



Budapest Sewage Works Ltd.



Business report 2006

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Introduction

The Budapest Sewage Works Ltd. (Fővárosi Csatornázási Művek Zrt., hereinafter “the Company”) has been successful in the fields of development of sewage disposal and treatment, increasing operational safety as well as environment protection throughout the past year.

The Company has spent more than ever (HUF 8.4 billion) on investments, despite the fact that the investment works of the North-Pest digestion unit were delayed to next year. It was primarily the network reconstructions that increased, the renovated network length was 24.2 km, exceeding the previous year's length by 4.4 km (22.2%). In the meantime, the value of sewer constructions reached HUF 5,278 million, increasing by HUF 1,170 million (28.5%) as opposed to the 2005 level. The modernization of the treatment plants went on. The energy self-sufficiency of the South-Pest plant increased and a great stride forward was achieved in the field of waste treatment and management. In the North Pest plant, the construction of the main sewer draining the wastewater from North-Buda and located under the river bed was finished as well as the preparation of the increase of the nutrient removal degree started.

55% of sewage invoiced was treated both biologically and chemically and the removal of nutritive matter was also full in 16%, while partial in 39%. The fact that both wastewater treatment plants have functioned continuously and efficiently has meant a great stride forward in the field of wastewater treatment. The parameters of the effluent water of our wastewater treatment plants have remained within the threshold limits. The quantity of collected wastewater and rainwater fell short of the previous year's value by 9.2%, more precisely the invoiced wastewater quantity fell short of the previous year's value by 6.5%.

The 2006 rainwater surplus caused severe floods and surface waters in our country and in neighbouring countries. Flood protection was necessary four times on the Budapest section of the Danube. The greatest flood in both time and runoff lasted from March 29 to April 14. Since water level data are recorded, this was the highest ever measured ice-free flood during which the Government decreed an extraordinary flood-protection state of emergency on the Hungarian section of the Danube.

The Company continued to work according to its quality assurance and environment focused control system under ISO 9001:2000 and ISO 14001 standards in 2006 as well.

The basic administration and technical tasks have been fulfilled under balanced financial conditions. As the collective result of savings in costs and revenues, the profit after tax of the Company reached HUF 3.3 billion. During the year, the financial situation of the Company remained solid – despite the drastic decrease of the invoiced wastewater quantities – and it has retained its continuous liquidity. In conclusion, it can be stated that the Company – taking into account its existing technical and financial possibilities – operated the public utilities efficiently and successfully in 2006 as well.

Budapest, March 2007

György Palkó
General Manager

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Organization and legal position of the Company

The General Assembly of the Municipality of Budapest transferred shares representing 25% + one vote of the Company's asset and specific operating and management control rights to a consortium formed by Berliner Wasser Betriebe (B.W.B.) and Compagnie Générale des Eaux (C.G.E.) for a period of 25 years. The contract was signed on 19 November 1997. In accordance with the Share Purchase Agreement, C.G.E. and B.W.B. established Csatorna Holding Vagyonkezelő Zrt. at the end of 1998.

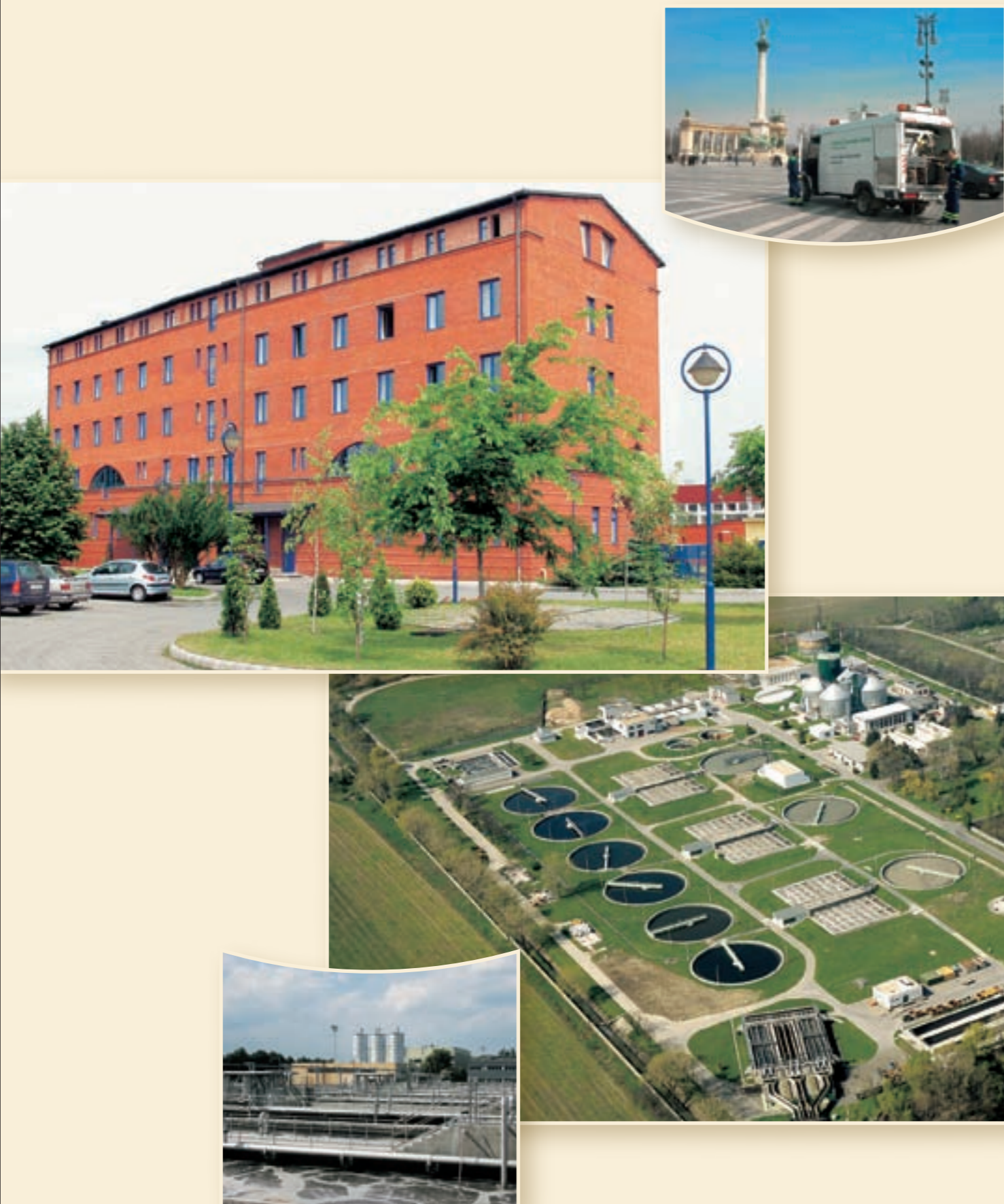
In the meantime, C.G.E. changed its name to Vivendi. On 6 June 2000, B.W.B. transferred its shares to Berlinwasser Holding AG.

On 26 March 2002, Vivendi transferred its shares – with indicating intermediate ownership of Vivendi Universal – to Vivendi Environnement, whose current name is Veolia Environnement S.A.

Owners: The Municipality of Budapest
Berlinwasser Holding AG
Veolia Environnement S.A.
Csatorna Holding Vagyonkezelő Zrt.
3 small investors

Name of the Company: Budapest Sewage Works Ltd.
Address: H-1087 Budapest, Asztalos Sándor str. 4.
Postal address: 1426 Budapest 72. PO Box 114.
Telephone: (+36 1) 455-4100
Fax: (+36 1) 455-4232
E-mail: vezig@fcsm.hu

Board of Directors: Kálmán Pákozdi – chairman
Sándor Bódás
Philippe Guitard
György Palkó
Ferenc Szűcs
Bernt Thümmel
Karl-Heinz Zorn



Supervisory Board:	January – February 14, 2006:	February 14 – December 31, 2006:
	Dieter Ernst – chairman	Dieter Ernst – chairman
	László Fecher	László Fecher
	Veronika Gólya	Veronika Gólya
	Antal Hőnigh	Antal Hőnigh
	Péter Lakatos	László Kollár
	dr. László Nyolczas	Péter Lakatos
	József Oláh	dr. László Nyolczas
	Étienne Petit	József Oláh
	Ágoston Péterffy	Étienne Petit
	Imre Rusznák	Ágoston Péterffy
	László Zsinka	Imre Rusznák
		László Zsinka

Independent auditor: Ernst & Young Kft.
Represented by: István Havas

Management:

György Palkó	Zsuzsanna Gubányi	Bernt Thümmel
General Manager	Deputy General Manager	Technical Deputy Manager

The person of the Deputy General Manager changes from January 1, 2007. dr. Éva Medovárszki fulfils this task instead of Zsuzsanna Gubányi.

Company organization

Based on the new legal dispositions, the company was transformed to a private limited company in 2006. The basis of the Company's current organizational structure was set up on 1 October 1998. Some organizational changes have taken place in 2006.

In compliance with the tasks, the international organization and names have changed at the Customer Services Department. The name of the Customer Services Department changed to Sales Department. The Accounts Administration Group was renamed to Invoicing and Accounts Management Group and the organization was shifted to the Sales Department. The Special Customer Group was named Accounts Receivables Management Group. The Customer Service and Invoicing Department was renamed Customer Services Department.

In compliance with the new tasks, the Research and Development Group was created within the Environment Protection Department during the year 2006, which deals primarily with the enhancement of the efficiency of applied technologies and the development of new technologies and methods.

Within the Network Maintenance Department of the Maintenance Department, the 3rd Network Maintenance Group was dissolved. Major modifications are made in this field from January 1, 2007. Accommodated with the new tasks, the name of the Maintenance Department was changed to Maintenance and Contracting Department and the Network Maintenance Service is dissolved, while the Network Maintenance Group I. and II. are incorporated into the Network Department.

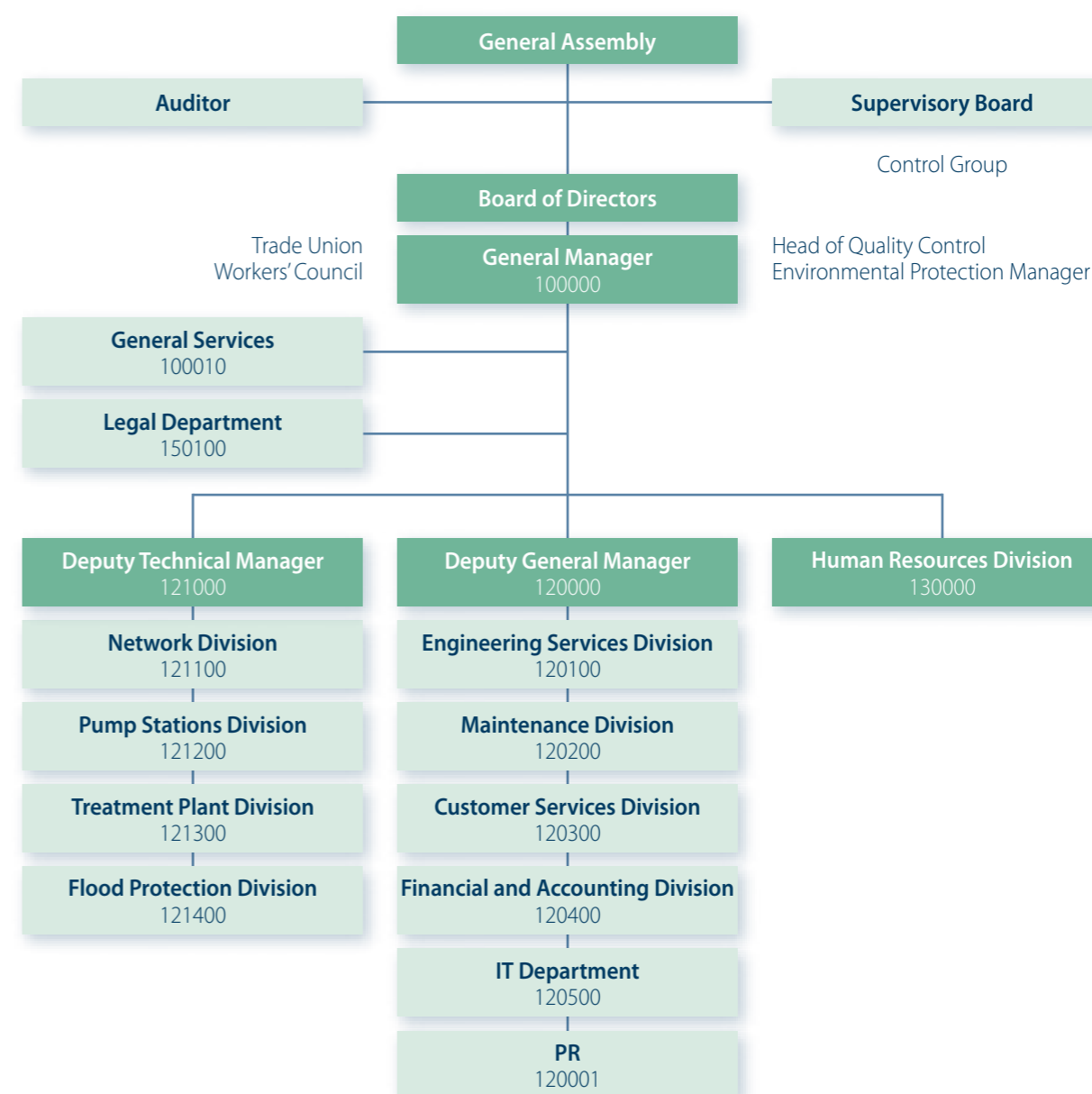
Territorial location of the Company

The management of the Company, all its functional organizations, as well as the Network Department are all located on a site that can be considered the core, in the 8th district of Budapest, at Asztalos Sándor str. 4, Kerepesi str. 19 and Kerepesi str. 21.

The IX. Soroksári site can be considered a basic site where the offices Flood Protection Department and the Trade Union can be found.

The Pump Stations Department and the Treatment Plant Department are physically located at the site where the tasks are fulfilled.

Organizational structure of the Budapest Sewage Works Ltd.



Scope of activities

The Municipality of Budapest has founded the Company to collect, treat wastewater and rainwater generated in the area of Budapest and to discharge them into the receptor. The rights and obligations related to the task are regulated by the Public Service Agreement concluded between the two parties on 3 November 1997.

