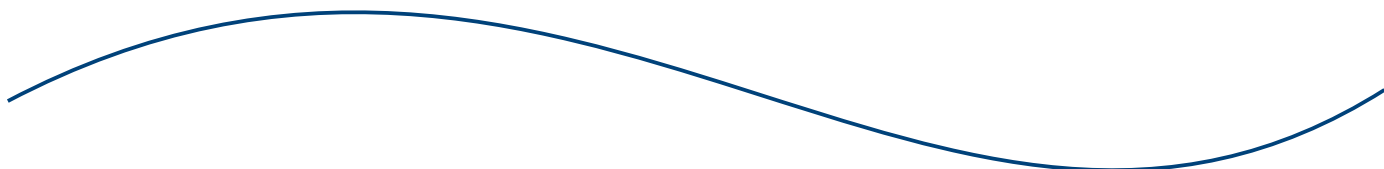




2006
Annual report



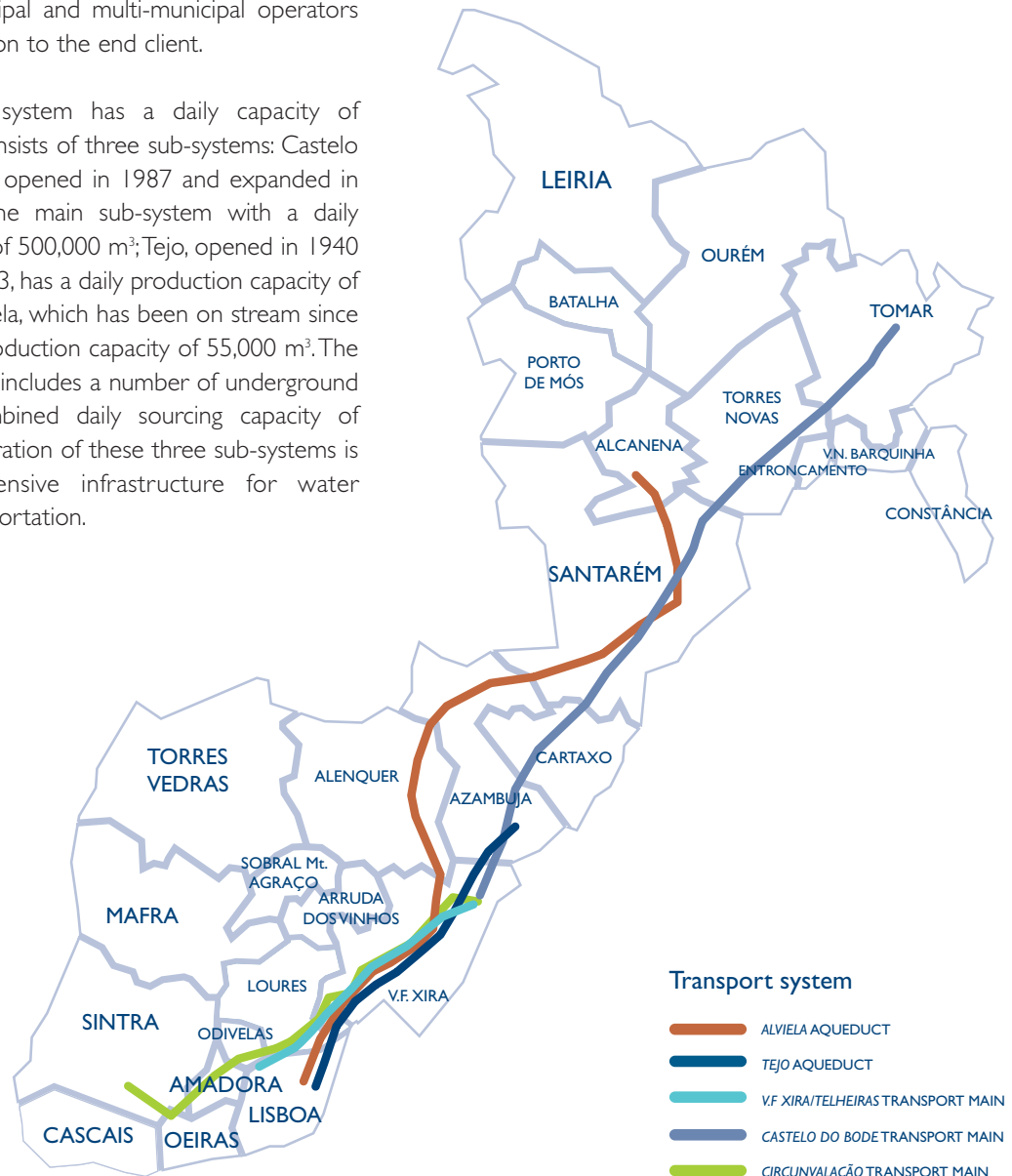
EPAL - Empresa Portuguesa das Águas Livres, S.A.
Annual report 2006



PROFILE

EPAL was originally founded in 1868 and its shares are ultimately held by the Portuguese state. Since 1993, its direct, sole shareholder has been ADP - Águas de Portugal, a state-owned holding company with operating affiliates in the water and waste sectors. EPAL's mission is to supply, directly or through third-party distributors, high-quality drinking water to 2.6 million people in Lisbon and 25 other counties north of the Portuguese capital. One of EPAL's main concerns is to produce and supply water in strict obedience of economic, social and environmental principles. The company's system for producing, transporting and distributing water includes 745 km of transport mains and 1,427 km of water mains for distribution in Lisbon where it had 344,530 contract-holding clients. Outside the Lisbon region, water is supplied to municipal and multi-municipal operators that ensure distribution to the end client.

EPAL's production system has a daily capacity of 1,045,000 m³ and consists of three sub-systems: Castelo do Bode, which was opened in 1987 and expanded in 1996, is currently the main sub-system with a daily production capacity of 500,000 m³; Tejo, opened in 1940 and expanded in 1963, has a daily production capacity of 220,000 m³; and Alviela, which has been on stream since 1880, with a daily production capacity of 55,000 m³. The Tejo sub-system also includes a number of underground springs with a combined daily sourcing capacity of 270,000 m³. The operation of these three sub-systems is supported by extensive infrastructure for water treatment and transportation.



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Garrulus glandarius

KEY INDICATORS

Operations

Volumes/capacities in cubic metres (m³)

	2002	2003	2004	2005	2006
Supplied water, m ³	219,42,927	221,650,618	222,720,242	218,850,664	211,237,773
Number of direct clients	334,671	336,564	339,111	341,924	344,690
Number of consumers ¹	2,500,204	2,556,955	2,577,629	2,594,033	2,608,042
Water supplied by consumer, m ³	87.8	86.7	86.4	84.4	81.0
Number of supplied counties	24	26	26	26	26
Supplied area, km ²	5,292	5,443	5,406	5,406	5,406
Renewed water mains, km	54	81	56	85	65
Water lost/Water abstracted, %	17.5%	16.8%	17.0%	14.8%	13.9%
Daily abstraction capacity	1,047,000	1,047,000	1,047,000	1,047,000	1,045,000
Daily production capacity	1,017,000	1,017,000	1,047,000	1,047,000	1,045,000

¹Resident population in the supplied area

Profit and loss account

Amounts in million euros

	2002	2003	2004	2005	2006
Revenue from water sales	125,023	131,146	136,464	134,034	134,424
Other revenue	4,762	5,051	5,802	5,639	4,482
Total revenues	129,785	136,197	142,266	139,673	138,906
Revenue from water sales/Total revenues, %	96.3%	96.3%	95.9%	96.0%	96.8%
EBITDA ¹	48,032	61,825	69,002	65,684	57,875
Depreciation charges	26,262	27,221	26,961	27,189	27,899
EBIT ²	21,770	34,604	42,041	38,495	29,976
Profit before tax	13,484	29,529	36,665	33,295	23,265
Net income	9,378	20,436	26,024	23,788	16,329
Cash flow ³	44,911	54,851	60,689	56,344	52,289

¹Earnings before interest, tax, depreciation and amortisation

²Earnings before interest and tax

³Net income plus depreciation and provisions

Balance sheet

Amounts in million euros

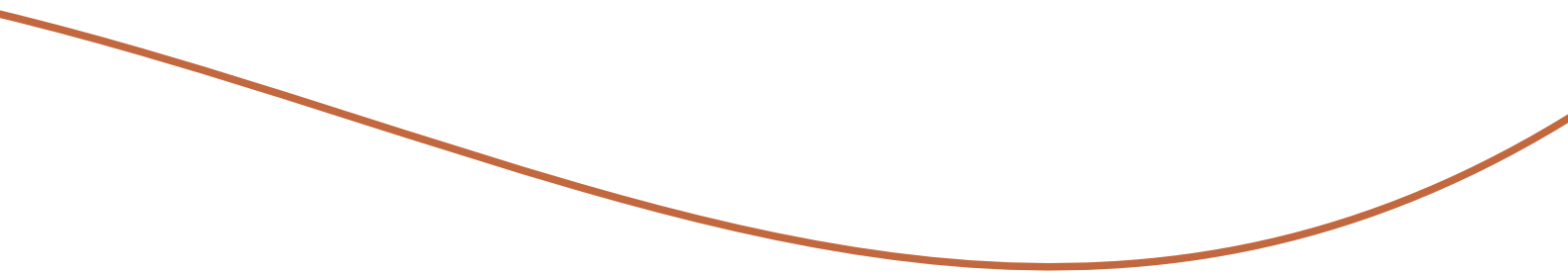
	2002	2003	2004	2005	2006
Share capital	150,000	150,000	150,000	150,000	150,000
Shareholders' equity	322,452	334,548	343,093	345,906	343,780
Revaluation reserves	107,150	104,110	101,340	118,165	114,105
Liabilities	282,435	316,031	332,276	341,880	371,405
Net total assets	604,887	650,580	675,369	687,786	715,185
Equity/Net total assets, %	53.3%	51.4%	50.8%	50.3%	48.1%
Medium- and long-term bank indebtedness	137,457	143,380	143,605	175,208	202,190
Capital expenditure ¹	45,301	39,950	59,520	57,372	57,195
Return on equity, %	2.9%	6.1%	7.6%	6.9%	4.7%
Return on assets, %	1.6%	3.1%	3.9%	3.5%	2.3%

¹New, gross of depreciation



Luscinia megarhynchos





MANAGEMENT REPORT



Buteo buteo

CHAIRMAN'S STATEMENT



João Manuel Lopes Fidalgo
Chairman

In 2006, EPAL accomplished once again its mission of supplying and distributing water and the smooth course of its operations and the quality of its service are evidenced by several indicators.

