accordance with AASB1029 "*Interim Financial Reporting*".

13. Other information

Other information which Hunter Water will provide to NSW Treasury on behalf of the voting shareholders during 2011/12 includes:

- Forecast financial information requested by Treasury e.g. five year forward estimates (FISTOES), annual financial statements (including FISTOES) and forecast capital works program (CAPTOES)
- Forecasts of all financial distributions and tax equivalents requested by Treasury (Return on Dividend and Income Tax)
- Reporting on capital projects via the Major Capital Projects Reporting System (MCPRS)
- Submissions for Projects of State Significance

14. Representation and commitment statement

The Board of Hunter Water Corporation confirms the following:

- The performance targets within the SCI are based on and supported by the Corporation's Business Plan.
- The Corporation has a Strategic Asset Management Plan, which is as far as practicable consistent with the principles of the *Total Asset Management (TAM) requirements for updating the NSW State Infrastructure Strategy (SIS) (TPP 08-2)* and the *NSW Government Procurement Policy (TPP 04-1)*. Its asset maintenance policies and processes are adequate and appropriate to manage and control risks associated with physical assets.
- The Corporation is aware of the requirements of *Ministerial Memorandum No. 2005-9, Major Infrastructure Coordination and Delivery* and will comply with these requirements if not contrary to the objectives of the Corporation.
- The requirements of the *Financial Appraisal Guidelines (TPP 07-4)* have been complied with for capital expenditure projects proposed to commence in 2011/12.
- All known 'key risks' and 'major emerging contingent liabilities' which could materially impact the current and future results of the Corporation have been disclosed.

- As a SOC, the Corporation will comply with NSW Treasury Circulars on accounting policy matters applicable to SOCs, as listed in Attachment 1 of the *Guidelines for Developing the 2010-11 Statement of Corporate Intent and Statement of Business Intent*.
- The Corporation is aware of the internal audit and risk management policy outlined in NSWTC 09/08 *Internal Audit and Risk Management Policy* and the associated TPP 09-5 *Internal Audit and Risk Management Policy for the NSW Public Sector*. The Corporation has demonstrated its own practices are consistent with standards recommended for Australian Securities Exchange (ASX) listed companies and where appropriate, has applied any additional requirements that are set out in NSWTC 09/08.
- The requirements of the *Treasury Management Policy* (TPP 07-7) have been complied with and related party interests, which may represent a possible conflict of interest for Directors, have been disclosed.
- The Corporation will comply with the requirements of *Ministerial Memorandum No. 2007-12 NSW Public Sector Wages Policy 2007*.
- The Corporation will comply with the requirements of *Ministerial Memorandum No 2010-07, Working Together: Public Sector Workplace Health and Safety and Injury Management Strategy 2010-2012* (or any future memorandum that supersedes M2010-07).
- The Corporation will comply with the requirements of *Premier's Memorandum No. 2009-04, Official Travel within Australia and Overseas*.
- The Corporation's Chief Executive Officer has an employment contract and performance agreement. The employment contract is appraised annually with the next appraisal scheduled for (September 2011).
- The Corporation's Board agrees to provide the voting shareholders with financial and other information, including information on major capital expenditure projects, on a quarterly basis to assess the performance against commitments in this SCI and to assess the value of the shareholders' investment in the business.
- The Corporation's Board agrees to comply with section 3.4 (Continuous Disclosure) of the *Reporting and Monitoring Policy for Government Businesses (TPP 05-2)*.
- Projects of State Significance have been identified in accordance with the criteria set down in the *Guidelines for Assessment of Projects of State Significance (TPP 02-4)*. In-principle approval from Cabinet Standing Committee on the Budget ("Budget Committee") and final approval from the voting shareholders be sought for Projects of State Significance planned to commence in 2011/12 if required.
- The Corporation will comply with the requirements of Premier's Memorandum No. 2010-03 *Strengthening Aboriginal Employment Opportunities and Community Partnerships*.
- The Corporation will comply with the requirements of Premier's Circular C2009-08 *The Local Jobs First Plan*.

15. Contract, performance agreement and annual appraisal for the chief executive officers

In accordance with Section 21(7) of the *State Owned Corporations Act 1989*, the Board of Hunter Water Corporation confirms the following:

- That the Chief Executive Officer has an employment contract and performance agreement.
- That the Chief Executive Officer's performance is appraised at least annually under the terms of the employment contract and performance agreement.
- That the employment contract and performance agreement of the Chief Executive Officer include as a minimum:
 - the duties of the Chief Executive Officer's position, including major tasks and accountabilities;
 - monetary remuneration and employment benefits for the position; and
 - performance criteria for the purposes of annual reviews of the Chief Executive Officer's performance.

The Chief Executive Officer's performance appraisal is performed on an annual basis in September following finalisation of the end of financial year.