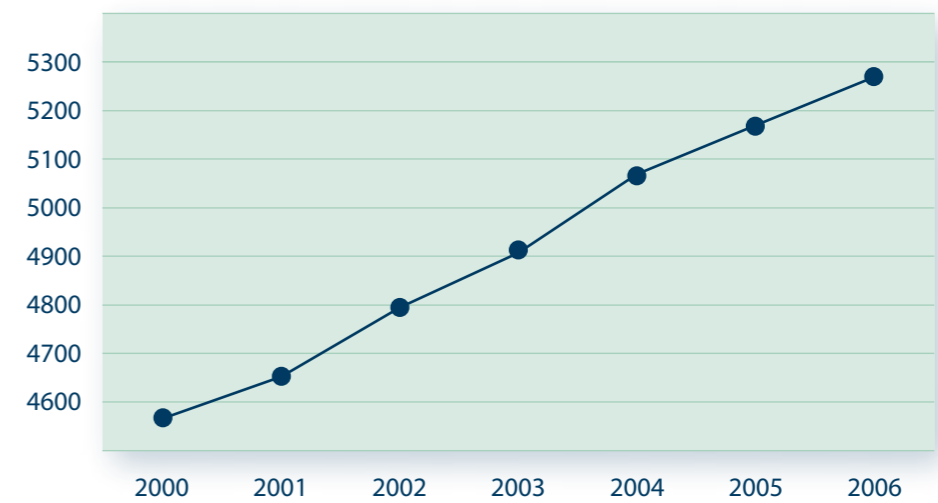
The Company has been organized exclusively for collecting and treating wastewater and rainwater. Although the Company serves only Budapest, sewers of some settlements outside the boundary of the capital are also connected to its network, based on the principle of their location in the drainage area.

As the Company provides a public utility service, it is a basic requirement that the service must be continuous and safe. The fulfilling of the task, the supply of the service is also a mandatory obligation of the organization mandated with the task. (Partial service provision obligation.)

The most important rules regarding the core activity are included in Government Decree 38/1995. (IV.5.) and its amendments.

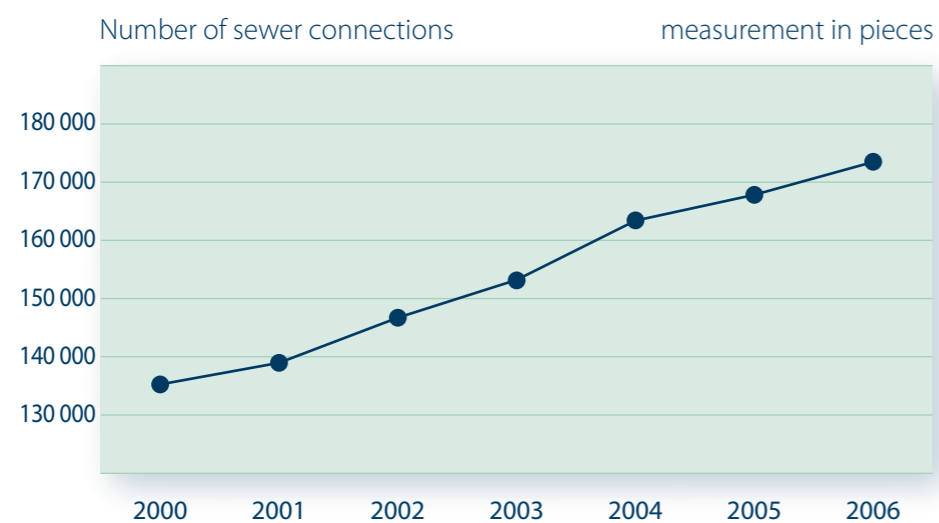
Beyond our core service, our Company provides another public service: we operate the flood and inland water control system of Budapest and make suggestions on the development of the flood protection installations.

Length of the sewage network in km



Main indicators of the sewage works

Description	unit	2002	2003	2004	2005	2006
Capacities on 31 December						
Length of the sewage network	km	4 799	4 915	5 075	5 179	5 282
- out of this: annual increase	lm	133 811	116 170	159 960	104 364	103 186
Number of sewer connections	pcs	148 551	154 031	162 753	167 949	173 660
- out of this: annual increase	pcs	6 205	5 480	8 053	5 196	5 711
Biological treatment capacity	thm ³ /day	280	280	280	280	280
- out of this: - South-Pest plant	thm ³ /day	80	80	80	80	80
- North-Pest plant	thm ³ /day	200	200	200	200	200
Nutrient removal capacity	thm ³ /day	80	80	80	80	80
Annual performance						
Collected sewage and rainwater	thm ³	240 871	224 203	248 162	259 538	235 540
- out of this: - discharged via free outlet	thm ³	27 798	26 400	25 298	25 439	24 000
- discharged via pump stations	thm ³	213 073	197 803	222 864	234 099	211 540
- out of this: - with biological treatment	thm ³	52 776	76 714	77 352	76 834	76 835
- nutrient removal	thm ³	20 701	20 932	22 066	21 862	22 085
Billed sewage	thm ³	159 192	153 785	150 542	149 527	139 873
- out of this: households	thm ³	99 534	96 667	95 996	98 188	91 705
industrial, corporate + other	thm ³	53 013	51 024	51 397	49 416	46 328
private well	thm ³	6 645	6 094	3 149	1 923	1 840



Equity position

Liabilities and equity

The initial asset structure and current capital structure of the Company was established on January 1, 1993. In 1996, decision 1406/1996. (X.31.) of the General Meeting decided on the capitalization of the sewer network operated by the Company. From this date, the value of the registered capital is HUF 70,045,200 thousand, and since 19 November 1997, 25% of the share capital (HUF 17,511 million) was transferred to foreign investors.

Equity (on December 31, 2006)

in thousand HUF

Description	2005	2006
Share capital	70 045 200	70 045 200
Capital reserve	13 556 590	13 556 590
Profit reserve	9 419 876	10 232 795
Revaluation reserve	-	-
Balance sheet profit figure	812 919	91 913
Equity total	93 834 585	93 926 498

The profit reserve has increased by the balance sheet profit of 2005 (HUF 813 million). No other change has occurred in 2006.

The 2006 balance sheet profit figure was determined by the fact that the profit before tax was HUF 5,006 million. After corrections with the items modifying the tax base and taking into account the additional tax, HUF 1,695 million was paid as tax, which resulted in HUF 3,311 million profit after tax. Decreasing the after tax profit with the HUF 3,219 million paid in dividends, the net profit of the Company in 2006 reached HUF 92 million.

The aggregate amount of the equity on 31 December 2006, amounted to HUF 93,926 million, exceeding the previous year's by HUF 92 million.

Changes in the composition of equity (on December 31, 2006)

Description	2005		2006	
	in thousand HUF	% ratio	in thousand HUF	% ratio
Working capital	10 188 319	10,9	8 945 973	9,5
Fixed assets	83 646 266	89,1	84 980 525	90,5
Equity total	93 834 585	100	93 926 498	100

Within the equity, the proportion of fixed assets increased to 90.5%, while the proportion of working capital decreased to 9.5%. The surplus of HUF 92 million in equity compared to the previous year decreased the working capital by HUF 1,242 million and increased the fixed assets by HUF 1,334 million.

Among the assets, the provisions for expected losses decreased by HUF 367 million in 2006. The change has occurred due to the following reasons. In 2005, the Company released its provisions for wastewater penalties, HUF 585 million and has constituted a provision for its wastewater penalty expected for the current year in the amount of HUF 1,020 million. The effect of the settlement of the environmental load tax affecting previous years is a change in provisions of HUF -786 million. In accordance with the international requirements, the provision of the current year for the coverage of defined personnel-type liabilities for the coming years was HUF 53 million, while the release of the previous year was HUF 37 million.

The long-term liabilities are figured in the balance sheet in the amount of HUF 37 thousand which is the part of the payable dividend of 2006 lessened by the dividend advance.

Short-term liabilities have been increased by HUF 621 million. Supplier – primarily investment supplier – payables decreased by HUF 121 million. Other short-term liabilities have increased by HUF 742 million due to the effect of the increase of the environmental load tax and VAT.

Accruals in 2006 reached HUF 13,798 million. These are:

■ Cost deferral:	HUF 31 million
■ other assets and assets received without payment:	HUF 4,641 million
■ cash taken over for development purposes:	HUF 9,126 million
out of this: from district municipalities:	HUF 270 million
From the Municipality of Budapest:	HUF 371 million
public utility development contributions:	HUF 8,340 million
from other sources:	HUF 145 million

The liabilities of the Company have increased in total by HUF 2,586 million in comparison to the previous year.

Balance sheet as of December 31, 2006

in thousand HUF

Description	2005	2006
Assets		
Intangible assets	51 072	66 427
Fixed assets	94 828 986	98 884 100
Long-term financial assets	147 596	355 250
Inventory	166 857	199 313
Receivables	3 964 502	4 293 891
Securities	6 850 353	3 773 072
Cash and bank	257 327	1 268 140
Prepayments	2 528 165	2 541 020
Assets total	108 794 858	111 381 213
Liabilities and equity		
Equity	93 834 585	93 926 498
Provisions	1 965 351	1 598 745
Long-term liabilities	244 133	37
Short-term liabilities	1 437 050	2 058 045
Accruals	11 313 739	13 797 888
Liabilities and equity total	108 794 858	111 381 213

Assets:

The level of assets was HUF 2,586 million higher than on December 31, 2005, with the following composition:

- The value of intangible fixed assets increased by HUF 15 million due to purchases.
- Due to the cumulative impact of investments and write-offs in the reporting period, the value of fixed assets increased by HUF 4,055 million.
- The value of long-term financial investments was HUF 208 million higher than in the previous year. In 2006, the Company did not have any new investments, but it acquired a HUF 200 million stake in Érd and Environs Regional Waterworks Ltd.
- Inventory increased by HUF 32 million in comparison to the same period of the previous year.
- Receivables increased by HUF 329 million. Within this, – including VAT increase – trade receivables increased by HUF 730 million (see detailed analysis in the financial chapter), while other receivables decreased by HUF 401 million.

■ The amount of securities decreased by HUF 3,077 million, of which HUF 1,011 million was embodied in cash and bank. Further decrease was primarily due to the increase of the payment obligations arising from the changes in the regulating system.

■ The value of cash and bank increased by HUF 1,011 million.

■ The level of accruals and prepaid expenditures was HUF 13 million higher than on December 31, 2005. This was due to the increase of accrued income by HUF 32 million and the decrease by HUF 19 million of the prepaid expenditures.

Further analysis of the assets indicates that 89% of our Company's assets are represented by fixed assets. 92% of the fixed assets consist of real estate and structures.

Fixed assets on December 31, 2006 in thousand HUF

Description	Properties	Machinery, equipment and vehicles	Other equipment and vehicles	Investment and advance payment	Total
Gross value	125 644 030	13 022 729	1 804 897	2 733 739	143 205 395
Depreciation	34 262 303	8 764 390	1 294 602	0	44 321 295
Net book value	91 381 727	4 258 339	510 295	2 733 739	98 884 100

Details of properties on December 31, 2006 in thousand HUF

Categories	Gross value	%	Net value	%
Sewer	104 922 977	83,5	74 314 304	81,3
Other ground structures	11 118 526	8,8	8 404 095	9,2
Land	3 361 608	2,7	3 361 608	3,7
Other buildings	6 240 919	5,0	5 301 720	5,8
Total	125 644 030	100,0	91 381 727	100,0

Besides its own assets, the Company also operates:

■ assets withdrawn when the Company was established (December 1, 1993): HUF 68,932 thousand,

■ sewers owned by district municipalities and the Municipality of Budapest HUF 1,788,291 thousand,

■ sewers established by using the development fund and sewers owned the city and capitalized since 1997: HUF 39,107,330 thousand (excluding apartment value replacement, and basic handover).

The gross value of third parties' properties and operated by the Company in 2006: HUF 40,964,553 thousand.

Technical specifications of the sewage works

The installations of the sewer system serve the public service collection and treatment of wastewater and rainwater generated in the area of Budapest and their discharge into the receptor. Some of the facilities at the sewage works provide for collecting sewage (through the network and the intermediary pump stations) and some for transferring sewage to the receptors (through the terminal pump station). Finally, the disposal of the sludge generated by operating the system must also be ensured.

Sewage collection

On 31 December 2006, a total of 5,282 km public sewers were operated, as detailed in the following:

Specifications of the sewer network in Budapest in km

Year	Main sewer	Connencting sewer	Total	Out of this: new construction
2000	3267	1306	4573	94
2001	3329	1336	4665	92
2002	3419	1380	4799	134
2003	3498	1417	4915	116
2004	3605	1470	5075	160
2005	3675	1504	5179	104
2006	3745	1537	5282	103

62.5% of the Budapest sewer network is combined, 29.3% is sewage and 8.2% is rainwater sewer.

Composition of the Budapest sewer network in km

Year	Sewage	Rainwater	Combined	Total
2000	1047	390	3136	4573
2001	1098	391	3176	4665
2002	1189	397	3213	4799
2003	1275	400	3240	4915
2004	1380	415	3280	5075
2005	1467	425	3287	5179
2006	1549	431	3302	5282

145 intermediary automatic pump stations are part of the sewer network and support the transfer of sewage from low laying areas, which are integrated into the sewer system. Beyond these pump stations we also operate a manned intermediate transfer pump station. We received trucked sewage collected from areas with no public sewer system at 7 concentrated septic-waste receiving stations also in 2006 and at 19 additional designated locations along the sewer network.

In relation with both the network and the terminal pump stations, the 2006 heavy showers but also the floods represented a considerable load. In the reporting period, flood waves reaching decreasing level occurred three times and once a flood wave that did not reach the decreasing level on the Budapest section of the Danube. In terms of duration, runoff and water level, the greatest flood lasted from March 29 to April 14. At that time the Government decreed an extraordinary flood-protection state of emergency on the Hungarian section of the Danube. Recording of water levels started 158 years ago. Since then in 2006, 860 cm was the highest recorded water level in Budapest. Flood protection was successful in all four cases.

The extreme weather phenomena due to climate change affect the drainage area of the Danube, thus we must expect the risk of floods more often. Similarly, the increase of the size of rain quantities falling locally represent a risk. This may cause quick floods and overflows on the capacity lacking sections of the operated small streams and rainwater collection dyke network. Taking into account the considerable part of the network runs through highly urbanized areas, even overflows of smaller surfaces can cause considerable damages.

Terminal stations

On December 31, 2006 two major sewage treatment plants operated in Budapest. In addition, 11 automatic and 8 manned terminal pump stations were transferring sewage into the river Danube. The pump station at Angyalföld plays the role of an intermediate transfer station as well. In total, our stations transferred 211,540 thm³ wastewater and rainwater, which represents 89.8% of the 235.540 thm³ sewage and rainwater collected in the capital.

54.9% of sewage generated in dry periods has been treated by the Company at the South-Pest and the North-Pest treatment plants. The combined total output of the two stations reached 280 thm³/day. The biological capacity of the South-Pest plant is 80 thm³, as well as 80 thm³ capacity for nutrients removal. In 2006, the North-Pest plant operated at its full capacity of 200 thm³/day.