Indeed, increasingly demanding goals for efficient resource management led the company to a good financial performance level despite a further contraction in water consumption.

At the same time, after reflecting upon the future, the board sponsored a number of actions - using the services of external consultants as and when required - aimed at reviewing the strategy to develop the company in terms of its sustainable management, the diversification of its operations and its alignment with an integrated water cycle management. From this review several initiatives and decisions followed that impacted both internal and external relationships.

In this context, the board reviewed two essential documents - the Master Plan (*Plano Director*) and the General Network Plan (*Plano Geral da Rede*) - whereby structural solutions were considered for the satisfaction of demand in a 20-year time horizon, taking into account risks to water supply.

The strategic management of the Lisbon distribution network proceeded in the year through its segmentation into Monitoring and Control Zones (*Zonas de Monitorização e Controlo* or ZMCs). Only by measuring

and classifying network performance is it possible to reduce detection and reaction lags as well as identify and quantify non-invoiced water. In 2006, 35 ZMCs were created that provided daily data for analysis covering 16% of the clients and 25% of the network. In the transport network 13 macro-measurement projects were initiated with a view to completing the works in 2007.

In the preparation of the 2007 budget and upon the aforementioned review of the general and master plans, the company undertook the development of a new capital budgeting policy for the purpose of rationalising capital employed. Accordingly, internal expert panels were set up for the formulation of renovation strategies by processing available data including renovation costs, repair costs as well as the age, past behaviour and criticality of existing infrastructure. Next step will be the implementation of an integrated model for the management of physical assets.

Reorganisation of the purchasing function led to the creation of a new structure in the company - the Logistics Department (LOG). This new unit was charged with the task to centralise and standardise buying processes that were hitherto scattered across the company resulting in a variety of procedures and inadequate control systems.

Stressing the importance of its relationship with clients, the company launched on 15 May 2006 - Consumer Day - a communication campaign aimed at projecting an

image of EPAL along three lines: service quality and dependability, process innovation, social and environmental responsibility.

Management of the company's human resources was strengthened in 2006, whereby knowledge management became an all-present ingredient in traineeships for a start in working life and in proposals for discontinuing employment relationships. Particular emphasis was also given to training and professional development programmes.

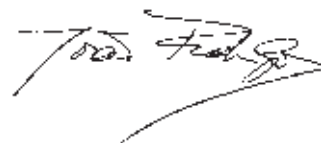
On 17 November 2006 the board decided to terminate the labour agreement (*Acordo de Empresa*) in force and presented a proposal to the unions consisting primarily of a change in the retirement plan towards a defined contribution scheme and the deletion of provisions made redundant by developments in labour law.

Besides complying with the government's guidelines, as jointly expressed by the Finance and Environment ministries, these negotiations are a unique opportunity for reflection on the outlook for EPAL's development as

a sustainable business enterprise and a major player in the Portuguese water sector.

Concerns about EPAL's financial sustainability as measured by the return on invested capital adjusted for the company's business risk are reflected in the relevant regulatory framework. For this reason, a working group on regulation was set up and a study was launched with the support of specialist consultants for the purpose of analysing regulatory models adapted to EPAL's specific features. It is our belief that this is a strategic issue requiring the attention of the board, the shareholder, the regulators and the government. The transparency of this process is essential for its credibility and adequate incentives must be created for improving service without added risk to invested capital.

As a closing remark, I should like to emphasise that EPAL published in 2006 its first sustainability report, a further token of the company's awareness of its responsibilities in terms of environmental ethics and social responsibility towards the communities in which it operates.



João Manuel Lopes Fidalgo
Chairman

MISSION AND OBJECTIVES

Mission

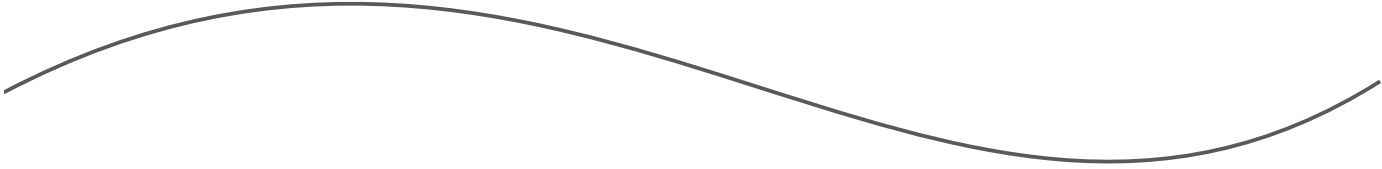
The mission of EPAL - Empresa Portuguesa das Águas Livres, S.A. is to supply water for human consumption in its service area and to ensure product quality and respect for essential social and environmental aspects while using its capabilities in the national interest.

Objectives

- Customer satisfaction through superior service levels
- Environmental sustainability
- Adequate return on invested capital



Streptopelia turtur



CORPORATE GOVERNANCE

Shareholder

EPAL is ultimately held by the Portuguese state and its sole direct shareholder is Águas de Portugal, SGPS, SA, the holding company of a group of water and waste treatment operators that includes EPAL.

Águas de Portugal was created in 1993 and is wholly owned by the Portuguese state. Group companies provide services to more than seven million inhabitants in Portugal in such fields as water supply, wastewater treatment and processing and recycling of solid waste.

Governing bodies

EPAL's general meeting committee is chaired by AMEGA - Associação de Municípios para Estudos e Gestão da Água, represented by Carlos Alberto Dias Teixeira, with Cristina Rebelo Pereira as vice-chairperson and Alexandra Varandas as secretary.

The general meeting convened once in 2006 to pass a resolution on the management report and accounts of 2005 and the proposed appropriation of net income for the year.

Supervision of the company is the responsibility of sole auditor António Dias Nabais, chartered accountant, and Joaquim Manuel da Silva Neves, his deputy.

The company's executive body is the board of directors, which has been elected for the 2005-2007 period and is composed of João Manuel Lopes Fidalgo, chairman, and Jorge Luís Ferrão de Mascarenhas Loureiro, José Alfredo Manita Vaz, António Bento Franco and Rui Manuel de Carvalho Godinho, directors.

In 2006, the board of directors met 47 times to decide on management objectives and policies, activity and investment plans and to manage the ordinary business affairs of the company.

According to article 8, paragraph 3. d) of the company's articles of association, it is the general meeting's responsibility to pass a resolution on the remuneration of governing body members for which purpose it may appoint a remuneration committee.

At the general meeting of 31 March 1992 a remuneration committee was set up whose current members - Pedro Eduardo Passos da Cunha Serra and Maria de Fátima Ferreira Pica Ferreira Borges - were elected at the general meeting of 9 June 2005. The last meeting of the remuneration committee was held on 15 May 2006.

The total amount of remunerations received by the members of the company's executive body in the financial year ended 31 December 2006 was the following:

Unid: Euros

	Annual remuneration
General meeting committee:	
Chairman	Attendance fee, 633.40
Vice-chairman	Attendance fee, 475.00
Secretary	Attendance fee, 316.70
Sub-total	Attendance fee, 1,425.10
Sole auditor	
António Dias Nabais (Chartered accountant)	17,911.88
Sub-total	17,911.88
Board of directors:	
Chairman of the board of directors [1] [2] [3]	135,964.50
Executive director I [2] [3]	126,787.50
Executive director II [2] [3]	126,787.50
Executive director III [2] [3]	126,787.50
Executive director IV [2] [3]	126,787.50
Sub-total	643.114,50
GRAND TOTAL	661,026.38 + 1,425.10 in attend. fee

[1] Amount paid to AdP SGPS.

[2] Includes amount pertaining to a retirement plan (PPR).

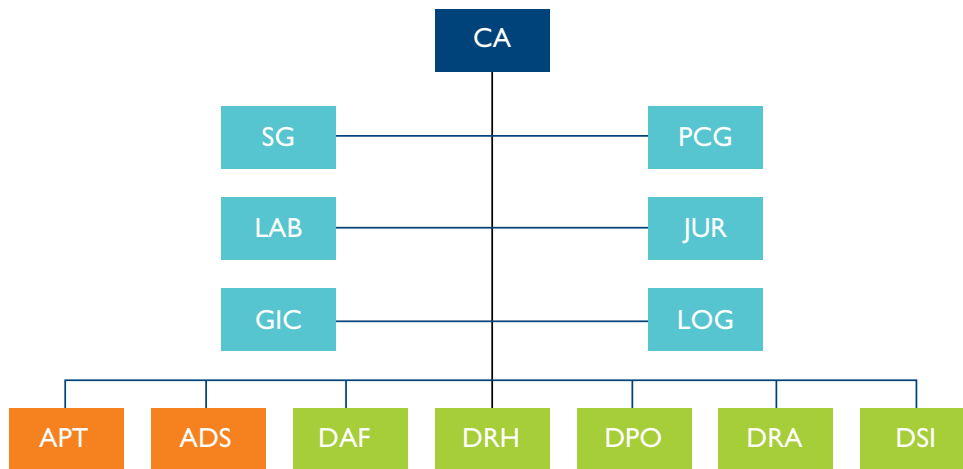
[3] The remuneration does not include a variable component because it is not applicable.

In order to appraise environmental issues, the company has an Environmental Impact Board chaired by Maria Helena

Veríssimo Colaço Alegre and of which Maria Paula Batista Antunes and Manuel Duarte Pinheiro also are members.

Organisational structure

The company's organisational set-up is illustrated by the following chart:



CA: Board of directors

SG: Company secretary

GIC: Communications Department

PCG: Department for Planning and Control

JUR: Legal Department

LAB: Central Laboratory - whose main responsibilities are the design, implementation and management of the Water Quality Monitoring Programme covering EPAL's entire supply system as well as all surface and underground abstractions

LOG: Logistics Department

APT: Production and Transport Division - whose remit covers all abstractions, treatment stations and transport mains for water production and transportation

ADS: Distribution Division - whose brief consists of the management and maintenance of the network used for the supply of water to residential customers in the county of Lisbon

DAF: Department for Administration and Finance

DRH: Human Resources Department

DPO: Projects and Works Department

DSI: Information Systems Department

DRA: Department for the Renewal and Expansion of the Lisbon Network

The Water Museum (MDA) and the Workgroup for Monitoring and Control (GMC) report directly to the board of directors.