Average actual biological treatment capacity in 2006 m³/day

Description	Average capacity	Load	Utilization %
North-Pest plant	200 000	150 000	75,0
South-Pest plant	80 000	60 507	75,6
Treatment plants total	280 000	210 507	75,2

The hydraulic load of the North-Pest treatment plant is satisfying on average, but great fluctuations happened during the year, since in the first semester, during the reconstruction of the main collector of Kassák Lajos avenue, the whole water quantity of the drainage area of the main collector was drained – by a temporary pump station – to the drainage area of the North-Pest plant. During the second half of the year, this temporary pumping ceased, however, a considerable part of the wastewater was drained to the Ferencváros Pump Station during the redevelopment of the Mexikói avenue sewer.

In 2006, the average polluting matter concentration of incoming wastewater showed an average increase of 10% for all parameters as opposed to the previous year. The Environmental Protection Inspectorate has set an individual threshold in terms of the quality of discharged treated water, which was satisfied by all parameters of the effluent water.

The plant has continuously received sewage delivered from the Angyalföld Pump Station. In 2006, the construction of the main sewer draining the wastewater from North-Buda and located under the river bed was finished. The expected date of commissioning of the delivery-pipe is April 2007. Following such commissioning, biological treatment of the wastewater quantities originated from here, of a quantity expected to reach 27,000 m³/day will be resolved. During the reporting period, the preparation of the nutrient removal phase also started.

During 2007, we expect the realization of the 24,000 m³ useful volume digestion units and the connected biogas utilization to start.

At the South-Pest treatment plant, 2006 was the year of enhancement of waste handling and management. The great capacity open air waste receiving and treatment equipment was built at the beginning of the year, which can be used by great volume transport vehicles as well. This equipment made possible the reception of dairy products withdrawn from canned catering. With the operation of the waste receptor and treatment unit, the quantity of produced biogas doubled in 2006 and the energy supply of the plant. The increase of the quantity of biogas required the increase of the capacity of the whole biogas pipe network.

In 2007, the following main investments are expected in order to increase the quality of services and the more cost-efficient operation:

- On the sludge line, the construction of the 200 m³ sludge container silo has started.
- The covering of the pre-mechanic installation and the construction of a biofilter in order to eliminate odours are planned.
- For the purpose of a better treatment efficacy, the development of the activated sludge biological system is expected, as well as the extension of the current aeration elements and the installation of a new air blower unit.

- On the sludge line, the construction of a 1,500 m³ sludge gasifier gas container, the extension of the digestion capacity by 2,600 m³ as well as the replacement of the heating system of the mesophile towers can be expected.

The parameters of the effluent water of our wastewater treatment plants have remained within the individual threshold limits set by the authorities in relation to all components in 2006.

Sludge disposal

Waste generated during the operation of the sewage system must be disposed according to relevant environment protection regulations and the issued permits. Sludge settled in the sewers is dehydrated in the South-Pest plant. This sludge, including dehydrated sand and waste collected by screens is collected, before disposal, at the South-Pest plant. Dehydrated sand and waste collected by the screens at major sites is delivered directly to companies responsible for collection.

In 2006, 145,498 m³ (119,975 tons) of sludge were generated, thus we had to ensure the disposal of an additional 15% of sludge compared to the base period, when this value was 126,747 m³. 17% of the waste was putrefied and dehydrated sludge for the South-Pest plant; the remaining 6% was given by general sewer waste. The greatest quantity (77% of waste) was generated at the North-Pest plant. 48% of this dehydrated sludge was placed at the landfill at Csomád, owned by the City but operated by the Company. 37% of the total quantity was placed at the Csomád landfill, the remaining 63% was treated and disposed by contractors operating with environmental protection permits.

We load the Csomád landfill since 1 November 2006, by taking into account of its capacity and its planned extension. For the purpose of increasing its cost-efficiency and of decreasing the risks of disposal, the transport and disposal of the remaining dehydrated sludge is made by a single external contractor for 5 years. The public procurement tender published for this purpose was won by EWC-H Kft.

Specifications of waste generated by the sewage network in 2006 in m³

Description	Volume	Disposal		
		Csomád	Third-party contractor	Total
Settled sand and sewer sludge	6 081		6 081	6 081
Screened waste	2 934		2 934	2 934
Compressed sludge from plants	136 483	53 170	83 313	136 483
Total	145 498	53 170	92 328	145 498

Financial position

The Company had a balanced liquidity position over the entire year. This financial balance was significantly influenced by changes in receivables.

Changes in receivables

In comparison to last year's figures, trade receivables increased by HUF 730.2 million, by 24% as of December 31. The greater part of the additional receivables are recognised flood expenses that have not yet been settled. The change was due to the transfers and changes of HUF -71.5 million credit balance trade receivables and the increase of amortizations by HUF 68.3 million (decreasing account receivables) and the increase of receivables by HUF 870 million (of which HUF 404.3 million is flood). 87% of receivables was made up by sewer usage charges. Sewer charge receivables within the due date increased by 12%, while that of past due receivables is 11%. The increase of past due receivables above the rate of the 6% tariff increase of the beginning of the year is the result of liquidation and lawsuit procedures started against some big consumers. The increase of the VAT rate from 15% to 20% during the year had a decisive effect on wastewater receivables – especially on receivables within due date. Receivables from other activities increased by HUF 476 million, by HUF 72 million excluding flood receivables. Uncollectible wastewater receivables were written off in a value of HUF 66 million in 2006.

Changes in receivables without amortizations on December 31, 2006 in thousand HUF

Description	2005		2006	
	Total	Sewage division	Other activities	Total
Overdue receivables				
0- 90 days	720 430	748 367	440 861	1 189 228
91- 180 days	190 956	207 483	7 581	215 064
181 -360 days	230 057	306 771	1 336	308 107
361 - day	299 022	309 445	6 755	316 200
Total overdue receivables	1 440 465	1 572 066	456 533	2 028 599
Receivables within due date	2 148 173	2 303 279	126 726	2 430 005
Total trade receivables	3 588 638	3 875 345	583 259	4 458 604
Overpayment to suppliers		323 225		251 734
Loss of value		-550 312		-618 583
Total trade receivables on 31st December	3 361 551			4 091 755

Cash flow

In 2006, the cash and bank income of the Company exceeded HUF 43,612 million; out of this HUF 43,580 million was unrestricted and HUF 32 million held in a separate bank account.

16% of the own coverage was opening balance, 72% of it came from wastewater services, public utility development contribution, interest income, sewer fines, revenues from export activities and 12% from other customers. Revenues exceeded the budget by 2%.

The financially realised income from wastewater collection was HUF 468 million less than expected, however, the revenues from other activities, sewer fines, interest and to a greater extent (by HUF 801 million) that of public utility development contribution.

The value of financial expenditure reached HUF 38,571 million, within this that of freely available cash was HUF 38,539 million, that is HUF 522 million higher than budgeted.

The Company did not have any past due liability towards the state budget, Social Security and its suppliers. The increase of our expenses as opposed to the plan was partly due to the fact that material purchase increased due to the capital city's road reconstructions, wages and their contributions increased as a consequence of higher than expected staff. Considerable payments above plan were: from environment load tax, capital city rental fees, taxes (due to the changes of the tax code – more precisely the additional tax – in September). VAT rates changed from 15% to 20% from September 1, 2006. The miscellaneous supplier payments increased primarily as an effect of the flood protection. These additional expenses were only partly balanced by the fact that our own investments were only partially realized and that the development fund decreased as a result of the wastewater volume lack.

In summary, the value of cash-type expenses in 2006 were HUF 5,041 million less than actual revenues. The Company retained its liquidity throughout the year.

Financial risk

Wastewater collection and treatment is an activity that is subject to partial service obligation in compliance with Government Decree 38/1995. (IV.5.). As per the dispositions of the decree, the service can be restricted in the case of only a part of the consumers (with determined conditions).

Another difficulty comes from the fact that the invoiced wastewater must be invoiced – in lack of measurement, on the basis of data from an organization independent from the Company – on the basis of the water consumption. Water consumption is followed by measurement, invoicing and then payment. However, the



service provision obligation is not combined by a payment obligation from the side of the consumer.

This is the reason why the greatest risk or rather uncertainty arising during wastewater services is the realization of the plan of invoiced wastewater (based on water consumption), the collection of the sewer charges and their schedule.

With the increase of the quality of the service, the increase of the proportion of treated wastewater, the expenses and thus the tariff also increase. The increase of the VAT rate also affects the tariff. With the increase of the tariff, the risks of collection also increase. Since the expenses of the activity are basically asset-based, costs do not decrease proportionately with the decrease of revenues in case of volume decrease. The weather constitutes another risk. In a rainy period, water consumption and wastewater emission (thus revenues) are smaller, while the additional costs of great showers are burdened on the service but are not invoiced.

The risks of the activity are taken into account in the cash flow type pricing. At its own discretion, the Company strives to decrease its receivables with the continuous inspection of receivables and with the tools as per the required processes in case of non-payment (prompt note, lawyer's note, personal collection, lawsuit, etc). In 2006, the 14 collectors collected HUF 4,039 million of past due fees.

The Company's risk management and hedging policies are justified by the fact that it settled its liabilities in time, has no tax debts and pays its invoices in time – without taking out credits.

For the purpose of preserving stable liquidity, a liquidity plan is prepared, with daily liquidity analysis, investments are safe. As a result of this, the Company's liquidity and willingness to pay is good and it economically enhances the continuous operation of the sewer network.

Cash flow I-XII. months 2006

Description	Plan	Actual	Difference	
	1-12 months	1-12 months	th.HUF	%
Opening balance	7 107 680	7 107 680		
Revenues from sewage charges	31 584 186	31 116 584	-467 602	98,52
Revenues from other activities	1 143 699	1 469 995	326 296	128,53
Revenues from export	0	19 638	19 638	
Sewage penalties	120 000	142 607	22 607	118,84
Public utility development contribution	1 680 000	2 481 118	801 118	147,69
Interest received	464 766	541 498	76 732	116,51
Other revenues	54 080	51 911	-2 169	95,99
Social Security	153 000	129 445	-23 555	84,60
Technical revenues	500 000	500 000	0	100,00
Cash for research and development on a separate account		20 088		
Total non-restricted cash available	42 807 411	43 580 564	773 153	101,81
Received for flood control equipment maintenance	27 000	31 657	4 657	117,25
Available on a separate account	27 000	31 657	4 657	117,25
Purchased materials	2 179 824	2 290 206	110 382	105,06
Energy	1 060 600	1 041 672	-18 928	98,22
Maintenance	531 944	482 248	-49 696	90,66
Wages, remunerations, compensations	1 991 362	2 188 582	197 220	109,90
Social Security	1 153 530	1 182 333	28 803	102,50
Private Pension Fund	198 085	205 990	7 905	103,99
Wastewater penalties	585 000	593 919	8 919	101,52
Environmental load tax	1 688 834	1 914 336	225 502	113,35
Taxes and penalties	3 249 341	3 477 780	228 439	107,03
Tax paid (VAT)	1 872 937	2 027 986	155 049	108,28
Bank fees and interest expenses	14 362	15 526	1 164	108,10
Own investment and value-added reconstruction	10 570 908	9 918 676	-652 232	93,83
Development fund	5 458 038	4 998 768	-459 270	91,59
Other resources for development	27 500	42 959	15 459	156,21
Dividends	3 463 318	3 463 244	-74	0,00
Other payments to suppliers	1 959 052	2 461 064	502 012	125,63
Rent paid to the Municipality	1 653 028	1 879 863	226 835	113,72
Compensation	359 200	354 200	-5 000	98,61
Total available financial instruments	38 016 863	38 539 352	522 489	101,37
Maintenance of flood control equipment	27 000	31 657	4 657	117,25
Restricted payments	27 000	31 657	4 657	117,25
Total financial instruments	4 790 548	5 041 212	250 664	105,23
fixed deposits	8 448	1 266 638	1 258 190	14993,35
fixed liquid securities, portfolio	4 780 000	3 773 072	-1 006 928	78,93
Closing financial balance	2 100	1 502	-598	71,52

Sewer charges

Revenues from collection and treatment of wastewater and rainwater are determined, beyond the volume of sewage, by the all-time level of sewer charges. This public service fee is a maximized price determined by the authorities. Since January 1, 1993, pursuant to Act LXXXVII/1990 amended by Act CIV/1993, the rights of the pricing authority are exercised by the body of representatives of local municipalities – in the case of our Company, by the Body of Representatives of the Municipality of Budapest. The formula used for determining sewer charges is approved by the Municipality of Budapest by Decision No.1422/96. (X.31.) of the General Assembly. Appendix No. 2 of the Public Utility Service Contract includes the tariff formula. The Company makes its suggestion on the tariff until October 31 on the basis of this formula.

Tariff suggestion for the year 2006 was negotiated in November 2005. According to Decree No. 85/2005. (XII.16.) of the General Assembly of Budapest, sewer charges for the City of Budapest from January 1, 2006 have been set at HUF 197/m³. The new service fee contains an average of HUF 43.8/m³ development contribution which is meant to cover the investments defined by the Capital City following the taxation and the transfer to the Municipality of the Capital. The sewage charge also contained environmental load tax in the amount of HUF 7.60/m³ determined by our Company based on Law LXXXIX of 2003 and re-charge to the users based on the Government Decree number 270/2003. (XII.24.).

Among the conditions of price application, the rules of watering discounts introduced in 1994 remained unchanged ever since the modifications of 2004 made through the Government Decree 38/1995. (IV.5.). Public baths, which signed a contract with the Municipality of Budapest, may enjoy a 50% discount on sewer charges applicable to water discharged from public baths since January 1, 2001 under certain conditions. This rule of the price application has not changed but does not apply to the re-charged environmental load tax. Sewer charges were accrued by 15% VAT until August 31, 2006 and by 20% VAT since September 1, 2006.

The Municipality of Budapest set the 2007 tariff at HUF 215.50/m³.

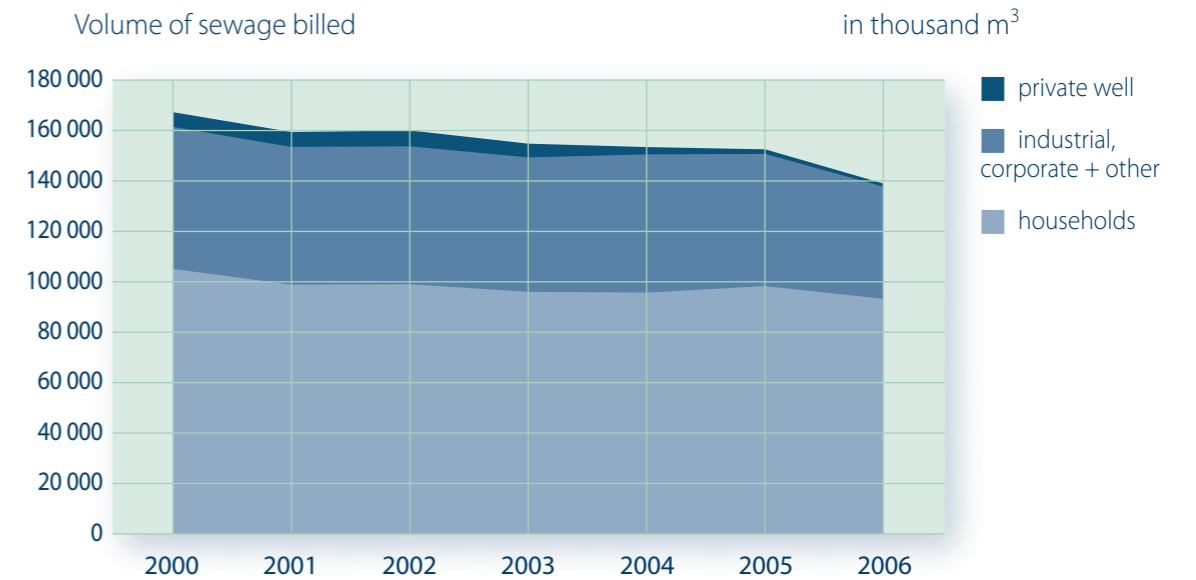
The greatest risk of the tariff is given by the unknown changes of the regulatory system and the wastewater quantity plans, which – in lack of measurements – can be determined on the basis of the invoiced water quantities in compliance with Government Decree 38/1995. (IV.5.) and its amendments. The latter is a data of an organization independent from the Company.

The General Assembly of the Municipality of Budapest, in its decision No. 2546/2005. (XI.24.) Kgy., requires from our Company a compensation fund of HUF 359.2 million for the year 2006, to be used for helping customers using the public sewer network. (HÁLÓZAT – Foundation for Customers in Budapest and for People with Outstanding Charges.) Settlement is made from March to March.

Business performance and results

Revenues

Annual income of the Company is basically determined by revenue from sewage collection and treatment, which is determined by current sewage charges and the volume of services rendered. In 2006 this income was HUF 27,470 million, which also contained HUF 1,062 million environmental load tax. The revenue is 1.3% higher than in the previous year due to the 5.9% increase of the tariff while the volume of invoiced sewage was reduced by 6.5%.



66% of the invoicing of 2006 was household wastewater emission, which was lower than in the previous year by 6,483 thm³. The 2006 non-household consumption fell short of the 2005 by 3,171 thm³. In the capital, the volume of billed wastewater to corporate and industrial consumers was 31.4% of the highest quantity ever measured. (For this consumer group, the highest service usage was in 1985, with 153.4 million m³.)

The wastewater quantity analyses are related to actually invoiced volumes. Their composition is known, however, deferred services are only estimated, and may vary according to actual sewage discharge. Invoiced volume consists of the following two parts: consumption in current year and invoices issued for previous years' consumption.

■ Current year's consumption remained 3.7% below last year's level, and actual bills for services were 1.9% below the plan.

■ The effect of previous years' consumption delayed to 2006 was 28.8% less than in the previous year – affected by the invoicing changes of 2005 – and 9.8% below the plan.

As the cumulated result of the above two factors, in 2006, billed sewage was 9,654 thm³ less than in 2005, and 3,727 thm³ less than planned.

Volume of sewage as per the year of consumption in thousand m³

Description	2005	2006	
		Plan	Actual
Brought forward	16 214	12 802	11 545
Current year consumption	133 313	130 798	128 328
Total billed volume	149 527	143 600	139 873
Deferred volume	12 802	12 662	12 271
Change in deferred volume	-3 946	-140	-531
Total in revenues	145 581	143 460	139 342

In 2005, the invoicing of a factoring client base – in accordance with the invoicing of the consumption – was modified. This change decreased the accrued quantity, while increasing the billed quantity in 2005. This change could already be taken into account when planning the wastewater quantities. The annual plan targeted the invoicing of 143,600 thm³ sewage, as well as deferred services of 12,662 thm³ sewage. Actual change was more drastic than that. In fact, 139,873 thm³ were billed, and 12,271 thm³ were accrued for. In total, the basis of revenue is 4 million m³ less than planned.

The change in deferment made possible the account of HUF 139,342 thm³ of sewage quantity as revenue. This was less than in the previous year by 6,239 thm³ and less than planned by 4,118 thm³.

As a summary, invoices for 139,873 thm³ sewage and HUF 2,425 million of deferred income made the accounting of HUF 27,470 million revenue possible. In 2006, a determining part of the net revenues of the Company (94%) came from wastewater collection and treatment. This proportion is 2% less than the previous year's. The reason of the change is that the proportion of the other activities – as an effect of the flood revenues – increased.

Based on the contract concluded with the Capital the water damage control and water quality protection activity generated HUF 552 million revenues. The revenues from flood protection reached HUF 396 million, that of the maintenance of flood protection equipment HUF 146 million, while that of water quality protection HUF 10 million.

Evolution of revenues

in thousand HUF

Description	2005 actual 1	2006 plan 2	2006 actual 3	Index % 3/1	Index % 3/2
1. Sewage collection and treatment	27 128 880	28 265 790	27 470 220	101,3	97,2
2. Bath discharges, secondary water meter	154 166	150 000	158 377	102,7	105,6
3. Other sewage services	175 803	194 810	376 468	214,1	193,2
4. Water damage control, quality protection	168 425	155 600	551 858	327,7	354,7
5. Industrial	8 282	10 000	19 240	232,3	192,4
6. Construction	3 728	5 000	1 134	30,4	22,7
7. Transport activities	4 845	1 500	6 330	130,7	422,0
8. Mediated services	52 443	43 000	53 618	102,2	124,7
9. Other activities	530 429	528 500	634 913	119,7	120,1
Revenues from domestic sales	28 227 001	29 354 200	29 272 158	103,7	99,7
Revenues from export sales	13 831	0	19 590	141,6	
I. Net sales revenue	28 240 832	29 354 200	29 291 748	103,7	99,8
II. Other revenues	13 312 092	13 193 300	13 277 930	99,7	100,6
A. Operating revenues	41 552 924	42 547 500	42 569 678	102,4	100,1
B. Financial revenues	789 269	510 000	581 732	73,7	114,1
C. Ordinary revenues	42 342 193	43 057 500	43 151 410	101,9	100,2
D. Extraordinary revenue	397 673	385 500	427 017	107,4	110,8
E. Total revenue	42 739 866	43 443 000	43 578 427	102,0	100,3

Apart from the capital city tasks, other services were rendered in relation with the sewer utilities for HUF 376 million. The swimming pool water collection determined with a tariff discount of 50% and the invoicing of secondary water counters generated HUF 158 million in revenues.

The industrial, building industry and transport activities generated HUF 27 million revenues to the Company in 2006.

The value of mediated services reached HUF 54 million.

Revenues from other activities increased by HUF 104 million compared to the previous year and reached HUF 635 million. Rent generated HUF 42 million, waste sales HUF 37 million, agglomeration sewer operation HUF 24 million and management of flood protection HUF 1 million additional revenues to the Company. The revenue change of the other activities balanced each other.

In 2006, the Company reached HUF 20 million revenues from export activities as a result of the sewer maintenance activities performed in Romania.



Other revenues are HUF 34 million below that of the previous year.

Two items decreased (by a total of HUF 536 million) in comparison with 2005, namely sewer penalties by HUF 23 million and provision usage by HUF 513 million. In the base period, the wastewater penalties of several years were paid and their provisions were released, while in 2006, only one penalty was paid, but two years' environmental load tax was paid. In comparison with the previous year, the other revenues increased by a total of HUF 502 million. The most important additional revenue was reached in the factoring revenues, which increased by HUF 401 million as a result of the tariff increase. Additional revenues from asset sales were HUF 36 million, HUF 10 million from damage events, HUF 17 million from penalties and late penalties, and HUF 9 million in total from other smaller items as opposed to the base period. The recovered depreciation generated an increase in technical revenues in the amount of HUF 29 million.

Additional revenues were HUF 85 million compared to the budget. There was HUF 170 million revenues above plan, primarily from: asset utilization (HUF +58 million), recovered amortization (HUF +36 million), sewer penalties (HUF +23 million), related to damage events (HUF +11 million), other penalties and late penalties (HUF +28 million) and smaller items (a total of HUF +14 million).

The amount of revenues falling short of the budget is HUF -85 million. Due to the decrease of the wastewater quantities, HUF 81 million less was received from factoring revenues and the provision release fell short of the budget by HUF 4 million.

Revenues from financial transactions were HUF 208 million below the level of the year 2005, since the amount of cash available for placement decreased. However, HUF 72 million revenue above the plan was reached. This primarily comes from the fact that due to the delay of the planned North-Pest investment, the cash temporarily available for interest was higher.

Amortization of assets received without compensation was included in extraordinary revenues, which was increased, in comparison to the base period, by HUF 29 million.

As a summary, in 2006 the Company's net revenues reached HUF 29,292 million, HUF 1,051 million more than in the previous year. The sewer tariff revenues resulted in 32.5% of the additional revenues, flood protection 36.5%, while the other activities 31%. The revenues of the Company exceeded HUF 43,578 million. This amount is higher by HUF 839 million (2%) than last year's.

Expenses

Due to the high level of operating assets required for water management services, a large part of the expenses – similar to revenues – are beyond our control. Asset-based expenses are incurred independently from the usage of the service, and these make up the major part of the expenses. Among these, amortization and maintenance are outstanding in terms of both volume and proportion. In 2006, asset-based costs reached 59.4% of the sales expenses, among which 41.4% was amortization and the amortization part of the rental fee and 17.8% was maintenance.

In total sales expenses increased by HUF 1,111 million, that is 7.4% in comparison with the base period. The yearly plan was basically achieved at 104.5%.

Sales expenses in thousand HUF

Description	2005 actual 1	2006 plan 2	2006 actual 3	Index % 3/1	Index % 3/2
Material-type expenses	6 394 344	6 226 000	6 741 416	105.4	108.3
Personnel-type expenses	4 213 743	4 294 000	4 614 624	109.5	107.5
Depreciation	4 652 967	5 095 000	4 975 977	106.9	97.7
Capitalized own products	-243 787	-185 400	-203 304	83.4	109.7
Operating expenses	15 017 268	15 429 600	16 128 713	107.4	104.5

Material-type expenses include all costs of materials, the costs of material-type, other and mediated services, in the value of HUF 6,741 million. Additional expenses of HUF 347 million in comparison to last year are mainly caused by the inflation and to a smaller extent by own maintenance and the increase of materials ensured for the capital city's road reconstructions.

Among material type expenses, 41% was materials and energy expenses, 56% was purchased services, 2% other services and 1% mediated services. Among purchased services, the rental fee of assets owned by the Municipality of Budapest, at a total of HUF 1,698 million, was the most important item. Among material type expenses, additional expenses compared to the budget was caused by higher than planned inflation, materials ensured for the capital city's road reconstructions above planned, not planned material type expenses of flood protection, additional material usage of own maintenance and sludge disposal tasks and expenses.

Personnel-type expenses reached HUF 4,615 million. Wages (68% of personnel-type expenses) indicate the impact of wage increase. Other personnel-type expenses contributed to 8% of the total of personnel-type expenses. Social insurance expenses make up 24% of personnel-type expenses. In terms of the personnel-type expenses there was a HUF 321 million excessive use mainly due to the personnel-type expenses of the flood protection, the higher than expected number of staff and additional expenses due to reorganization.

In 2006, amortization was HUF 4,976 million. The increase was caused by the increase in the value of fixed assets. As a combined effect of depreciation, delay in time of capitalizations and write-offs, it remained below the plan by HUF 119 million.

Capitalized own production contributed HUF 203 million to the above listed expenses. This amount, due to changing demand and possibilities, was HUF 41 million less than in last year and exceeded the planned amount by HUF 18 million.

Evolution of expenses in thousand HUF

Description	2005 actual 1	2006 plan 2	2006 actual 3	Index % 3/1	Index % 3/2
Trade expenses	15 017 267	15 429 600	16 128 713	107.4	104.5
Other expenditure	16 160 964	16 520 600	16 980 793	105.1	102.8
Operational costs	31 178 231	31 950 200	33 109 506	106.2	103.6
Financial expenditure	19 849	30 000	49 953	251.7	166.5
Ordinary expenses	31 198 080	31 980 200	33 159 459	106.3	103.7
Extraordinary expenses	5 692 559	5 848 500	5 412 981	95.1	92.6
Total costs and expenses	36 890 639	37 828 700	38 572 440	104.6	102.0

Above operational expenses, other expenditure reached HUF 16,981 million. This is HUF 820 million higher than last year's figure. Items with the highest level of increase: environmental load tax was HUF +1,119 million as per the legislation, the increase of the cost of factoring was HUF +407million, receivables write-off HUF +33 million. The following other expenditures decreased: wastewater penalty (only one year) by HUF -584 million and the provisions by HUF -157 million. The joint change of the other items is HUF +2 million. Compared to the budget, additional costs reach HUF 460 million: additional environmental load tax: HUF +278 million, provision: HUF +204 million, depreciation and above plan write-off: HUF +27 million, asset utilization revenues: HUF +22 million, factoring expenses: HUF -84 million, the change of the other items in total: HUF +13 million.

The cost of financial transactions of the Company reached HUF 50 million.

In 2006, extraordinary expenses reached HUF 5,413 million. Its major part is the development fund with HUF 5,013 million. Payables to the fund providing compensation for sewage users reached HUF 354 million. Other payables of HUF 44 million were included in the extraordinary expenses category.

In summary, total expenses of the Company reached HUF 38,572 million. Because of this and the revenues, profit before tax was HUF 5,006 million.



Profit

Profit before tax of the Company was influenced by the following factors: operating profit, influenced by the development contribution and by savings, reached HUF 9,460 million. Profit from financial transactions increased this by HUF 532 million. However, financial instruments transferred for development without repayment reduced this extraordinary loss by HUF 4,986 million. The combined effect of the above resulted in the profit before tax of HUF 5,006 million. In 2006 the Company had a profit tax obligation of HUF 1,695 million, since factors increasing the taxable income exceeded the factors decreasing it by HUF 4,753 million.