Standards and regulations

In its day-to-day operations, EPAL enforces obedience to the law. The company's activities are laid down in a government decree of 1991 (Decreto-Lei nº 230/91 of 21 June) which approved its articles of association. A number of other specific rules are applicable to its operations covering the production and distribution of drinking water:

There are four kinds of internal rules:

- **Ordens de serviço**

Documents issued by the board of directors which are binding upon the whole company and deal with over-

riding matters such as the allocation of tasks to board members, EPAL's organisational structure, powers of attorney, among others;

- **Procedimentos administrativos**

Documents dealing with roles and processes of a predominantly administrative nature;

- **Procedimentos operativos**

Documents dealing with roles and processes regarding the abstraction, production, treatment, transportation, distribution and measurement of water as well as maintenance work;

- **Instruções de trabalho**

Documents describing in detail one or more specific tasks in a process.



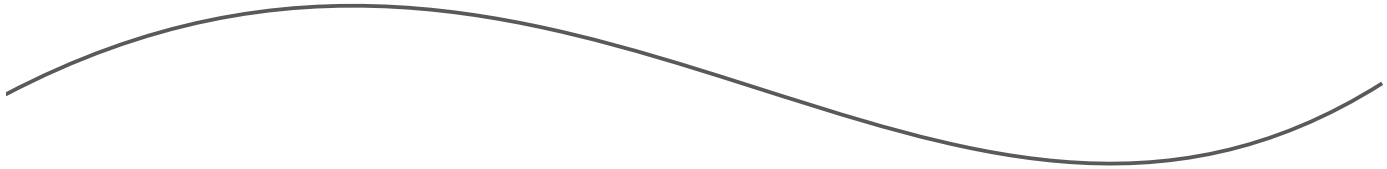
Board of Directors:

João Manuel Lopes Fidalgo, *Chairman*

Jorge Luís Ferrão de Mascarenhas Loureiro, António Bento Franco,
José Alfredo Manita Vaz e Rui Manuel de Carvalho Godinho, *Directors*



Turdus merula



FROM PRODUCTION TO DISTRIBUTION

The supply of drinking water by EPAL is preceded by an elaborate process of abstraction, treatment and transport.

In order to supply 2.6 million consumers - directly in the Lisbon area and indirectly in 25 counties north and west of the capital through municipal and multi-municipal distributors - EPAL has 745 km of transport mains and 1,427 km of water mains for urban distribution.

Production

EPAL operates a system with a daily production capacity of close to 1,045,000 m³. This infrastructure consists of three sub-systems:

- **Castelo do Bode**, with a daily production capacity of 500,000 m³ of water abstracted from the surface;
- **Tejo**, with a daily production capacity of 220,000 m³ of surface water and close to 270,000 m³ of groundwater;
- **Alviela**, with an average daily production of 55,000 m³ of spring water.



Operation of these three sub-systems is supported by a vast infrastructure for the transportation of abstracted and treated water.

The total volume of water abstracted in 2006 was 244,350,667 m³. The volume of water produced after treatment was 244,063,092 m³, with the difference representing process water resulting from treatment operations.



Distribution

EPAL supplies water to the following municipalities for further distribution to end consumers:

Sintra	Ourém	Cartaxo
Loures/Odivelas	Torres Novas	Batalha
Oeiras/Amadora	Alcanena	Torres Vedras
Cascais	Porto de Mós	Arruda dos Vinhos
Vila Franca de Xira	V. N. da Barquinha	Sobral de Monte Agraço
Mafra	Constância	Azambuja
Tomar	Leiria	Alenquer
Entroncamento	Santarém	

To Torres Vedras, Arruda dos Vinhos, Sobral de Monte Agraço, Azambuja and Alenquer water is supplied through Águas do Oeste, a multi-municipal company. The volume supplied to distributors in 2006 was 150,662,222 m³, down 3.96% on 2005.

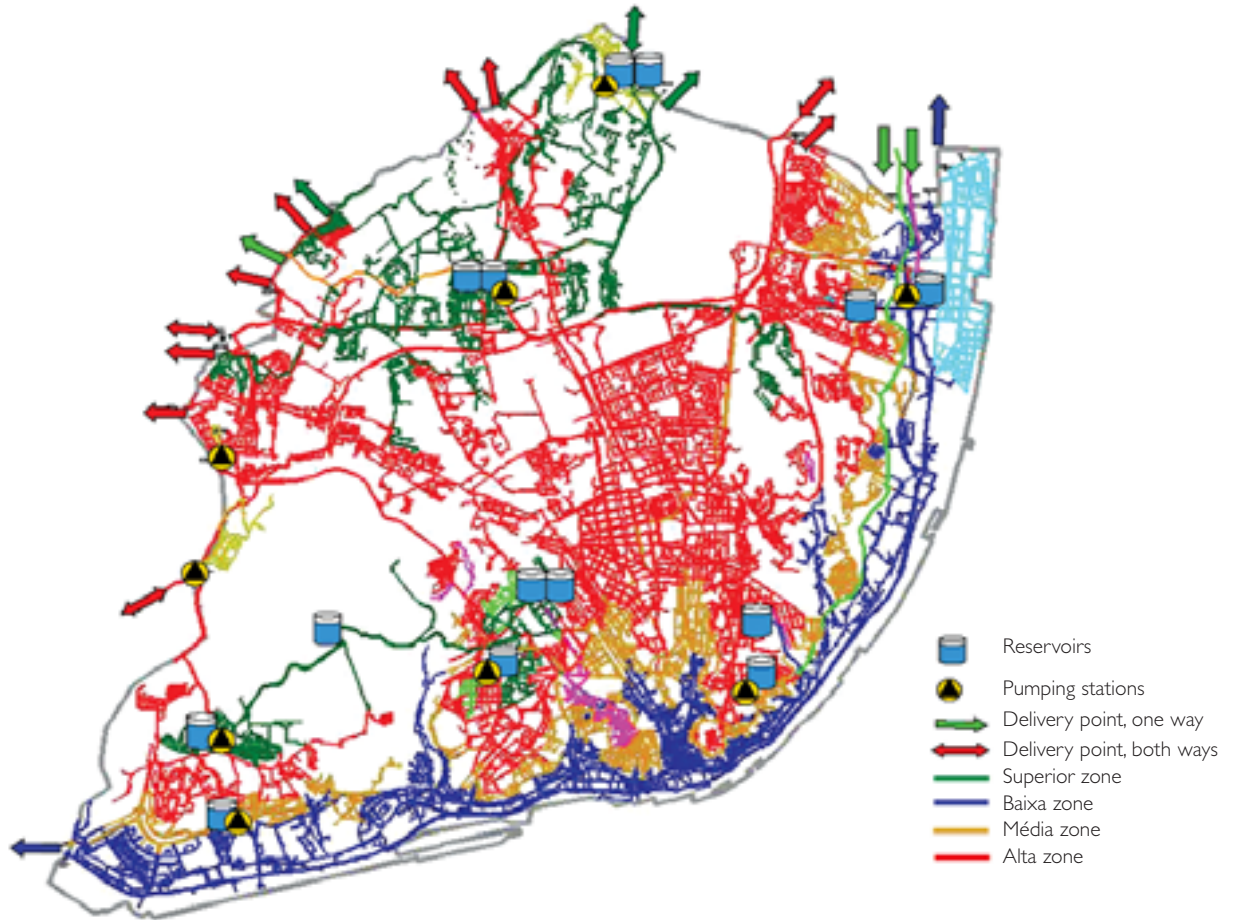
In Lisbon, EPAL distributes water directly to end clients. The distribution network has 1,427 km and consists of 14 reservoirs, 9 pumping stations and 90,000 supply pipes. This infrastructure supports the supply of water to an area of 85 km² with 519,795 inhabitants (according to

the National Statistics Bureau's estimate for 31 December 2005). The network is fed by the Alviela and Tejo aqueducts and the Vila Franca de Xira-Telheiras and Circunvalação transport mains, whose daily capacities to supply Lisbon are 35,000 m³, 360,000 m³, 240,000 m³ and 60,000 m³, respectively.

The distribution network is divided into four altimetric zones of increasing height - *Baixa*, *Média*, *Alta* and *Superior* - defined according to the city's topography.



Water distribution in Lisbon

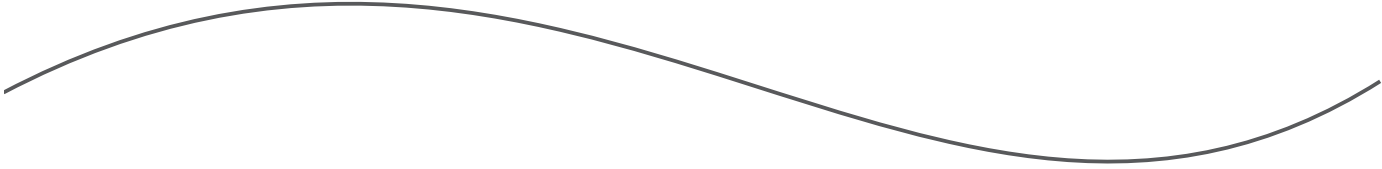


The volume of water supplied to clients in the distribution area was 59,719,197 m³, a 1.8% decrease compared to

the year before, which was due to a large extent to the company's own campaigns for the rational use of water:



Erithacus rubecula



WATER QUALITY

EPAL's system for managing water quality ensures process and parameter control along the abstraction, treatment, transportation and distribution stages. Quality control is ensured by the company's central laboratory (LAB) and the laboratories of Asseiceira and Vale da Pedra.

Monitoring

The central laboratory is responsible for the design, implementation and management of the Water Quality Monitoring Programme (PMQA). In 2006 the LAB completed the schedule provided for in the PMQA for sampling and analysis of the water abstracted on the surface and in the ground, transported, supplied to distributors and distributed in the city of Lisbon. The programme's purpose was to obtain data for the support and guidance of management actions towards ensuring water quality.