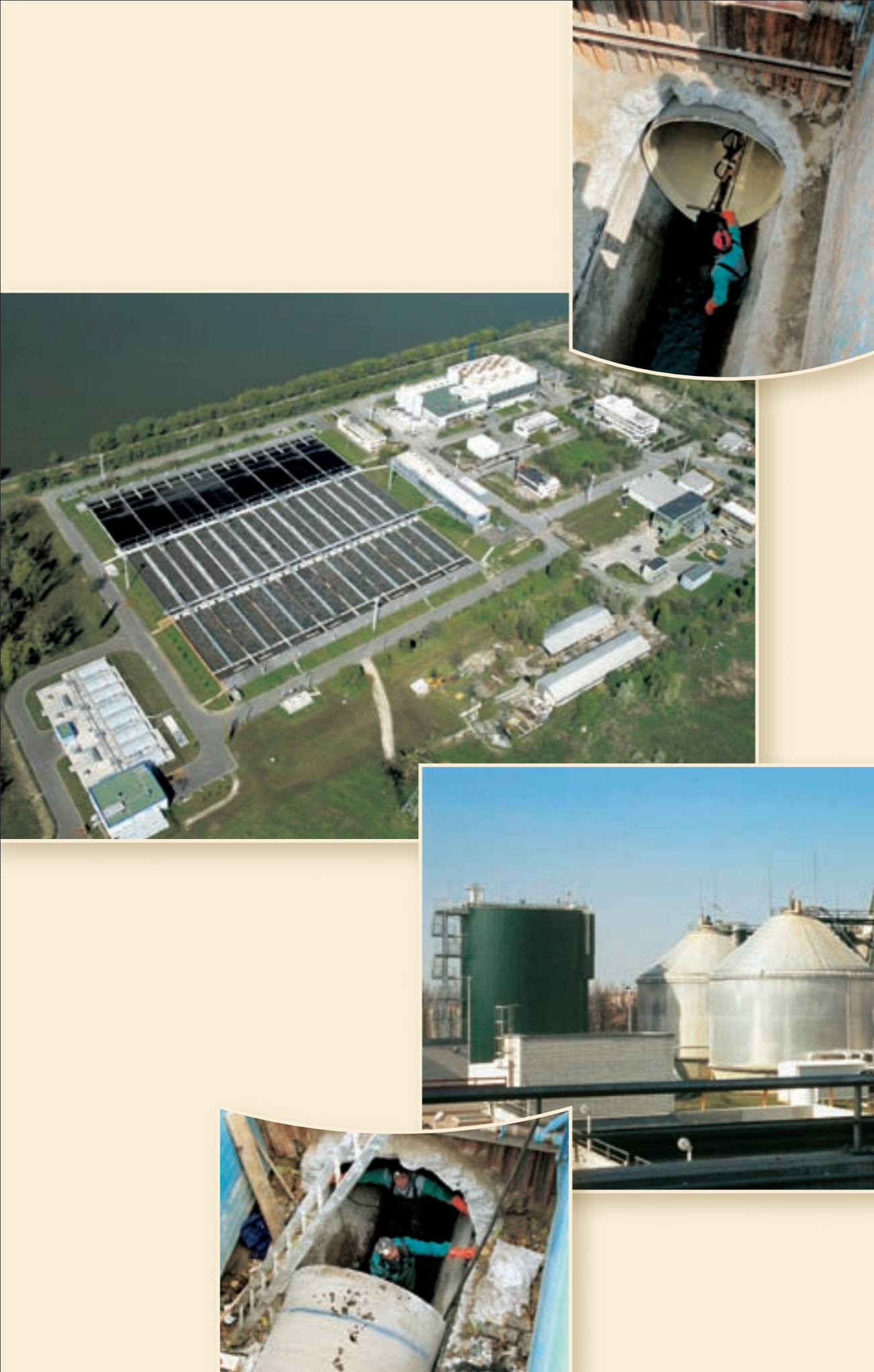
Evolution of the profit in 2006 in thousand HUF

Description	Revenues	Expenses	Profit
Operating services	42 569 678	33 109 506	9 460 172
Financial transactions	581 732	49 953	531 779
Usual business activity	43 151 410	33 159 459	9 991 951
Extraordinary activity	427 017	5 412 981	-4 985 964
Profit before tax	43 578 427	38 572 440	5 005 987
Tax payable	0	0	1 694 889
Profit after tax			3 311 098
Paid (approved) dividend			3 219 185
Balance sheet profit figure			91 913

After analysing the activities of the Company, we can declare a net operating profit (as a result of the development contribution) in the sewage division (HUF 9,287 million), in other water management services (HUF 350 million), as well as in other activities not related to the core activities (HUF 199 million) and a loss in the fields of water damage control (HUF -373 million) as well as industrial and building industry activities (HUF -3 million).

Profit after tax is reduced by HUF 3,219 million dividends paid, thus the retained profit stood at HUF 92 million.

Investments and developments



Capital investments

The operation of sewers is investment intensive. Development and reconstruction expenses are high and of a bigger volume as well. Sewers of the capital are still incomplete, both in terms of sewage and rainwater collection and their treatment. At present, capital investment for sewage works may come from the following financial sources:

- EU and state subsidy (via the Municipality of Budapest),
- budget of the Municipality of Budapest and development fund incorporated into sewage charges,
- own development resources of the Company,
- contribution from district municipalities,
- financial resources of the general public, for the construction of sewers (in general with additional subsidies from the district municipalities).

All completed developments are operated by our Company.

I. Development financed by the Municipality of Budapest

In 2006 our Company – with the shareholders' approval – contributed to the development of the sewage network in Budapest through the funds accumulated from the development contribution incorporated into sewage charges and from rental payments. The capital city's development coverage is determined in the fee jointly and specifically on the basis of the volume plan of invoiced wastewater.

Planned development resources of the Municipality of Budapest at the time of approving the sewer charges for 2006 in thousand HUF

Description	Planned transfer of funds allocated for development	Actually transferred development funds	Rent transferred to Local Administration	Total
Transfer of development charges	5 400 000	5 117 520	5 013 313	-104 207
Transfer on net rent	1 700 000	1 697 680	1 697 680	0
Total	7 100 000	6 815 200	6 710 993	-104 207



In 2006, the average development, rental and usage fee portion was HUF 55.48/m³, which represented a total development resource of HUF 7,100 million after tax. This value ensured in the tariff was modified to an actual value of HUF 6.711 million due to the change in wastewater volume and the shift of internal proportions towards untaxed resources.

Sewage works owned by the Municipality of Budapest are operated by our Company. The Company pays rent and usage fees for assets under our operation. In 2006 it was HUF 12.14/m³ instead of the planned HUF 11.60/m³ due to the takeover of district sewers as well as the decrease of the wastewater volume (total HUF 1,698 million).

The actually transferred (net) part of the development contribution to the Municipality of Budapest is to be accounted in extraordinary expenses as definitely transferred development resources. Instead of the HUF 43.88/m³ gross and HUF 36.86/m³ net tariff portion – due to the higher than planned amount of rental fee, the decrease of wastewater volumes and the additional tax imposed on the development fund – an average of HUF 43.34/m³ gross and HUF 35.84/m³ net development fund was reached. The amount of the revenue originated from the created development fund in 2006 was HUF 6,063 million, which decreased the development fund payment obligation to HUF 5,013 million after tax. On the basis of expected data, the amount transferred until the end of December was HUF 5,117 million.

Investments in the possession of the Municipality of Budapest and taken over by the Company for operation (excluding property value, replacement for housing property value and transfer of funds)

in thousand HUF

Project description	until end of 2005	in 2006	until end of 2006
Main sewer at XI. Hamzsabégy-Ajnácskő str.	389 176		389 176
Main sewer at Rákospölgy-North	1 870 149		1 870 149
Main sewer along IV-XV. Szilas-stream	356 666		356 666
Main sewer at IV. Corvin-Bajza-Fóti str.	382 990		382 990
Pump station at II. Zsigmond Square	1 491 219		1 491 219
South-Pest Wastewater Treatment Plant	6 535 840		6 535 840
North-Pest Wastewater Treatment Plant	5 572 653		5 572 653
Main sewer at South-Buda	657 546		657 546
Septage receiving station at North-Pest	38 927		38 927
Septage receiving station at Albertfalva	46 127		46 127
Main sewer at Bécsi str.	277 429		277 429
Main sewer at Kőbánya	775 220		775 220
Hungária boulevard	608 851		608 851
XI. Etele square	77 446		77 446
Expo site	345 745		345 745
XV. Szócs and Eötvös str.	33 519		33 519
Hungária - Könyves Kálmán boulevards	241 230		241 230
Main traffic road no. 5	321 338		321 338
VI-VII-XIV Dózsa György avenue	80 174		80 174
XVIII Süllyás street pump station	37 523		37 523
Haller street in the IX district	67 786		67 786
Fiumei avenue	90 124		90 124
Rákospölgy - Péceli str.	92 016		92 016
Orczy avenue	1 316		1 316
Bácskai street - Laskay str.	279 435		279 435
IV distr. Káposztásmegyér developm. area	184 357		184 357
Properties	14 572	2 821	17 393
District sewers	12 484 314	5 750 821	18 235 135
Total	33 353 688	5 753 642	39 107 330

II. Projects completed from own resources of the Company

In 2006 own development resources of the Company reached HUF 9,504.4 million and were the following:

- Opening amount of available financial resources HUF 2,126 million.
- Development contribution received: HUF 2,069.5 million.
- Amortization: HUF 4,976 million in the reporting period.
- Book value of assets written off: HUF 102.7 million.
- Cumulated interest of development funds was: HUF 194.9 million.
- The usage of amount out of the environmental load tax for instruments was HUF 12.6 million.
- Resources from real estate sale were HUF 19.9 million.
- HUF 2.8 million was received for sewage damage compensation.

Utilization of resources available for development

HUF 8,351.7 million was contributed from the Company's own resources. The Company devoted HUF 15.7 million out of separated resource, the re-charged environmental load tax, to the purchase of environmental protection instruments. The amount spent in total was HUF 8,367.4 million.

From own resources, 99% was reconstruction and replacement of tools and the proportion spent on development only 1%.

In the reporting period our Company did not utilize HUF 1,137 million from all its available financial resources. The high level of closing balance was due to the fact that the investment works of the North-Pest digestion unit were delayed to next year due to the length of the authorization process. This is covered by HUF 1.2 billion from own resources. However, this closing balance is smaller than the coverage need of deferred liabilities. The reason for this is that at the time when the extension of the length of the authorization process of the digestion unit became obvious, some investments scheduled for 2007 were realized earlier with the approval of the Board of Directors.

The investments of our projects fall under the process of public procurement. In order to handle the related tasks our Company operates a Public Procurement Group. In 2006, the group managed 37 public procurement processes related to our investments.

Detailed allocation of own financial resources in 2006 in million HUF

Description	2005 actual	2006 plan
Sewage treatment		
Reconstruction with added value	172,8	145,9
Reconstruction	329,9	390,1
Pump Station		
Reconstruction with added value	89,3	114,0
Reconstruction	274,6	580,8
Network		
Own investment	0,0	0,0
Reconstruction	4 108,0	5 278,3
Other		
Reconstruction with added value	339,9	344,0
Reconstruction	66,2	477,9
Design	78,6	148,8
Total reconstruction	5 459,3	7 479,8
Information technology	46,4	171,0
Special machinery	53,5	276,5
Transport equipment	216,9	165,9
Small machines, instruments	143,0	66,9
Fixed assets with low value	82,6	105,4
Total replacement	542,4	785,7
Reconstruction and replacement	6 001,7	8 265,5
Wastewater treatment		
Pump station		
Information technology	258,2	42,7
Fund transfer for development purposes		
Odour emission prevention	37,5	0,5
Operational building construction	78,5	
Building purchase	0,0	0,0
Small machines, instruments		16,7
Fixed assets with low value	67,6	26,3
Development total	441,8	86,2
Own usage	6 443,5	8 351,7
Purchase of environment protection instrument	184,9	15,7
Csomád landfill	0,0	0,0
Separate liability (Bartók B. str.)	0,0	0,0
Other liability towards Capital City	0,0	0,0
Usage	6 628,4	8 367,4

Reconstruction, value-added renovation, replacement

Out of the reconstruction utilization and replacement was HUF 8,265.5 million. We have spent 63.9% of the total usage on the reconstruction of sewers, 6.5% on that of wastewater treatment plants, 8.4% on that of pumps stations and 11.7% on that of other tools. The replacement of assets constituted 9.5% of the utilization.

The Company spent proportionately less on treatment plants, since the investments planned have been delayed – due to external reasons – to the next year. The reconstruction of other equipments was increased both in value and in proportion by the transformation of the North-Pest laboratory.

In 2006, we have spent HUF 5,278 million on network reconstructions. The capitalized sewers have been transformed in a good quality until the deadlines determined in the contracts. Due to the capital city's road reconstructions, we have closed the sewer reconstructions with a considerable excess on the plan, 69 street sections have been renewed in a length of 24.2 km.

The lining technology put forward during renovations resulted in cost-savings in the case of road renovations and was combined with a more advantageous traffic management.

Among the sewer reconstruction projects realized in 2006 the followings were the largest ones:

- District I Logodi str. (Korlát lépcső-Mikó u.)
- District IX Ecseri str.
- District X Bihari str. (Mázsa-Ceglédi)
- District XII Maros str. (Acsádi-Csaba)
- District XII Mártonhegyi str. (Nárcisz-Diana)
- District XIII Kassák L. str. (Bulcsú-Botond)
- District XIV Gervay str. (Rákospatak-Körvasútsor)
- District XIV Dorozsmai str. (Rákosszeg-Öv)
- District XIV Kövér L. str. (Szugló-Egressy)
- District XIX Határ str. (Nagykőrösi-Ady E.)
- District XX Baba str. (Pölteberg-Nagysándor)



The amount spent on the reconstruction of wastewater treatment plants was HUF 390 million. For the purpose of enhancing the wastewater treatment efficacy, a zeolite receptor, container and dosing technological unit was built at the North-Pest Wastewater Treatment Plant. A modern bridge crane was built in the sludge hall and the obsolete shell pump pumping machinery room was also modernised.

At the South-Pest Wastewater Treatment Plant, the greatest task was the energy rationalization program, in the framework of which process control was modernized, waste handling was extended, technology was optimized and the heat supply system was transformed and modernized. Besides, the sludge wagon system was also transformed.

The reconstruction of pump stations has made up HUF 581 million. The greatest task was the modernization and transformation of the 24 automated pump stations and the 10 URH distance surveillance stations. At the Kelenföld pump station, the transformation of the shower machinery room was finished. At several pump stations, great size flood gates were replaced.

Value-added renovations reached HUF 604 million.

The value of value adding reconstruction conducted as outsourced work was HUF 400 million while as in house was HUF 204 million. At the North-Pest plant, the transformation of the central building and the laboratory cost HUF 386.4 million. The new laboratory represents a serious development at its accredited wastewater inspection activities.

In connection with the replacement of small machinery, ground machinery and transport equipment, we have spent a total of HUF 276.5 million, of which the followings have been purchased: 2 Mercedes sewer inspection vehicles, 2 automated equipped with cameras, 2 MUT combined sewer cleaning vehicles, 1 Komatsu dragging-loading machine and 1 winch cleaning machine with a trailer.

In 2006, we have spent a total of HUF 213.7 million on information technology, including development. The greatest extent work was the installation of the SZOLINFO integrated customer relationship system.

We have spent a total of HUF 165.9 million on transport equipment, which are the followings: 26 small trucks and maintenance vehicles, 2 trailers and 10 medley transport containers.

Maintenance

The ensuring of the continuous operation ability of the high stock of assets can be achieved with an appropriate maintenance activity, which is co-ordinated by the Maintenance and Contracting Department.

The primary objective of the maintenance activity is to preserve and ameliorate the technical conditions of the asset park of the services. In 2006 the Company was able to ensure the technical conditions of continuous and safe operation. This goal could be achieved in a most cost-effective way by applying the following measures in order to increase efficiency:

- to optimise the amount spent on external maintenance; with bargaining and tendering, or by replacement with our own workforce;
- to distinguish the technical and economic aspects of value-added reconstruction and other maintenance services;
- to perform feasibility studies (to analyse the age, net value and conditions of maintenance equipment and the expenses of the required works), before technical works (maintenance, reconstruction, replacement) commenced;
- to reduce time required for maintenance provided by our own workforce, first of all, time required for completing sewer maintenance;
- to sign operating and maintenance contracts (for example in case of heating-cooling systems).

In 2006 our Company spent HUF 2,870 million on maintaining fixed assets. Maintenance contributed to 17.8% of actual sales expenses.

Evolution of maintenance in thousand HUF

Description	2005	2006	Index %
Own maintenance	2 008 969	2 382 872	118,6
External maintenance	492 016	486 866	99,0
Total	2 500 985	2 869 738	114,7



In 2006, the value of maintenance made through external contractors was HUF 487 million. This was 17% of all expenses of maintenance. External contracting was mainly used for the maintenance of technological machinery equipment necessitating special skills, as well as the maintenance of equipment of the operation, social and other activities.

In construction projects of new wastewater treatment plants more and more complex equipment are installed that require a high level of maintenance, whose maintenance requires the services of specialized companies.

83% of maintenance was our own execution. Most of these works involved sewer maintenance, which can be illustrated by natural figures in the following table.

Network maintenance

Description	Unit of measure	2005	2006	Index %
Cleaning main sewers	lm	18 905	16 666	88,2
Traditional cleaning with pulleys	lm	18 320	14 105	77,0
Cleaning with high pressure machines	lm	492 467	461 593	93,7
Total	lm	529 692	492 364	93,0
Blockage removal	lm	53 505	52 660	98,4
Total cleaning	lm	583 197	545 024	93,5
Cleaning of lines of street drains	pc	29 321	24 812	84,6
Cleaning specific drains	pc	14 228	12 840	90,2
Total cleaning of drains	pc	43 549	37 652	86,5
Blockage removal	pc	3 429	3 411	99,5
Sludge discharge	m³	39 854	30 757	77,2
Length of sewers inspected	lm	1 458 117	1 680 064	115,2
Length of sewers repaired	lm	4 637	4 242	91,5

In compliance with the needs, the cleaning of greater diameter sewers increased in the reporting period. The specific working hours need of the cleaning increases proportionately with the section size. Beside equal work, this represented a decreasing cleaned length and costs increasing by inflation.

Due to the good maintenance state of the network – and in spite of the strong rains and long precipitations – the number of unexpected failures was lower. This is also shown by the fact that the number of sewer blockages and the number of sinkholes have decreased in comparison to the previous year (both in terms of number and linear meter).

The inspected sewer length exceeded the previous year's outstanding quantity by 15%. A major part of the additional 222 km inspection was given by the discovery of illegal rain-water sewer connections, as well the surveys preceding road constructions. The applied inspection evaluation system has greatly eased the gain of information on the network as well as the preparation of construction proposals during sewer reconstructions.



Main risks of the network maintenance activity

The average age of the sewer network increases, thus the need for reconstructions is more and more pressing. Due to the sewer reconstructions falling short of the desired level (1% per annum), the failures and the preventive maintenance needs increased. In relation with global warming, the frequency of great intensity showers concentrated on small areas increases, thus the average load and stress of the network is also higher.

The Company strives for the minimization of the failure causing effect of risks. For this purpose, it applies new technologies (introduction of repair technologies without uncovering, expanding the scope of the lining technologies), develops its technical IT system (sewer hydraulics model, reconstruction-planning module, map digitalization, vehicle tracking, introduction of electronic worksheet) and not least increases and modernises the machine park of network maintenance (the purchase of 5 specialized machines is expected in 2007).

Environment protection

The environmental activities of our Company in 2006 were still influenced by the legal changes occurring as a result of the legal harmonization processes due to the accession to the EU. The Company operates in the fields of water quality protection, waste management and air purity protection on the basis of Act LIII of 1995. In the operational area of the Company, among the main tasks, one can find the tasks in connection to the environment, the control of the wastewater quality flowing into the capital's public sewer network and the Danube, registration of data and the compliance with the data supply requirements.

The Company one of the biggest water utility companies of the country, and via its wastewater collection and treatment activities, it is in the meantime the greatest environment protection company in the country. The Company's Environment Management System (KIR) defines the most important principles in detail.

In terms of the tools for environment protection, the principles of the policy applied by the Company are:

- 1** We present our policy related to quality and environment protection to our suppliers and subcontractors and make them accept them and conclude our services according to these.
- 2** In cooperation with our owners, we strive to realize quality and environment centred solutions during reconstructions.
- 3** We regularly inform our owners, consumers, partners, authorities and the general public of our objectives and results.
- 4** We strengthen the feeling of responsibility for our environment at all levels of the Company.
- 5** We continuously optimize the wastewater treatment technologies that constitute our core activity to that the discharged wastewater burdens the environment less and less. In compliance with the EU environment protection requirements, we intend to increase the quantity of biologically treated wastewater as well as the efficiency of treatment.
- 6** During wastewater treatment – besides laboratory quality control – we continuously examine the effects made on the environment and implement measures to decrease the load on the environment.



- 7 We examine and estimate the effects of all new technologies to be introduced before the introduction. We strive to achieve that the new technology be environment friendlier than the previous one.
- 8 We implement measures to prevent and decrease pollution.
- 9 We ensure broad cooperation with the authorities.
- 10 During purchase, development and operation of equipment, we take into consideration their energy and material usage.
- 11 Through the application of modern sewer cleaning appliances and technologies we strive to ensure the population's environmental ease.
- 12 We enhance the relationship with our consumers through a modern and well installed system and develop satisfaction on the basis of surveys.

Our Company intends to achieve the qualitative and quantitative development of its service provision activities together with the creation of a healthy environment to the satisfaction of our consumers, employees, and the inhabitants of the capital city of Budapest and its surroundings.

The Company organises its activities according to its ISO 9001:2000 quality assurance and ISO 14001:2004 environment focused control system standards. The system transformed according to the standard was audited and certified satisfactory by Lloyd's Register Quality Assurance Ltd. Hungary. The transformed system was introduced in 2006. The North-Pest and South-Pest treatment plants have had quality certifying documents since June 11, 2001. The issued certification deeds are valid through 2007. The KIR programs planned for 2006 were realized pro rata temporis at both sites. In the area of environment protection, contacts with authorities happens through the relationship manager system, contacts were balanced and without problems throughout the year.

Environmental objectives, plans and programs related to the South-Pest Wastewater Treatment Plant:

- 1 Extension of renewable energy sources.
- 2 Elimination of the foam generated during the operation of the centrifuges.
- 3 Change from chloring disinfection to UV radiation.
- 4 Increasing the efficacy of the activated sludge treatment unit.
- 5 Construction of the sewer utility waste disinfection installation.
- 6 Making the posterior digestion unit able to heat and mix.
- 7 Modernization of the heating system.

- 8 Modernization of the process control system.

- 9 The redemption of the old activated sludge basins with the construction of new aeration basins.

Environmental objectives, plans and programs related to the North-Pest Wastewater Treatment Plant:

- 1 Inspection of the effect of the treated wastewater on the Danube.
- 2 Inspection of the effect of the wastewater sludge on the environment.
- 3 Inspection of the environmental effect of the chemical gases emitted into the air.
- 4 Utilization of the created wastewater sludge.
- 5 Decreasing the environmental noise nuisances.
- 6 Inspection of the polluting effect of showers and diluted waters on the Danube.

The Company has regulated waste management, more precisely the tasks related to hazardous materials. The 2006 waste management plan was also finished, which reflects the aspects issued for the national plan as well as the regional objectives. Besides complying with all obligations regarding the data supply and permitting pertaining to waste, the greatest results of waste management in 2006 were the followings:

- Five phases of the waste landfill have environment usage permits.
- The fourth phase of the Csomád landfill was finished during the reporting period.
- In 2006, experiments were carried out at the North-Pest Wastewater Treatment Plant for the recycling of wastewater sludge in agriculture.
- For the purpose of optimizing sludge management and enhancing the efficacy of the technological system, laboratory experiments were carried out with the addition of chemicals of various quality.
- The Company has transformed its waste and hazardous waste registry system.
- The possibility of selective waste collection was created at the central sites.

We completed all tasks related to the protection of air cleanness for the entire Company. The Company has entirely performed the air purity measurements and data supply obligations. Currently, air suction and treatment is 100% at the covered installations of the two treatment plants.

In order to prevent odour formation and outflow – at the critical points of the network – biofilters placed in pitches are operated. For the purpose of odour elimination, we have performed the odour closing of 119 sinkholes and odour closing installations have been put instead of 71 sewer covers in 2006.

In the framework of energy rationalization, the unification of the heating systems of the installations located at 19 and 21 Kerepesi site was realized, resulting in the stopping of one furnace. In the digestion units operated at the South-Pest Wastewater Treatment Plant, the recycling of biogas – gained from organic waste – is under way. The energy necessary for the operation of the plant is more and more coming from the digestion of organic waste. In 2006, the Company has spent almost HUF 94 million on research and experimental development. Cooperation with the universities and research centres affected almost all fields of operation. The Research and Development Group was created during the year, which deals with the enhancement of the efficiency of applied technologies and the development of new technologies and methods. In 2006, external and own research related to the optimization of the treatment activity and wastewater collection as well as the traceability of transport works. The Company applied and won funds at the tender of NKFP in partnership with the Faculties of the Budapest Technical and Economics University and an industrial partner. The object of the project is pre-treatment experiment of physico-chemical-based wastewater, its total budget for the 2006-2008 period is HUF 452 million.

The inspection of wastewater discharges

We have placed great emphasis on the inspection of the origins of the public sewage damages caused by industrial outputs. As a result of legal obligations – in the case of industrial factories emitting considerable load – the number of self-controls has increased.

The inspection of the wastewater emitters as well as the self-control inspections are carried out by the accredited central laboratory and wastewater sampling unit operating according to ISO standards. The revision of the accreditation in 2006 at both units was successful. Considerable technical developments were carried out in the laboratories between 2003 and 2006, the measurement technique investments necessary to comply with the current legislation have been performed. The new central laboratory was finished during 2006, which disposes of the most modern measurement techniques on a surface of 700 m² and even satisfies the measurement requirements of the 21st century.

On the basis of contracts for the use of receiving locations for communal liquid waste, the control of the suppliers was also carried out during the reporting period.

Activities of the year 2006

Activity	No. of measurements	
	2005	2006
Inspection of business units	531	538
Inspection of complaints of the population	125	63
Number of self control sampling	885	935
The control of the transfer of the communal the liquid waste	2 553	2 353
Project documentation opinion	240	309
Number of samples processed at the laboratory	20 227	21 305
Number of laboratory analyses	99 488	90 809

Quality of effluent wastewater

We inspect the quality of wastewater running into the Danube as receptor within the framework of the self control agreement concluded with the Central-Danube-Valley Environmental Protectorate. The results of the inspections are recorded in a modernized data management system. Partner organizations are continuously informed of the results.

The trend of harmful substances led into the Danube via the sites of the Company kg/year

Year	COD	Organic eluting solvent extract	Total nitrogen	Phosphorus
2002	66 275 464	5 533 592	6 615 212	1 171 011
2003	60 174 527	4 005 975	6 482 266	1 070 177
2004	54 554 307	3 517 474	6 831 992	1 142 162
2005	54 051 006	3 149 767	5 760 390	1 012 649
2006	55 825 965	3 958 477	6 272 491	1 120 267

The obligation of the Company, (in accordance with the Public Utilities Service Contract concluded with the Municipality) is not to increase the contaminant load of the Danube in comparison to last year (up to 20% load increase) and not to allow the quality parameters of the wastewater of the treatment plants to worsen in comparison to 1996. Their evolution by plant is the following:

South-Pest Wastewater Treatment Plant

The capacity of the plant is 80.000 m³/day, while its actual daily water output is 60.50 m³, its load was 75.6% in the reporting period. The third cleaning grade of a same capacity makes possible the removal of nutrient (phosphorus and nitrogen) at the full quantity. The parameters of the treated wastewater effluent from the plant have changed as follows since 1996:

Water quality parameters of the South-Pest plant in mg/l

Component	Effluent water quality		Planning threshold	Threshold from June 1, 2003
	1996	2006		
COD	70,0	40,0	50	50
BOD ₅	12,6	10,2	10	
Floating matter	21,0	5,4	35	100
NH ₄ nitrogen	25,7	1,6	0	2
Total phosphorus	2,4	0,9	1	1,8

As it is apparent from the table, there has been significant water quality improvement since 1996 while its impact on the Danube at Soroksár will only be detectable in the future.



North-Pest Wastewater Treatment Plant

The capacity of the North-Pest Wastewater Treatment Plant is 200,000 m³/day. Its load in 2006 was 75%. The great load activated sludge treatment process is completed by a partial chemical phosphorous removal process.

Water quality parameters of the North-Pest plant in mg/l

Component	Effluent water quality		Planning value	Threshold
	1996	2006		
COD	52,0	58,8	93,0	75,0
Floating matter	13,7	7,9	32,0	100,0
NH ₄ nitrogen	14,1	17,7	27,0	25,0
Total phosphorus	4,9	2,1	4,0	5,0

There is partial nutrient removal carried out in the plant, there is no nitrification. In 2006, at the North-Pest Wastewater Treatment Plant, the average hydraulic load was 150,000 m³/day, which complies with the current capacity. However, the 2006 yearly 45,900 kg BOD₅/day average nutrient load considerably exceeded the planned average 25, 500 kg BOD₅/day value.

The quality parameters of the effluent wastewater either decreased or did not increase in the same extent as the average nutrient load exceeded the capacity.

The concentration of COD and N-NH₄ of the cleaned effluent water in 2006 was higher than the figure of 1996. However, the daily average load of the site increased by a rate exceeding 20% compared to the 1996 level, from 21 million m³ to 55 million m³. In relation with Budapest, the increase of the treated water quantity represents an essential amelioration.

In its decision number 30709-3/03, the Environmental Protection Inspectorate has set an individual threshold in terms of the quality of discharged treated water. This is significantly more restrictive in terms of the COD and N-NH₄ than the threshold set in the establishing permit – and thus the threshold used for planning. In spite of all this, the quality parameters of the cleaned water were below the planned value and the individual threshold.

Major risks and uncertainties observed in relation with environment protection

The quantity of wastewater discharged via the public sewers has been continuously decreasing since the beginning of the 1990's, hence the emission concentration shows an increasing trend. The Company has no control on the quality of the collected wastewater and their treatment equipment park is also given. Based on this, the greatest risk is given by the followings:

- The current capacity does not make it possible to treat all the wastewater generated in Budapest.
- The individual thresholds defined on the basis of the decrees in force adopted during EU harmonization are stricter that they used to be.
- The calculation method of the penalty also changed in an unfavourable manner.