The PMQA that has been approved by EPAL's board of directors consists of two types of control: legal control and operational or 'surveillance' control. While legal control refers to supervision by the water and waste regulator

(Instituto Regulador de Águas e Resíduos, IRAR) regarding enforcement of the legal requirements EPAL must obey in its capacity as supplier of water for human consumption - the purpose of operational or 'surveillance' control is to check the quality of drinking water in the whole supply system as well as to timely detect possible failures, either occasional or systematic, for effective preventive action to be taken. Under the PMQA particular attention is given to monitoring microbiological standards and residual chlorine through daily sampling.

Under the programme 7,239 samples were taken at 264 fixed points representing the whole EPAL system - abstractions, water treatment stations, transport mains, points of delivery to distributors and the Lisbon distribution network - and at 1,352 sampling points in consumer taps in Lisbon. A total of 174,709 tests were performed for a variety of substances and species determining water quality, whose distribution is shown in Table 1.

EPAL had also operational control plans for water quality at the Castelo do Bode and Tejo sub-systems, which were entirely executed.

Tests performed in 2006 in EPAL's supply system

	Number of tests (species)
Legal control	
Lisbon network	
(Consumer taps)	21,875
Deliveries to distributors	45,366
Direct clients outside Lisbon	1,110
Operational/surveillance control	
Underground abstractions	8,783
Surface abstractions	5,815
Water treatment station (process water)	312
Transportation system	44,798
Lisbon network (fixed points)	46,650
Total	174,709

Tests performed in 2006 for operational control

Operational process control	Number of tests
Laboratory control at Asseiceira	74,200
Laboratory control at Vale da Pedra	194,790
Total	268,990

Findings

Water quality at source

At the abstraction level used during the year by EPAL at the Castelo do Bode dam lake, no result was found above the maximum recommended values (VMRs) as defined by government decree *Decreto-Lei n° 236/98* for classes A1/A2/A3 for the temperature parameter:

The incidence of pH values, total coliforms, fecal coliforms and streptococci, though it was found to be of a systematic nature, was easily solved by the treatment system at the Asseiceira station, which has been confirmed by the results found when monitoring treated water flowing out of the station. These values were never in non-conformity with the quality standards set out in *Decreto-Lei n° 243/2001*.

Despite the high quality of the drinking water produced after treatment at Asseiceira, EPAL is aware that it is imperative to protect the abstraction zone as provided for by law, particularly when abnormal values are recorded at levels that are close to the surface.

The incidence of abnormal values of total coliforms and chemical oxygen fault at Rio Tejo - Valada Tejo was not

considered to be systematic and was eliminated by treatment at Vale da Pedra as borne out by the monitored microbiological quality of the water coming out of the station.

At Rio Alviela - Nascente dos Olhos de Água abstracted water proved to be mineralised. In 2006 no analytical test was recorded with values that were higher than the maximum acceptable values (VMAs) established for Class I in accordance with article 16, n°3 of *Anexo I* to *Decreto-Lei n° 236/98*.

Water abstracted from underground sources in the limestone aquifers at Ota and Alenquer was classed as rather mineralised, hard and with a low content of clorets and sulphates. In 2006 one single analytical test was found with higher values than the VMA established for Class I in accordance with article 16, n°3 of *Anexo I* to *Decreto-Lei n.° 236/98*.

Water abstracted from the aquifer under the flood plains of the Tejo basin and dating back to the Miocene was classed as rather mineralised, averagely hard, with clorets and sulphates. In these underground abstractions, the temperature and barium parameters recorded levels exceeding the VMA for Class I according to *Decreto-Lei n° 236/98*. Underground abstractions from sedimentary deposits at Poços de Valada were classed as very mineralised water:





Quality of drinking water

The number of tests performed for controlling water quality against the legal requirements of *Decreto-Lei n.º 243/2001* reached 21,875, with residential and public taps fed by the Lisbon distribution network (at hospitals, schools, health centres) sampled on a daily basis.

Data analysis of the tap samples led to the conclusion that, except for a few isolated, non-recurring cases, the water complied with the quality standards required by Portuguese law. Only in 0.23% of the cases did tests produce non-conforming values.

In comparison with 2005, there was a broad improvement in the quality of the drinking water

supplied by EPAL. This was confirmed by a lower number of non-compliances, in both absolute and percentage terms, in the samples of water distributed in Lisbon (legal and operational controls) and delivered to distributors.

EPAL disclosed monthly on its website statistical data about the compliance tests performed in water taken at consumer taps in Lisbon, at fixed sampling points in the Lisbon distribution network and at points for delivery to distributors.

In 2006 the report *Quality of drinking water supplied by EPAL in 2005* was published where data were disclosed about compliance with the applicable quality standards.

EPAL's drinking water supply system
 Quality of drinking water delivered on consumers tap at the city of Lisbon
 N. of sampling points: 1059

N° of DETERMINATIONS: 18,309			Det. n°PV: 31		SAMPLING PERIOD: YEAR / 2006	
Parameter	N. of SAMPLES		Determined Value		Parametric Value (DL n. 243/2001)	N. Samples + Parametric Value
	Analyzed	Frequency	Maximum	Minimum		
Parameters of Check Monitoring 1.	4057					47
Total Chlorine (mg/L Cl ₂)	1353	26 x Semans	1.3	0.03	-	-
Free Chlorine (mg/L Cl ₂)	1353	26 x Semans	1.13	0.02	-	-
Coliform bacteria (ufc/100 mL)	1352	26 x Semans	>300	0	0	41
E.coli (ufc/100 mL)	1352	26 x Semans	300	0	0	5
Parameters of Check Monitoring 2	12,525					1
Colony count at 37°C (ufc/mL)	825	16 x Semans	>300	0	without discernible alteration	-
Colony count at 22°C (ufc/mL)	825	16 x Semans	>300	0	without discernible alteration	-
Coliform bacteria (ufc/100 mL)	825	16 x Semans	1	0	0	1
Colour (mg/L Pt-Co)	823	16 x Semans	3.77	-2.00	20	0
Turbidity (NTU)	823	16 x Semans	3.17	-0.400	4	0
Odour (Dilution rate at 25° C) *	823	16 x Semans	0	0	3	0
Taste (Dilution rate at 22° C) *	823	16 x Semans	0	0	3	0
pH (pH unit)	823	16 x Semans	8.89	7.26	7.65 ≤ pH ≤ 8.0	0
Temperature of measurement of pH(°C)	823	16 x Semans	27.3	-	-	-
Permanganate Index (mg/L O ₂)	823	16 x Semans	2.68	-0.40	5.0	0
Conductivity (µS/cm at 25° C)	823	16 x Semans	549	121.1	2500	0
Ammonia (mg/L NH ₃)	823	16 x Semans	0.09	-0.070	0.50	0
Nitrate (mg/L NO ₃)	823	16 x Semans	-0.0050	-	0.5	0
Nitrite (mg/L NO ₂)	823	16 x Semans	4.77	1.2	50	0
Aluminium (µg/L Al)	823	16 x Semans	86.1	-60.0	200	0
Iron (µg/L Fe)	34	2 x 16s	127.0	-20.0	300.0	0
Manganese (µg/L Mn)	823	16 x Semans	27.7	-3.00	50	0
Parameters of Audit Monitoring	695					3
Enterococci (ufc/100 mL)	34	2 x 16s	8	0	0	2
Total indicator dose (coliform) **	0	-	-	-	0.10	-
Chloride (mg/L Cl)	34	2 x 16s	48.3	+15.0	250	0
Sulfate (mg/L SO ₄)	34	2 x 16s	72.6	11.5	250	0
Fluoride (µg/L F)	34	2 x 16s	3.19	71	1500	0
Bromate (µg/L BrO ₃)	34	2 x 16s	+20	-	10	0
Iodine (µg/L I ₂)	34	2 x 16s	53.8	4.33	300	0
Cadmium (µg/L Cd)	34	2 x 16s	+0.10	-	5.0	0
Lead (µg/L Pb)	34	2 x 16s	4.22	-0.00	15	0
Copper (µg/L Cu)	34	2 x 16s	+0.20	-	1.000	0
Chromium (µg/L Cr)	34	2 x 16s	+0.00	-	50	0
Nickel (µg/L Ni)	34	2 x 16s	+0.00	-	30	0
Antimony (µg/L Sb)	34	2 x 16s	+0.00	-	5.0	0
Arsenic (µg/L As)	34	2 x 16s	1.93	+0.50	10	0
Selenium (µg/L Se)	34	2 x 16s	+1.00	-	10	0
Mercury (µg/L Hg)	34	2 x 16s	+0.20	-	1.0	0
Boron (µg/L B)	34	2 x 16s	54.7	-20.0	1.000	0
Total organic carbon (mg/L C)	34	2 x 16s	3.81	-	without discernible alteration	-
Gross alpha (Bq/L) **	34	2 x 16s	0.11	-0.030	0.1	1
Gross beta (Bq/L) **	34	2 x 16s	0.19	-0.030	1.0	0
Strontium (Bq/L) **	0	-	-	-	50	-
Chloro (µg/L CH) **	33	2 x 16s	+5	-	30	0
Acrylamide (µg/L) **	0	-	-	-	0.10	-
Total THM (µg/L)	34	2 x 16s	101.8	30.3	100	0
Bromochloroform (µg/L)	34	2 x 16s	19.3	5.9	-	-
Bromoform (µg/L)	34	2 x 16s	20.2	-0.50	-	-
Chloroform (µg/L)	34	2 x 16s	49.8	4.88	-	-
Dibromochloromethane (µg/L)	34	2 x 16s	18.0	5.2	-	-
Sum of Trichloroethylene and Tetrachloroethylene (µg/L)	34	2 x 16s	0.136	-	10	0
Trichloroethylene (µg/L)	34	2 x 16s	+1.0	-	-	-
Tetrachloroethylene (µg/L)	34	2 x 16s	+1.0	-	-	-
Benz(a)pyrene (µg/L)	34	2 x 16s	-0.00180	-	0.010	0
Naphthalene (µg/L)	34	2 x 16s	+0.0140	-	-	-
Acenaphthylene (µg/L)	34	2 x 16s	+0.0220	-	-	-
Acenaphthene (µg/L)	34	2 x 16s	+0.0080	-	-	-
Fluorene (µg/L)	34	2 x 16s	+0.0190	-	-	-
Dibenz(a,h)anthracene (µg/L)	34	2 x 16s	+0.0020	-	-	-
Phenanthrene (µg/L)	34	2 x 16s	0.0160	+0.0060	-	-
Anthracene (µg/L)	34	2 x 16s	+0.0070	-	-	-
Fluoranthene (µg/L)	34	2 x 16s	0.0060	-0.0040	-	-
Pyrene (µg/L)	34	2 x 16s	+0.0130	-	-	-
Benzo(a)anthracene (µg/L)	34	2 x 16s	+0.00100	-	-	-
Crysen (µg/L)	34	2 x 16s	+0.0020	-	-	-
Total PAH class of monoaromatics ** (µg/L)	34	2 x 16s	-	-	0.10	0
Benzo(b)fluoranthene (µg/L) *	34	2 x 16s	+0.0021	-	-	-
Benzo(k)fluoranthene (µg/L) *	34	2 x 16s	+0.00150	-	-	-
Benzo(a)fluoranthene (µg/L) *	34	2 x 16s	+0.0130	-	-	-
Indeno(1,2,3-cd)perylene (µg/L) *	34	2 x 16s	+0.0200	-	-	-
Benzenes (µg/L)	34	2 x 16s	+0.30	-	1.0	0
Epichlorohydrin (µg/L)	34	2 x 16s	+0.06	-	0.10	0
1,2-dichloroethane (µg/L)	34	2 x 16s	+0.10	-	1.0	0
Vinyl chloride (µg/L)	34	2 x 16s	+0.03	-	0.50	0
Individual and total Pesticides (µg/L) **	34	2 x 16s	-	-	-	-
Pesticides Group 1 - total (µg/L) **	34	2 x 16s	-	-	-	-
Alachlor (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Atrazine (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Carbofuran (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Cimoxafen (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Desmethylatrazine (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Desethylatrazine (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Desethylterbutylazine (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Diuron (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Dimethoate (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Dinoseb (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Linoson (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Methalaxol (µg/L)	34	2 x 16s	+0.1	-	0.10	0
3-Metholaxol (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Methidathion (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Phloxin (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Pyrimethanil (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Propargil (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Sensone (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Tebuconazol (µg/L)	15	2 x 16s	+0.1	-	0.10	0
Terbufosinate (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Pesticides Group 2 - total (µg/L) **	34	2 x 16s	-	-	-	-
IPCA (µg/L)	34	2 x 16s	+0.1	-	0.10	0
1,4-D (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Benzene (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Pesticides Group 3 - total (µg/L) **	34	2 x 16s	-	-	-	-
Thymol (µg/L)	34	2 x 16s	-	-	0.10	0
Pesticides Group 4 - total (µg/L) **	34	2 x 16s	-	-	-	-
Permethrin (µg/L)	34	2 x 16s	+0.1	-	0.10	0
Pesticides Group 5 - total (µg/L) **	34	2 x 16s	-	-	-	-
Azoxystrobin (µg/L)	34	2 x 16s	+0.02	-	0.10	0
Pesticides LCPH - total (µg/L)	9	2 x 16s	-	-	-	-
Dimethoate (µg/L)	9	2 x 16s	+0.030	-	0.10	0
Cimoxafen (µg/L)	9	2 x 16s	+0.050	-	0.10	0
Carbofuran (µg/L)	9	2 x 16s	+0.005	-	0.10	0
Diuron (µg/L)	9	2 x 16s	+0.050	-	0.10	0
Linoson (µg/L)	9	2 x 16s	+0.030	-	0.10	0
Pyrimethanil (µg/L)	9	2 x 16s	+0.020	-	0.10	0
Tebuconazol (µg/L)	9	2 x 16s	+0.030	-	0.10	0