On the basis of the above, the rate of wastewater penalty shows an increasing trend until the Csepel central and the South-Buda wastewater treatment plants are finished.

The quality control of the rainwater sewers leading to small streams will have to be resolved in the near future. This means the increase of the number of sampling and laboratory examinations, and at sections where no pre-treatment unit is available before the terminal point, the increase of the wastewater penalty should increase.

Developments expected in the field of environment protection

In the coming years, considerable sewer utility developments from own sources and capital city sources are expected. The quantity of wastewater discharged from the existing treatment plant increases and their quality ameliorates:

- In 2006, the construction of the main sewer draining the wastewater from North-Buda and located under the river bed was finished, as a consequence of which the cleaned wastewater quantity increases and the load on the Danube decreases.
- The construction of the third phase of the treatment starts at the North-Pest Wastewater Treatment Plant and the diminution of the nitrogen content becomes possible.
- For the purpose of the realization of the environment friendly method of sludge management as well as the diminution of costs, putrefaction towers are being built at the North-Pest plant.
- At the South-Pest Wastewater Treatment plant, the objective is the complete coverage of the pre-mechanic unit and the 100% treatment of the sucked air.

The number of treatment plants increases:

- The realization of the Csepel central wastewater treatment plant is under way.
- The design of the South-Buda wastewater treatment plant is under way.

After the commissioning of the two new treatment plants, the treatment of the total wastewater quantity created in Budapest becomes possible.



Human resources

In 2006 the human resources activity was mainly determined by the strategic targets and the achievement of the tasks of the Company defined in the Shareholders' Agreement. These activities also played a role in achieving the 2006 business goals of the Company, efficiency was increased and the Company continuously maintained its operational capacity and stability.

A staff decrease of 2% was included in the staff plans, however, for the purpose of realization of the strategic objectives, the staff stagnated at the 2005 level despite the natural decrease of staff and the rationalization of the staff of the Maintenance Department. The yearly statistical staff was 1,129 persons.

Average number of employees

Description	2005		2006	
	persons	%	persons	%
Blue-collar	731	64,69	723	64,04
White-collar	378	33,45	386	34,19
Total full time	1 109	98,14	1 109	98,23
Part-time	21	1,86	20	1,77
Total staff	1 130	100,00	1 129	100,00

In the reporting period the employment of 74 people was terminated. During the year, 65 people were recruited.

Distribution of job terminations

Reason for job termination	persons
Mutual agreement	22
Employee's normal resignation	1
Termination within probation period	1
Employer's normal termination	10
Expiry of work permit	-
Extraordinary termination	8
Retired	24
Premature retirement	-
Sickness retirement	2
Deceased	6
Total job terminations	74

Wages

In 2006, based on the wage-increase provided by the Municipality of Budapest in the fees but upon the approval by the investors, an exceeding 5.25% wage increase was implemented. The utilization of the wage increase happened in three steps based on an agreement with the Workers' Council and the Trade Union. In the first step, a basic wage increase of 5.25% was implemented from 1 April not retroactively. In the second step, an amount equalling half a month of base salary of the employees was paid out in May, while the third step involved the payment of one month of base salary to the employees in November as premiums from the floating salary.

Government Decree 316/2005. (XII.25.) entered into force regarding the compulsory wages (minimum wages) and the definition of the guaranteed wage minimum. Between the years 2006-2008, the requirements related to the minimum wage must be implemented on 1 January of every year. The guaranteed wage minimum must be defined on the basis of education and practice time and has entered into force from July 1, 2006. Further requirements related to the guaranteed wage minimum must be implemented from January 1 of every year in the 2007-2008 period.

Wage costs were further increased as opposed to the plan by the HUF 13,571 thousand related to the minimum wage correction and the guaranteed wage minimum, as well as the wages HUF 86,892 thousand ensured from the flood protection special coverage. These, combined with the additional staff compared to the plan resulted in a wage increase of 9.5%.

The development of the labour cost in thousand HUF

Description	2005	2006	Index %
Full-time blue-collar workers	1 515 029	1 670 480	110,3
Full-time white-collar employees	1 238 511	1 334 608	107,8
Total full-time employees	2 753 540	3 005 088	109,1
Part-time workers	25 791	26 640	103,3
Remunerations on assignments	44 820	61 764	137,8
Total payroll for employees	2 824 151	3 093 492	109,5
Remunerations	42 339	44 736	105,7
Total payroll	2 866 490	3 138 228	109,5

In 2006, the average wage of all employees of the Company reached HUF 2,740,028/person/annum, which is higher than the previous year's HUF 2,499,249/person/annum by 9.6%. The average wage without the salaries paid out during the flood will constitute the wage increases of the coming year, that is: HUF 2,663,065/person/annum.

In order to increase professional education and the level of quality, we spent HUF 22,253 thousand on education and trainings. We treat courses leading to skills in a



profession as prime importance. The IT and language trainings of our employees were also continuous. Education and trainings ensured the complex achievement of the tasks, compliance with the new requirements and the development of competences. We were among the first in the country to complete an under water construction diver course included in the National Training List (OKJ). For the purpose of ensuring skilled labour supply in the national water sector and within the Company, this was the third year to continue the professional training resulting in a sewer operator OKJ diploma.

In the field of holidays, 5 holiday resorts were at the disposition of employees for their and their families' regeneration (with a total of 154 places), three with continuous opening and two with seasonal opening. In 2006, 1,629 people took this opportunity (employees and their family members). We have ensured group wise holiday opportunity to 100 persons among the children of our employees in the summer holidays.

Within the framework and possibilities provided by the law on health services – the Company's corporate health service was ensured to the employees in 2006 as well with regular medical checks and job suitability control, but also dental services. Besides, the services provided – upon payment – to employees of FCSM Mélyépítő, UPONOR, and Enviroduna Ltd. based on contracts concluded with them. For the purpose of prevention of infectious diseases, the Company's employees were regularly provided with vaccinations - and extraordinary ones in case of floods.

Employees could take part at preventive (large intestine cancer examination, ultrasonic diagnosis, women's oncology, men's PSA prevention) examinations for the purpose of health protection.

We have financed the housing loans from the amounts of re-payment of previous loans. In 2006, this coverage exceeded HUF 30 million. The amount provided non-interest bearing (reimbursable) loans for 35 people – for home building, purchasing and modernization – in the value of HUF 24,600 thousand.

The 72-room worker's hostel operating at the upper level of the Soroksári avenue operated with an average occupancy of 89% in 2006. The accommodation equipped with a dining room, a lounge and a smoking area at each level had an average of 64 occupants.

In 2006 the Company provided meal contribution to its employees, in the value of HUF 4,500 /person/month.

IT technology

During the previous years, the Company put its IT infrastructure on new grounds. In 2005, it introduced the server-based network client system. As an effect of the experience gathered during system administration, the server park ensuring the operation was moved from Kerepesi site to an installation exclusively dedicated to server locating in 2006. During previous operation, electricity shortcuts caused problems several times.

Another reason for the server relocation was safety, this way, both physical access and its control, air conditioning, fire and asset protection and safe electricity supply are resolved at a professional level. With the relocation of the server park, the connection of the Kerepesi site with the server centre had to be resolved. Currently, the connection is ensured by a fiberglass-based network. The Company performed the network building by using its own resources.

The realization of the technological pilot projects took place during the year at the external network client sites – primarily at the North-Pest, the South-Pest and the Ferencváros pump station – to control its operation. As a result of the pilot, the inclusion of the external sites into the thin client system can be started in 2007.

During 2006, the Company planned and introduced the barcode-based warehouse registry system. The operation of the system is ensured by mobile and cable barcode reader devices at both the central and the site warehouses. The cable barcode reader devices fit into the network client system. A radio network was installed for the operation of the mobile devices.

The introduction of the SZOLINFO system went on in 2006, the testing of certain modules was started. The trial operation of the SZAK and SZOLÁR modules is expected for 2007.

The sewer network registry program was extended by a new module in the reporting period. Inspection results used to be transferred to the system manually. The new function made it possible to transfer the data from the IKAS sewer inspection program into the new system automatically, without manual data input.

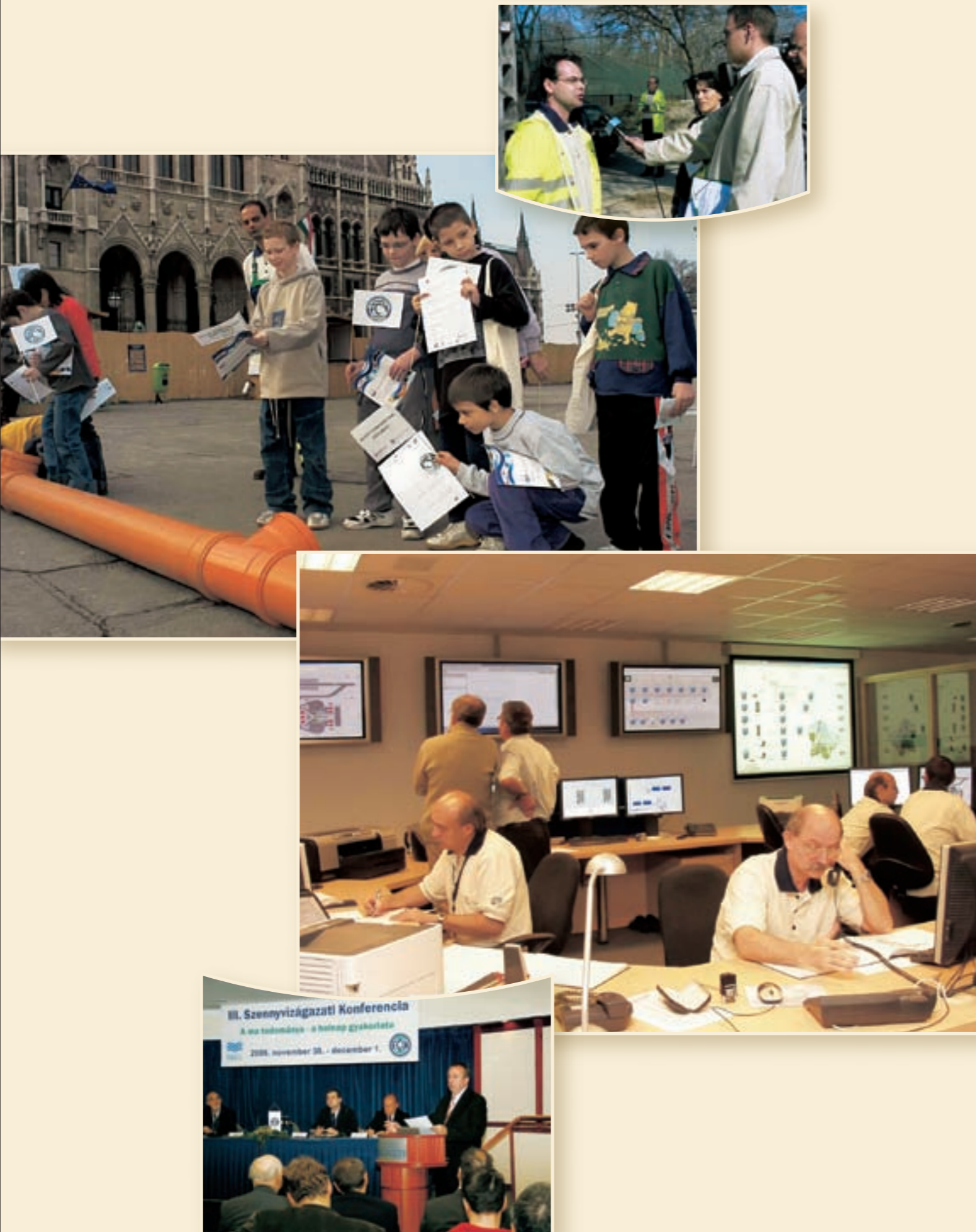
At the Tímár site, the computer and telephone systems have also been renewed simultaneously with the renovation of the administration building. In the new IT room of the building, all network devices – previously operating in a decentralized manner – were also placed besides the servers.

Communication

The Budapest Sewage Works Company – thanks to its own enormous investments and those of the Municipality of Budapest, as well as the technological know how of its professional investors – has left its old role behind and has by now become the country's biggest environment management company. Complying with today's environment protection requirements and challenges, apart from our core tasks, we deal with water and air purity protection, waste management, and even the production of bioenergy.

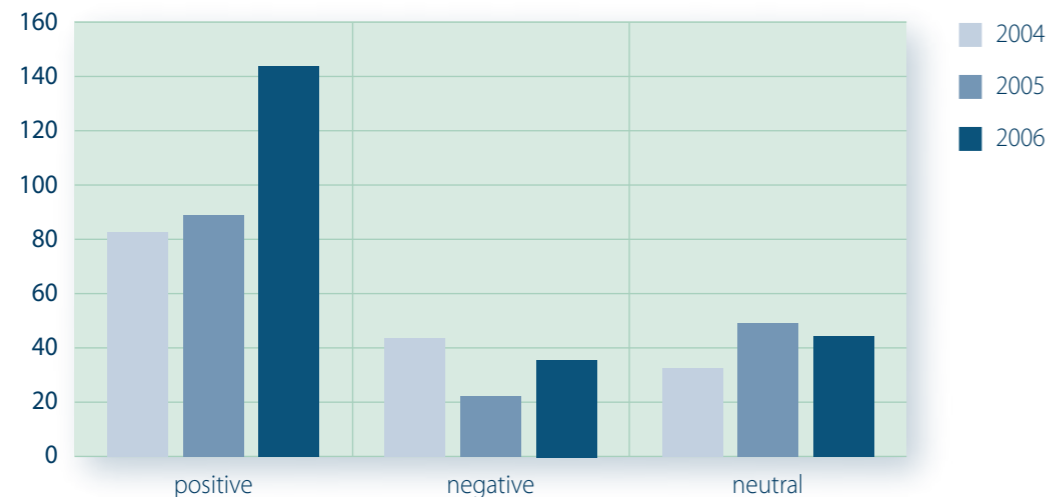
Our long-term communication objective is to communicate this quality change. For this purpose, we have organized several events in 2006. At the beginning of the year, we have drawn the attention of the general public to the bioenergy production at South-Pest and thus environment management with the visit of mayor Gábor Demszky. In professional circles, the national Wastewater Industry Conference created and organized by the Company gave an obvious opportunity for communication. The growing up generation - as an important target group - got to know our environment protection and environment management role during our events for the International Water Day. Our events were well coloured by the short film "Bioenergy" that presented the production of electric and heat energy from wastewater sludge. The Company's general brochure also represents this new direction. Our new corporate brochure is distributed not only to the participants of the listed events, but also to visitors arriving to the sites and not least our customers visiting our customer service office. We have reinforced our media facings with paid articles in some leading papers.

The communication of 2006 was greatly determined by the record level floods. FCSM is the only water public utility service company in the country to have flood protection tasks as well. In spring, we have successfully fought the highest ever icefree water level of the Danube (860 cm). In the most critical period, 800 persons fought day and night in shifts hammering away with the quickly coming and slowly going flood. Everybody was recognised for this commitment. The value of the performance is well shown by the fact that the mayor attended the ceremony of handover of the honours, some of our colleagues received separate recognition from the Municipality of Budapest and the leader of the flood protection even received a state recognition at the national ceremony. During the fight against nature, we issued press releases every day and were shown in almost all media. While we protected Budapest from the 2002 flood so that the general public basically knew nothing about it, we appeared in almost one hundred printed and electronic media coverage in 2006. We have prepared a compilation of the television coverage. We have presented this 20-minute film and the short PR film made about the flood protection to our employees.



Through the flood protection communication, we had 40 % more media coverage than last year. Some 170 articles and more than 60 radio and TV programs dealt with the activities of our Company. 65% of coverage was positive, 19% was neutral and 16% was negative.

Evolution of media coverage



Our positive image was also enhanced by our programs organised at several locations for the occasion of the International Water Day. The wastewater treatment plant open days are now considered traditional, where some 800 students could get acquainted with the cycle of water and the importance of environment protection. By connecting to the program of the Municipality of Budapest, some 12,000 adults and children could follow the presentation of the sewer cleaning and camera inspection, watch our short films and participate in our game-like water experiments on the square in front of the Parliament. Although these events got only little media attention, we offered a possibility to gather experience to some 13,000 people.

Though some of our events did not catch the centre of media attention, their PR value was all the more considerable. Such was the recognition given to policemen for the efficient help provided in the flood protection, which strengthened our relationship with the authorities.

Our most prestigious event was not followed by media echo either, but the visit of the deputy prime minister of China was all the more honourable for us. The second highest ranked person of the Chinese government was expressly curious about Hungary's currently most modern wastewater treatment plant.

We were proud to show him our developments so far to satisfy his professional interest. At the visit of Zeng Peiyan, Miklós Persányi, minister for environment protection and water affairs was also present on behalf of the state.

The already mentioned 3rd Wastewater Industry Conference did not catch media attention either, which event strengthened our sectoral, professional relationships.

We serve the 1.7 million inhabitants of Budapest every day. Apart from the mediation of the media, we regularly communicate with them via the back of the issued invoices as well as through our newsletter published every quarter. Our customers can call our call-centre out of office hours, 24 hours a day. Interactivity is ensured by our central supervision that can be called day and night. With the help of one of the most modern centres of the country, we are able to react faster to complaints from costumers and to failures. Our customers had the opportunity to personally meet the Company's top management at the series of programs called Open Municipality. In the organization of the Municipality of Budapest, relocated public service customer service offices operated in various districts during five weekends.

An important communication tool is the internet portal through which our informative data are available continuously, twenty four hours a day and in the quickest manner. Apart from our own website, we pursue a continuous dialogue with the organizations dedicated to environment protection via the portal of the "greens", the Greenfo.

Our publications unified in their image all serve the transfer of information. We have already mentioned our renewed brochure and newsletter. The English version of the South-Pest plan brochure is also finished. In the meantime, our publication about the Company's own patent, the settlement-free sinkhole was so much demanded that we have already run out of its second edition.

We have prepared short films about several activities of the Company. Apart from the short films called Bioenergy and Flood Protection, a short film was also shot on the management of small streams. On the basis of one of the film producing companies of the Hungarian public television, we have shot two longer films as well: The First Hungarian Pump Station and The First Hungarian Water and Sewer Network. Both films were aired twice at the program "Hungarian Firsts" (Magyar Elsők) on m1 channel.

The Company's image was basically not affected by the transformation from limited company to private limited company. Since there was no complete name change, we have performed minimal formal transformations in the emblem, preserving the font, colour and forms of the image. We have not changed the slightly changed emblem in all media elements simultaneously. Naturally, the change was made on the fascias, papers, envelopes, but we will proceed to a gradual change on vehicles, business cards and smocks.

Sponsoring, as a PR tool is also primarily at the service of the environment. As the greatest environment management company of the country, we consider it our core task to support environment protection initiatives and environment-aware education. Furthermore we spend more and more every year on decreasing the fee payment liability of disadvantaged families and contribute considerable amounts to Hungarian competition sports.

Appendix



6.) We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Qualification

7.) The revenues of Fővárosi Csatornázási Művek Zrt. are based on actual water consumption and sewer usage metered by an independent third party. Billed water consumption and sewer usage information was not fully available for certain consumers as of the balance sheet date. In these cases, revenues were accrued based on estimates made by management. Billed water consumption and sewer usage information is expected to become available in the first six months of 2007. In the absence of this information, we were unable to satisfy ourselves as to the completeness of accrued income stated at HUF 2,417 millions. Any adjustment which may become necessary based on a comparison of billed consumption and the disclosed accrued income, may have the impact of increasing/reducing net sales and the after-tax profit with a retrospective effect.

Opinion

8.) We have audited the elements of and disclosures in the annual financial statements, along with underlying records and supporting documentation, of Fővárosi Csatornázási Művek Zrt. in accordance with Hungarian National Auditing Standards and, except for the matter referred to in preceding paragraph, have gained sufficient and appropriate evidence that the annual financial statements have been prepared in accordance with the Hungarian Accounting Law and with generally accepted accounting principles in Hungary. In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the completeness of the accrued revenue, the annual financial statements give a true and fair view of the equity and financial position of Fővárosi Csatornázási Művek Zrt. as at 31 December 2006 and of the results of its operations for the year then ended. The business report corresponds to the disclosures in the financial statements.

Budapest, March 23, 2007
except for the dividend payment of MHUF 3,219 for the year ended 31 December, 2006, as to which the date is 25 May, 2007.


Ernst & Young Kft.
Registration No.: 001185


Havas István
Registered Auditor
Registration No.: 003395

**This is a translation of the Hungarian Report
Independent Auditors' Report**

To the Shareholders of Fővárosi Csatornázási Művek Zrt.

1.) We have audited the accompanying 2006 annual financial statements of Fővárosi Csatornázási Művek Zrt. ("the Company"), which comprises the balance sheet as at 31 December 2006 - showing a balance sheet total of HUF 111,381 millions and a profit after tax for the year of HUF 3,311 millions -, the related profit and loss account for the year then ended and the summary of significant accounting policies and other explanatory notes.

2.) We issued a qualified opinion on the Company's annual financial statements as at 31 December 2006 on March 24, 2006 on the following grounds:
The revenues of Fővárosi Csatornázási Művek Rt. were based on actual water consumption and sewer usage metered by an independent third party. Billed water consumption and sewer usage information was not fully available for certain consumers as of the balance sheet date. In the absence of this information, we were unable to satisfy ourselves as to the completeness of accrued income stated at HUF 2,382 millions.

Management's Responsibility for the Financial Statements

3.) Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Hungarian Accounting Law and generally accepted accounting principles in Hungary. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

4.) Our responsibility is to express an opinion on these financial statements based on the audit and to assess whether the business report is consistent with the financial statements. Except as discussed in paragraph 7 we conducted our audit in accordance with Hungarian National Auditing Standards and with applicable laws and regulations in Hungary. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

5.) An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. Our work regarding the business report is restricted to assessing whether the business report is consistent with the financial statements and does not include reviewing other information originated from non-audited financial records.

Balance sheet

in million HUF

a	b	c	d	e
Description		Previous year	Modific. of prev. year(s)	Current year
01.	A. Fixed assets (02.+10.+18. lines)	95 028		99 306
02.	I. INTANGIBLE ASSETS (03.-09. lines)	51		66
03.	Capitalised foundation/restructuring			
04.	Capitalised research and development			15
05.	Concessions, licences and similar rights	12		9
06.	Trade-marks, patents and similar assets	39		42
07.	Goodwill			
08.	Advance payments for intangible assets			
09.	Adjusted value of intangible assets			
10.	II. TANGIBLE ASSETS (11.-17. lines)	94 829		98 885
11.	Land and building and related property rights	87 766		91 382
12.	Plant, machinery, equipment and vehicles	3 847		4 258
13.	Other equipment, fixtures and fittings, vehicles	581		511
14.	Breeding stock			
15.	Assets in the course of construction	2 635		2 734
16.	Prepayments for capital expenditures			
17.	Adjusted value of tangible assets			
18.	III. LONG-TERM FINANCIAL ASSETS (19.-25. lines)	148		355
19.	Long-term participations in related parties	72		72
20.	Long-term loans granted to related parties			
21.	Other long-term investments			200
22.	Long-term loans granted to other investments			
23.	Other long-term loans granted	76		83
24.	Long-term debt securities			
25.	Adjusted value of financial investments			

Balance sheet

in million HUF

a	b	c	d	e
Description		Previous year	Modific. of prev. year(s)	Current year
26.	B. Current assets (27.+34.+40.+45. lines)	11 239		9 534
27.	I. STOCKS (28.-33. lines)	167		199
28.	Raw materials and consumables	167		198
29.	Work in progress and semi finished products			
30.	Animals for breeding, fattening and livestock			
31.	Finished products			
32.	Goods			
33.	Advance payments for stocks			1
34.	II. RECEIVABLES (35.-39. lines)	3 965		4 294
35.	Trade debtors	3 308		4 011
36.	Receivables from related parties	53		81
37.	Receivables from other investments			
38.	Bills of exchange receivables			
39.	Other receivables	604		202
40.	III. SECURITIES (41.-44. lines)	6 850		3 773
41.	Participations in related parties			
42.	Other participations			
43.	Treasury shares and own participation			
44.	Marketable debt securities	6 850		3 773
45.	IV. LIQUID ASSETS (46.-47. lines)	257		1 268
46.	Cash, cheques	2		1
47.	Bank deposits	255		1 267
48.	C. Prepaid expenses and accrued income (49-51. lines)	2 528		2 541
49.	Accrued income	2 394		2 425
50.	Prepaid expenses	134		116
51.	Deferred expenses			
52.	TOTAL ASSETS (01.+26.+48. lines)	108 795		111 381

Balance sheet

in million HUF

a	b	c	d	e
53.	D. Shareholders' equity (54.+56.+57.+58.+59.+60.+61. lines)	93 835		93 927
54.	I. ISSUED CAPITAL	70 045		70 045
55.	of which: treasury shares redeemed at face value			
56.	II. ISSUED CAPITAL NOT PAID (-)			
57.	III. CAPITAL RESERVE	13 557		13 557
58.	IV. RETAINED EARNINGS / (LOSSES)	9 420		10 233
59.	V. ALLOCATED RESERVES			
60.	VI. REVALUATION RESERVE			
61.	VII. PROFIT OR LOSS FOR THE YEAR	813		92
62.	E. Provisions (63.-65. lines)	1 965		1 599
63.	Provisions for contingent liabilities	1 965		1 599
64.	Provisions for future commitments			
65.	Other provisions			

Balance sheet

in million HUF

a	b	c	d	e
66.	F. Liabilities (67.+71.+80. lines)	1 681		2 057
67.	I. SUBORDINATED DEBTS (68.-70. lines)			
68.	Subordinated debts to related parties			
69.	Subordinated debts to other investments			
70.	Subordinated debts to third parties			
71.	II. LONG-TERM LIABILITIES (72.-79. lines)	244		0
72.	Long-term borrowings			
73.	Convertible bonds			
74.	Debts from the issue of bonds			
75.	Investment and development loans			
76.	Other long-term loans			
77.	Long-term debts to related parties			
78.	Long-term debts to other investments			
79.	Other long-term liabilities	244		
80.	III. CURRENT LIABILITIES (81. and 83.-89. lines)	1 437		2 057
81.	Short-term borrowings			
82.	of which: convertible bonds			
83.	Other short-term loans			
84.	Prepayments received from debtors			
85.	Creditors	602		483
86.	Bills of exchange payable			
87.	Short-term debts to related parties	3		1
88.	Short-term debts to other investments			
89.	Other current liabilities	832		1 573
90.	G. Accrued expenses and deferred income (91.-93. lines)	11 314		13 798
91.	Deferred income			20
92.	Accrued expenses	10		11
93.	Deferred extraordinary revenues and negative goodwill	11 304		13 767
94.	TOTAL LIABILITIES (53.+62.+66.+90. lines)	108 795		111 381

Profit and loss statement

in million HUF

a	Description b	Previous year c	Modific. of prev. year(s) d	Current year e
01.	Domestic sales, net	28 227		29 272
02.	Export sales, net	14		20
I.	Total sales, net (01.+02.)	28 241		29 292
03.	Direct cost of sales	12 988		13 951
04.	Cost of goods sold			2
05.	Provision of (consignment) services	40		53
II.	Direct costs of sales (03.+04.+05.)	13 028		14 006
III.	Gross sales (I.-II.)	15 213		15 286
06.	Selling and marketing costs	35		35
07.	Administration costs	1 118		1 133
08.	Other general overhead	836		955
IV.	Indirect costs of sales (06.+07.+08.)	1 989		2 123
V.	Other revenues	13 312		13 278
	of which: diminution in value	7		36
VI.	Other expenditures	16 161		16 981
	of which: reserved diminution in value	213		237
A.	OPERATING PROFIT/(LOSS) (±III.-IV.+V.-VI.)	10 375		9 460

Profit and loss statement

in million HUF

a	Description b	Previous year c	Modific. of prev. year(s) d	Current year e
09.	Dividends and profit-sharing (received or due)	10		13
	of which: dividends from related parties	10		13
10.	Exchange gains disposal of shares			
	of which: from related parties			
11.	Interest and capital gains on long-term financial assets			
	of which: from related parties			
12.	Other interests and similar income (received or due)	692		505
	of which: from related parties			
13.	Other revenues from financial transactions	87		64
VII.	Financial revenues (09.+10.+11.+12.+13.)	789		582
14.	Exchange losses on long-term financial assets			
	of which: from related parties			
15.	Interest payable and similar charges			
	of which: from related parties			
16.	Diminution in the values of shares, securities and bank deposits			
17.	Other expenditures on financial transactions	20		50
VIII.	Financial expenditures (14.+15.+16.+17.)	20		50
B.	FINANCIAL PROFIT OR LOSS (VII.-VIII.)	769		532
C.	PROFIT OR LOSS OF ORDINARY ACTIVITIES (±A.±B.)	11 144		9 992
IX.	Extraordinary revenues	398		427
X.	Extraordinary expenditures	5 693		5 413
D.	EXTRAORDINARY PROFIT OR LOSS (IX.-X.)	-5 295		-4 986
E.	PROFIT BEFORE TAX (±C.±D.)	5 849		5 006
XI.	Tax payable	1 817		1 695
F.	PROFIT AFTER TAX (±E.-XI.)	4 032		3 311
18.	Dividends and profit-sharing paid from retained earnings			
19.	Dividends and profit-sharing paid (payable)	3 219		3 219
G.	PROFIT OR LOSS OF THE YEAR (±F.+18.-19.)	813		92

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