* Test not included in the accreditation scope
 ** Subcontracted and accredited parameter
 ** Subcontracted and not accredited parameter

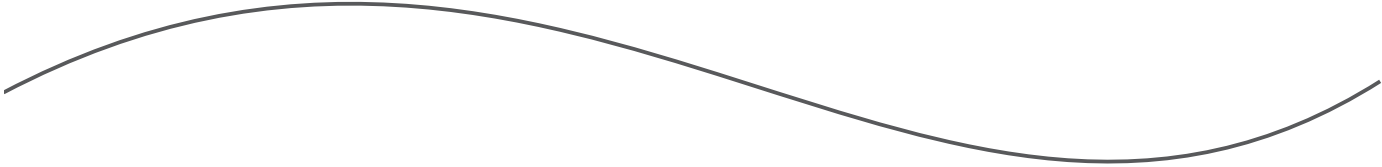
EPAL's drinking water supply system
 Quality of drinking water delivered to water supply companies
 N. of sampling points: 91

N° of DETERMINATIONS: 33,694		N° Det. > PV: 22		SAMPLING PERIOD: YEAR / 2006	
Parameter	N. of SAMPLES Analyzed	Maximum	Minimum	Parameter Values (PV) (DL n. 143/2001)	N° of Samples > Parameter Value
Parameters of Check Monitoring I					
Total chlorine (mg/L Cl ₂)	2095	3.58	0	-	0
Free chlorine (mg/L Cl ₂)	2095	3.58	0	-	0
Coliform bacteria (ufc/100 mL)	2089	16	0	0	0
E.coli (ufc/100 mL)	2089	1	0	0	0
Parameters of Check Monitoring 2					
Colony count at 22°C (ufc/mL)	766	240	0	without abnormal alteration	0
Colony count at 22°C (ufc/mL)	766	35	0	without abnormal alteration	0
Coliform bacteria (ufc/100 mL)	760	3	0	0	0
Colour (mg/L Pt-Co)	764	4.3	<=1.5	20	0
Turbidity (NTU)	863	13.9	<=0.20	4	4
Oxidor (Dilution rate at 22° C) *	764	1	0	3	0
Toxic (Dilution rate at 22° C) *	764	0	0	3	0
pH (pH unit)	686	8.7	6.92	7.65 <= 9.0	0
Temperature of measurement of pH(°C)	686	27.3	14.80	-	-
Permanganate index (mg/L O ₂)	805	3.1	0.3	5.0	0
Conductivity (µS/cm at 20°C)	2006	776	98	2500	0
Ammonia (mg/L NH ₃)	641	0.11	<=0.050	0.50	0
Nitrate (mg/L NO ₃)	641	0.0075	<=0.050	0.5	0
Nitrite (mg/L NO ₂)	3004	<=1.00	<=1.00	50	0
Aluminium (µg/L Al)	641	369	<=40.0	200	0
Iron (µg/L Fe)	145	81.7	<=20.0	200.0	0
Manganese (µg/L Mn)	641	84.6	<=5.00	50	0
Parameters of Audit Monitoring					
Staphylococci (ufc/100 mL)	1073	1	0	0	0
Total indicative dose (ind/100 mL) **	0	0	0	0.10	0
Chloride (mg/L Cl)	212	128	<=1.0	250	0
Sulphate (mg/L SO ₄)	207	140	<=0.0	350	0
Fluoride (µg/L F)	174	472	<=0	<=1000	0
Bromate (µg/L BrO ₃)	174	<=20	<=20	10	0
Sodium (µg/L Na)	209	182	<=1.00	200	0
Cadmium (µg/L Cd)	174	0.23	<=0.10	5.0	0
Lead (µg/L Pb)	145	3.3	<=3.00	25	0
Copper (µg/L Cu)	145	27.9	<=0.0	2 000	0
Chromium (µg/L Cr)	174	8.26	<=3.00	50	0
Nickel (µg/L Ni)	145	5.8	<=3.00	30	0
Antimony (µg/L Sb)	174	<=0.08	<=0.08	5.0	0
Arsenic (µg/L As)	174	3.42	<=0.50	10	0
Selenium (µg/L Se)	174	<=1.00	<=1.00	10	0
Mercury (µg/L Hg)	174	<=0.20	<=0.20	1.0	0
Boron (µg/L B)	174	145	<=20.0	1 000	0
Total organic carbon (mg/L C)	174	2.93	<=2	without abnormal alteration	0
Crystallinity (µg/L) *	149	0.14	<=0.028	0.1	0
Crystallinity (µg/L) *	149	0.21	<=0.030	1.0	0
Titanium (µg/L Ti) *	0	0	0	50	0
Cyanide (µg/L CN) *	174	7	<=5	50	0
Acrylamide (µg/L) *	1	<=0.10	-	0.10	0
Total THM (µg/L)	235	<=14.2	-	100	0
Bromodichloromethane (µg/L)	235	34.5	<=0.50	-	-
Bromoform (µg/L)	235	29.0	<=0.50	-	-
Chloroform (µg/L)	235	95.2	<=1.0	-	-
Dibromochloromethane (µg/L)	235	30.0	0.500	-	-
Sum of Trichloroethylene and Dichloroethylene (µg/L)	235	1233.000	-	10	0
Trichloroethylene (µg/L)	235	<=1	-	-	-
Tetrachloroethylene (µg/L)	235	1.2300	<=0.05	-	-
Benzenopyrene (µg/L)	145	<=0.00100	-	0.010	0
Naphthalene (µg/L)	145	<=0.0140	-	-	-
Acenaphthylene (µg/L)	145	<=0.0220	-	-	-
Acenaphthene (µg/L)	145	<=0.0080	-	-	-
Fluorene (µg/L)	145	<=0.0070	-	-	-
Dibenz(a,h)anthracene (µg/L)	145	<=0.00220	-	-	-
Phenanthrene (µg/L)	145	0.0120	<=0.040	-	-
Anthracene (µg/L)	145	<=0.00070	-	-	-
Fluoranthene (µg/L)	145	<=0.00040	-	-	-
Pyrene (µg/L)	145	<=0.0120	-	-	-
Benz(a)anthracene (µg/L)	145	<=0.00100	-	-	-
Crysen (µg/L)	145	<=0.00080	-	-	-
Total Mill Equiv of monochloro T / cell *	145	-	-	0.10	0
Acenaphthene (µg/L) *	145	<=0.0021	-	-	-
Acenaphthylene (µg/L) *	145	<=0.00150	-	-	-
Acenaphthene (µg/L) *	145	<=0.0130	-	-	-
Indeno(1,2,3-cd)fluorene (µg/L) *	145	<=0.0200	-	-	-
Benzo(a)pyrene (µg/L)	174	<=0.30	-	1.0	0
Sachharose (µg/L)	145	<=0.06	-	0.10	0
1,2-dichloroethane (µg/L)	174	<=0.10	-	2.0	0
Vinyl chloride (µg/L)	145	<=0.03	-	0.50	0
Individual and total Pesticides (µg/L) *	174	-	-	0.50	0
Pesticides Group 1 - total (µg/L) *	174	-	-	-	-
Alachlor (µg/L)	174	<=0.1	-	0.10	0
Atrazine (µg/L)	174	<=0.1	-	0.10	0
Carbofuran (µg/L)	125	<=0.1	-	0.10	0
Cimoxanil (µg/L)	125	<=0.1	-	0.10	0
Dicyclanil (µg/L)	174	<=0.1	-	0.10	0
Dicyclanil (µg/L)	174	<=0.1	-	0.10	0
Dicyclobutylamine (µg/L)	174	<=0.1	-	0.10	0
Diuron (µg/L)	174	<=0.1	-	0.10	0
Dimethoate (µg/L)	125	<=0.1	-	0.10	0
Dinocap (µg/L)	125	<=0.1	-	0.10	0
Linuron (µg/L)	174	<=0.1	-	0.10	0
Metolachlor (µg/L)	174	<=0.1	-	0.10	0
S-Metholachlor (µg/L)	174	<=0.1	-	0.10	0
Mecbuzate (µg/L)	125	<=0.1	-	0.10	0
Molinate (µg/L)	174	<=0.1	-	0.10	0
Pyrimethanil (µg/L)	125	<=0.1	-	0.10	0
Propazin (µg/L)	174	<=0.1	-	0.10	0
Simazine (µg/L)	174	<=0.1	-	0.10	0
Tebuconazol (µg/L)	125	<=0.1	-	0.10	0
Terbufosinate (µg/L)	174	<=0.1	-	0.10	0
Pesticides Group 2 - total (µg/L) *	174	-	-	-	-
MPCA (µg/L)	174	<=0.1	-	0.10	0
2,4-D (µg/L)	174	<=0.1	-	0.10	0
Bentazone (µg/L)	174	<=0.1	-	0.10	0
Pesticides Group 3 - total (µg/L) *	174	-	-	-	-
Thiopyr (µg/L)	174	<=0.1	-	0.10	0
Pesticides Group 4 - total (µg/L) *	174	-	-	-	-
Permethrin (µg/L)	174	<=0.1	-	0.10	0
Pesticides Group 5 - total (µg/L) *	174	-	-	-	-
Azinphos (µg/L)	174	<=0.02	-	0.10	0
Pesticides LCPS - total (µg/L)	49	-	-	-	-
Dimethoate (µg/L)	49	<=0.020	-	0.10	0
Cimoxanil (µg/L)	49	<=0.050	-	0.10	0
Carbofuran (µg/L)	49	<=0.005	-	0.10	0
Diuron (µg/L)	49	<=0.050	-	0.10	0
Linuron (µg/L)	49	<=0.030	-	0.10	0
Pyrimethanil (µg/L)	49	<=0.020	-	0.10	0
Tebuconazol (µg/L)	49	<=0.020	-	0.10	0

* Test not included in the accreditation scope
 * Subcontracted and accredited parameter
 ** Subcontracted and not accredited parameter



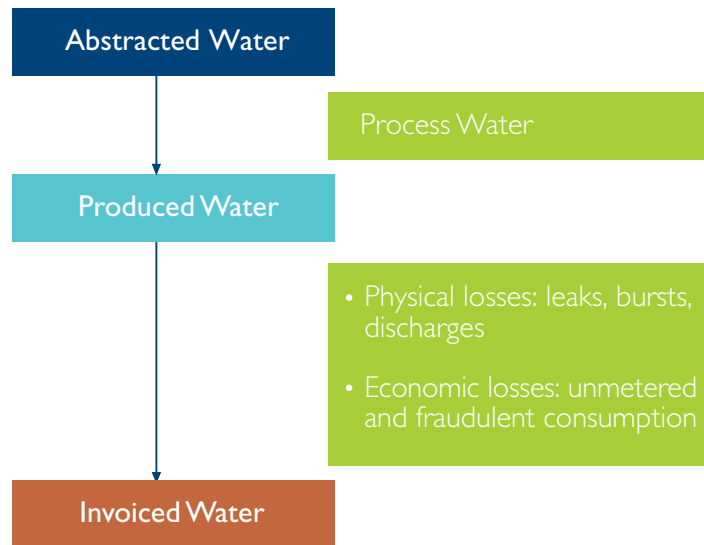
Serinus serinus



NON-INVOICED WATER

Although the difference between water abstracted and water produced may be deemed immaterial - it represents 0.1% and consists of the water that could not be recovered in treatment operations - the difference between water produced and water invoiced to both

end clients and distributors is, indeed, material and, therefore, requires permanent attention as well as prompt action as required. The following diagram illustrates the volume of water loss throughout the stages of the abstraction-to-consumption cycle:



The volume of water lost during transportation prior to arrival in Lisbon or delivery to municipal distributors reached 10.6 million cubic metres or 4.3% of water produced. In distribution, the volume lost was an additional 23.4 million cubic metres or 20.2% of the volume of water arriving in Lisbon. Total non-invoiced water was, therefore, 34 million cubic metres or 13.9% of total water abstracted.

In this context, losses as a consequence of bursts in water mains are particularly relevant. Due to the aging of its system, EPAL faces a challenge of renewing the network of mains and pipes to which it has responded with a considerable investment effort. The replacement of aged piping has led to a decline in the number of bursts as shown in the following table:

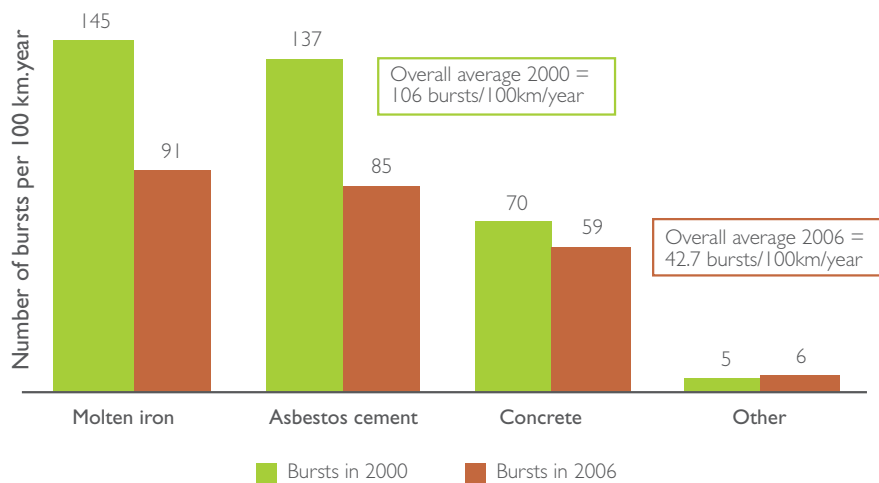
Number of bursts in mains and pipes

	2002	2003	2004	2005	2006	Change 2002-2006 %
Bursts in mains	1,294	906	724	692	601	-54%
Bursts in pipes	4,027	4,016	2,563	2,048	1,727	-57%
TOTAL	5,321	4,922	3,287	2,740	2,328	-56%

Between 2002 and 2006, 306.7 km out of the 1,427 km of mains in the Lisbon distribution network with a diameter between 110 and 1,000 mm were replaced. As a

result, the number of bursts per 100 km between 2002 and 2006 fell from 106 to 42.7 per year, as shown in the following diagram.

Number of bursts in the distribution network per 100km/year



Another indicator with relevance to loss reduction is the percentage of bursts repaired in less than 24 hours, which reached 91.5% for piping with a diameter of less than 400 mm.

The Plan for Monitoring and Control of Water Losses prepared by the Monitoring and Control Group (GMC) in cooperation with EPAL's operating units was launched in January 2006 and its purpose was to monitor and examine transportation and distribution networks - with the help of such new tools as G/Interaqua, Epanet and

telemetrics - as well as take appropriate action for reducing non-invoiced water.

In distribution, the primary objective was to implement Monitoring and Control Zones (ZMCs) and Monitoring and Transport Zones (ZMTs) across the whole network. Segmentation in ZMCs will allow EPAL to map the distribution system, to shorten detection and reaction lags in case of network failures, to improve client service and system reliability, to manage proactively as well as identify non-invoiced water resulting from both real and





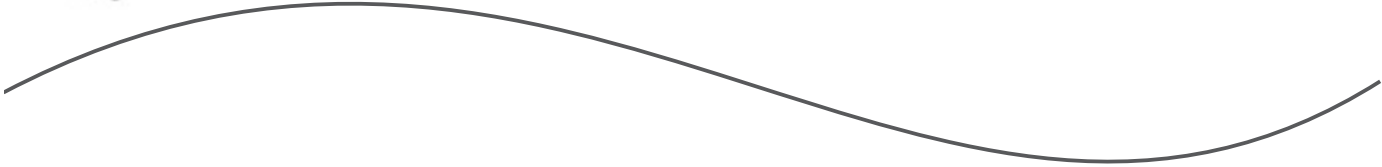
apparent losses. Up to December 2006, 35 ZMCs had been implemented covering 56,000 clients or 16% of the total and 276 km or 23% of the network.

During the year, an innovative computer application named *IMC - Integration, Monitoring and Control* was developed for the purpose of processing the data collected from the ZMCs by the telemetrics and telemanagement systems.

In December, the board of directors approved the first inspection of the large transport mains with the help of SAHARA, a system developed in the UK by the Water Research Centre. SAHARA is an advanced system for the detection and location of bursts by acoustic methods which also allows viewing and inspection of the mains' inner part by remote TV. The first inspection trials were scheduled for March 2007 in the Vila Franca de Xira/Telheiras transport mains, in the mains for untreated water at Valada Tejo and at selected locations in the larger mains in the Lisbon network's Média and Baixa zones.



Athene noctua



CAPITAL EXPENDITURE

Investment spending totalled 57.2 million euros in 2006, which was in line with the 57.4 million euros spent the year before. Total expenditure is broken down below by strategic area:

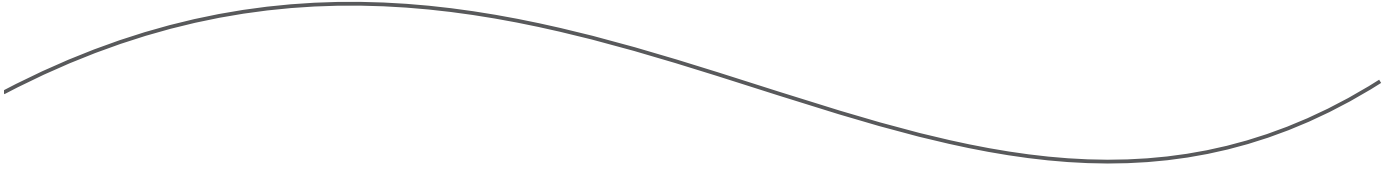
	euros
Certainty of supply	46.175,668
Enlargement of the Castelo do Bode sub-system	6,785,629
Enlargement of the treatment station at Asseiceira	15,613,453
Duplication of the stretch between Quinta da Marquesa and the plant at Vila Franca de Xira	10,898,916
Upgrade of supply to Mafra	4,963,511
Renewal of 63 km in the distribution network	13,501,866
Quality guarantee	766,809
Renewal of laboratory equipment	358,907
Installation of automatic and online analysers	143,791
Overhaul of the treatment line at Vale da Pedra	15,708
New building for the central laboratory - Projects	172,993
Infrastructure safety	8,954,395
Alviela aqueduct	8,233,914
Renewal of the Alcanhões/Alcoentre stretch	6,151,912
Renewal of siphons 35 e 36 (underway)	997,222
Maintenance and improvement of reservoirs	70,726
Other investments for infrastructure safety	649,755
Information technology and systems	948,917
Upgrade of telemanagement systems' ability to recover from an emergency situation	98,794
Upgrade of the data transfer capacity	200,795
Technological innovation	585,641
Appraisal of the distribution network's efficiency	161,424
Improvement of automatic telemanagement	151,800
Pilot model for powering automation equipments by solar energy	26,680

The company's two instruments for long-term planning - the *Master Plan for the Supply System* and the *General Plan for the Lisbon Distribution Network* - were revised and updated in 2006. With a 20-year time horizon, the plans consider the most likely development scenarios for the company's service area and set out the possible structural

models to satisfy supply needs. The scenarios have also taken into account the risks to EPAL's operations. The plans contain a capital budgeting policy oriented towards customer satisfaction, increased efficiency in production, transportation and distribution systems, and guaranteed quantity and quality of the water supplied.



Larus fuscus



CUSTOMER CARE

EPAL strives to learn about the degree of satisfaction and the aspirations of its clients, both retail and institutional, in order to take adequate steps towards improving service and meeting expectations.

Retail clients

Customer satisfaction

EPAL's Customer Satisfaction Index (CSI) is based on a poll of a representative sample of 1,300 clients about 14 features found to be relevant. For each feature the score depends on the importance attached by the client in a 1 to 5 scale and the degree of satisfaction experienced as measured by a 1 to 10 scale.

The scores obtained in the last four years are shown in the following table:



CSI 2006

Segment	2002	2003	2004	2006
Business	5.8	5.9	6.4	6.4
Residential	5.9	6.0	6.5	6.8
Complaints	5.9	5.8	7.0	6.8
Total	5,9*	6,0*	6,5*	6,7*

(* Global average weighted by the importance of each segment)





The absence of scores for 2005 is explained by the reappraisal in that year of the features considered to be most relevant. The study found that the drought in 2005 brought a higher degree of awareness of water as a valuable commodity, which led to more importance being attached to the management and maintenance of the supply network as well as the efficient use of water in parallel with concerns about its quality. In 2006, the poll found that the features obtaining the highest marks were consistency, pressure of supply and friendliness in contacts while price scored lowest. Features relating to water quality also scored high.

Action taken

On 15 March, Consumer Day, EPAL presented to its clients a refurbished store and made available in Braille

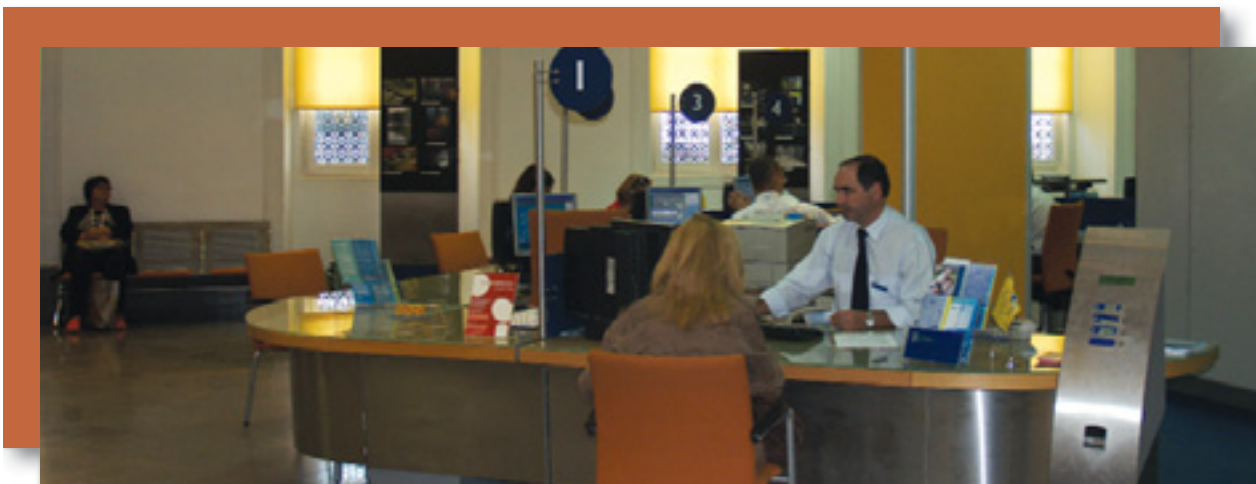
the *Water Bill*, the *Client's Handbook* and the *Useful Information* leaflet.

In April an electronic invoicing service was launched allowing the water bill to be sent by email. This service was enlarged in November with EPAL's participation in ViaCTT, an email functionality made available to the public by CTT, the national mail service.

Making use of new technologies, EPAL created in November an interactive stall at the head office store providing access to EPAL's website, where clients can explore all functionalities relating to their contractual relationship with the company, from contract signing, meter readings and invoicing to termination. Other available tools include the update of client data and the filing of complaints and suggestions.

In order to respond to clients' concerns about bills not reflecting actual consumption and to minimise the effects of consumption estimates, EPAL now offers 2-hour bookings for meter reading in cases where meters have not been read for more than 12 months and for home assistance.

In 2006, EPAL had 130,000 visits to its stores - where more than 80% of clients waited for less than 15 minutes before being served - and more than 280,000 contacts to its Contact Centre, with 78% of calls being answered in less than 30 seconds. These indicators represent an improvement in comparison with the year before and show significantly shorter waiting times.





Institutional (municipal and multi-municipal) clients

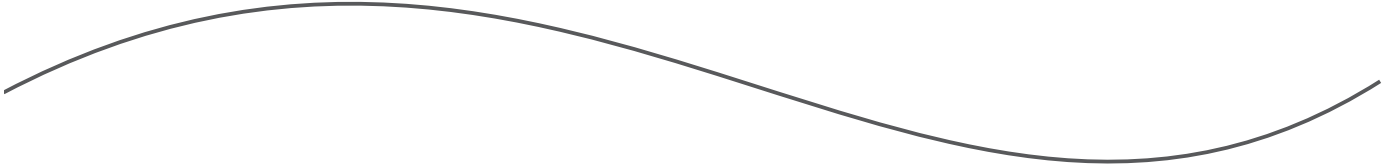
Regular contacts and meetings were held with this client category for the purpose of furthering cooperation and agreeing the best methods for solving pending matters and finding ways to satisfy clients' needs.

During the year, 13 complaints were filed by institutional clients, or a 19% reduction compared to those filed in 2005. All complaints were answered in less than eight working days.

The largest number of complaints related to discontinued supply, an area that has since been given particular importance in order to find solutions for minimising adverse consequences for clients.



Passer domesticus



LABOUR POLICY

In order to implement the guidelines set for the development and management of the company's human resources, a range of actions were undertaken such as the evaluation of the company's internal climate, a programme for integrated talent management and a project for identifying strategic management and leadership skills.

The first steps were taken towards an advanced management programme to provide people with adequate skills for the performance of their roles and also to give them the required competences for future, more qualified positions.

In 2006 a trainee programme was organised for the purpose of introducing 25 young people to professional life. The main objectives of this programme were the promotion of employment opportunities, the renewal of the staff base, the introduction of new know-how, values and competences and the attraction of both academic and technical talent.



Spending on training reached 182,898 euros - a 40.8% increase compared to 2005 - for 23,044 hours of internal and external actions attended by 458 employees. Major indicators of workplace safety developed favourably in the year as shown in the following graphs:

Indicators	2006
TF - Accident rate for total workplace accidents	18.21
Tf - Accident rate for workplace accidents resulting in sick leave	8.71
Tg - Degree of severity (first year only)	0.47 468 ¹
TG -Degree of severity (including repercussions from accidents in earlier years)	0.67 673 ¹

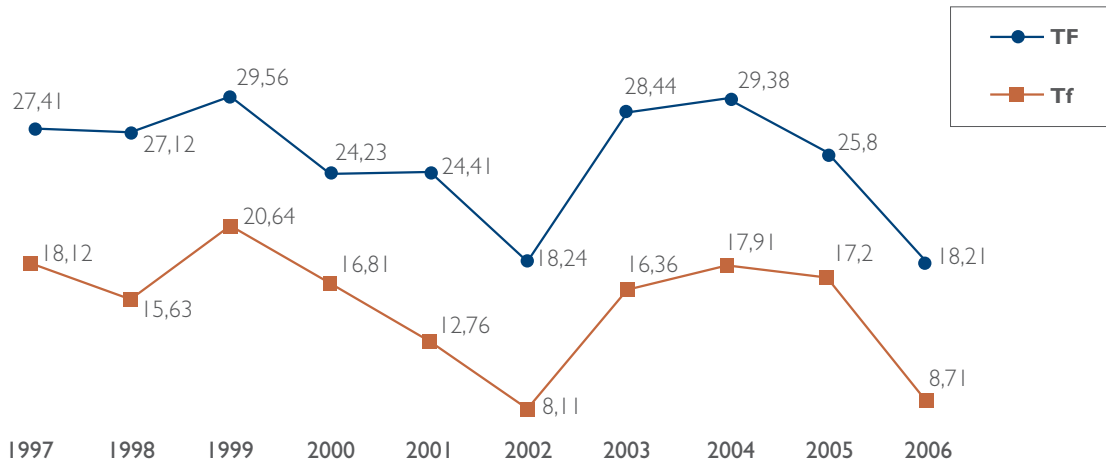
¹ Calculation made according to the International Labour Organisation (ILO)'s recommendation using the following expressions:

TG = Number of disability days (including those following accidents in earlier years) X 10⁶: hours of exposure to risk;

Tg = Number of disability days (only in the accident year) X 10⁶: hours of exposure to risk



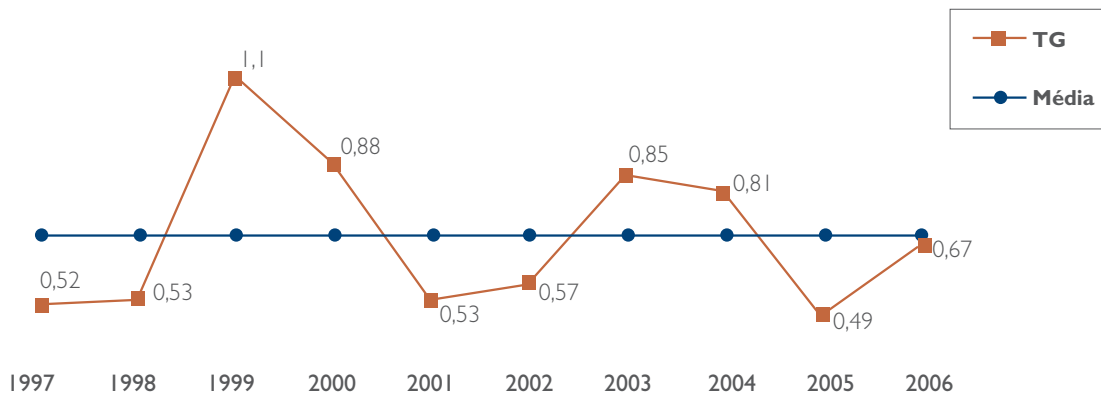
Accident rates in the last 10 years



TF = Total number of accidents $\times 10^6$: hours of exposure to risk

Tf = Number of accidents with absolute temporary disability $\times 10^6$: hours of exposure to risk

Degree of severity in the last 10 years



TG = Number of disability days (includes those for accidents in earlier years) $\times 10^3$: hours of exposure to risk



In terms of medical care provided, 1,387 medical examinations and 1,639 dental care sessions took place. In addition, flu vaccination campaigns and voluntary blood donations were carried out. Another important step was the preparation - with the help of international specialists - of a contingency plan to mitigate the effects of a possible bird flu pandemic.

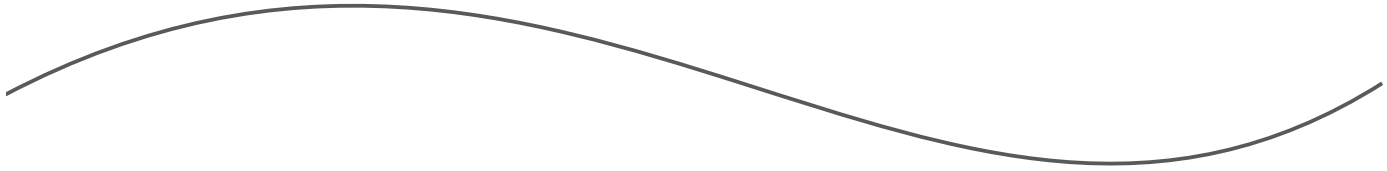
In terms of food-providing amenities, close to 90,000 lunches were served in six company canteens whose operating conditions were the subject of 243 technical inspections.

Following a traditional custom, a Christmas basket was given to the company's active, pre-retired and retired employees as well as to the employees of security and catering providers. As usual, a Christmas supper was served to all employees on duty on Christmas Eve.

In November 2006 the board of directors decided to terminate the Enterprise Agreement (*Acordo de Empresa*) signed with the unions by invoking the lack of legitimacy of its provisions against the general labour law. In this context, a proposal was presented for changing the present pension retirement plan towards a defined contribution model.



Falco tinnunculus



SUSTAINABILITY

In 2006, EPAL published its first sustainability report according to international guidelines in which the company's economic, social and environmental performance was described in detail.

The data disclosed in that document showed the predominantly favourable effects the company's operations have on society and its stakeholders' well-being. With the help of a large number of indicators, the company's action in several areas was amply documented.

The report's initial statement sums up the company's guiding principles for sustainable development:

- To achieve efficiency in water production, generating an adequate return on invested capital
- To minimise operations' footprint on the environment
- To follow fair labour policies that will foster efficiency
- To invest in new production technology
- To promote the efficient use of water

Although EPAL's second sustainability report is due for publication in the first half of 2007, a few achievements in 2006 can be listed here,

on the economic front:

- Share of net income distributed to the shareholder
- Protection of employees' purchasing power
- Sustained capital expenditure levels

on the social front:

- Funded level of retirement plan obligations
- Equal opportunity in recruitment and promotion of employees
- Access to computer equipment by the visually impaired

on the environmental front:

- Water loss in steady decline to 13.6% of total abstracted water
- Energy consumption in line with objectives in the five-year plan
- Lower production of waste and higher percentage of recycled products.

In 2006, EPAL's second environmental progress report was delivered, showing significant improvements compared to the first report in 2002. In this second edition aspects were covered that had either not been considered or





had been insufficiently covered in the first report; indicators were defined for a more rigorous annual evaluation of improvements in environmental performance with a view to generating, in the system's annual reviews, more relevant data for the design of annual environmental management programmes.

In the social area, an institutional campaign with a focus on closer client contacts was launched along three essential ideas - quality, modernism and social and environmental responsibility. The main activities in this context were the sponsoring of the Paralympics swimming team until the next Games in the People's Republic of China in 2008, the organisation of *Troféu*

EPAL, a regatta on the river Tagus with the participation of 31 boats, the launch of the *H2Oilha* project together with the *Fórum Estudante* involving a score of secondary schools and about 2,000 students in a number of actions designed to spread information about water and introduce participants to professions related to water supply activities, and the organisation of visits to the company's water museum facilities.

In 2006, EPAL's website was overhauled, allowing it to be used by the visually handicapped. At the same time, the website was uploaded with additional information and new services, namely EPAL Net and EPAL Net Professional. The new features also include a consumption simulator for checking and helping to change water consumption patterns.

The Water Museum welcomed 49,580 visitors and organised a programme of events on monumental and historical places including 20 exhibitions of painting, photography, painted tiles, sculpture and serigraphy, 3 art workshops and several guided tours. For the ninth year in a row, the *Águas Livres* pedagogical service was organised with the participation of 200,000 secondary-level students from 1,200 schools across the country.

Finally, considering the various building sites both in Lisbon and the municipalities crossed by the EPAL supply system's transport mains, an agreement was reached

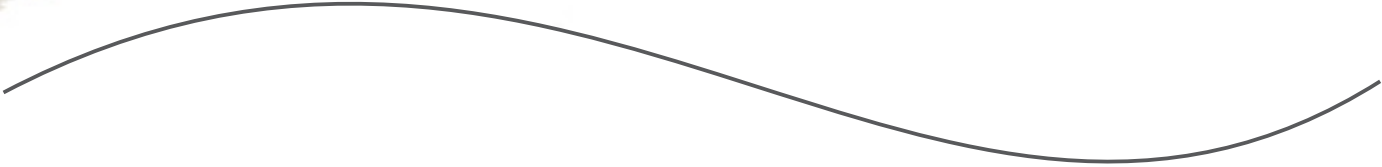




with the Portuguese Archaeological Society whereby procedures were laid down and the framework was set for archaeological work on building sites with a view to protecting archaeological finds. During the work for duplicating the Castelo do Bode transport main, ruins of a Roman villa built in the High Empire were found. Among the relevant archaeological remnants of the villa, which was still in existence in the late period of Roman rule in the Iberian Peninsula, an in situ polychrome tile fragment was found.



Dendrocopos major



OTHER ACTIVITIES

EPAL's quality systems and activities, achieved by its investment efforts, have prompted the company to offer a number of services to the market in order to enhance returns from its installed and available capacity.

In providing testing services to external entities, EPAL's Central Laboratory received 1,517 samples and conducted 13,032 trials of water quality, while the Meter Laboratory checked, fine-tuned and repaired meters for external parties.

In technology and information systems, EPAL focused its efforts on the following four areas: telecommunications, industrial automation and centralised supervision, innovative schemes for the distribution of drinking water and strategic and technological realignment of the customer relationship platform. Named AQUAmatrix®, this platform was fitted with a number of new functionalities designed to meet the company's internal needs and the requirements for integrated and effective commercial management. In this way, the basis was provided for the commercial use of AQUAmatrix® as an application service provider. In Torres Vedras, northwest of the capital, EPAL's bid won the public tender organised by the local municipality. Other bids were submitted to the

Águas de Santo André water company, in Alentejo, and the municipal company Praia Ambiente on Terceira island, on the Azores.

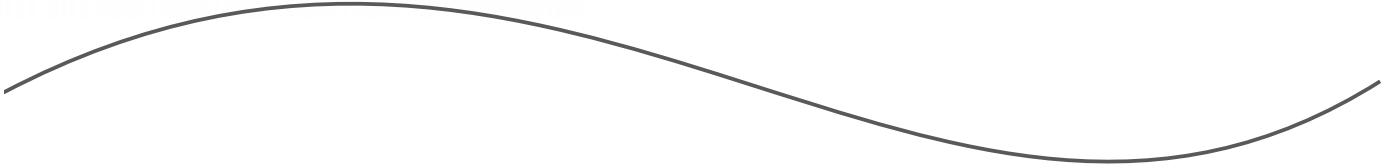
In consortium with COBA - Consultores de Engenharia and NEE - Nationale Eau Environnement, EPAL is developing a fact-finding and renewal study of the distribution systems for drinking water in the cities of Bejaia, Tizi-Ouzou and Chlef, a project it was awarded by the Algerian Ministry for Water Resources. Under this consortium, EPAL is responsible for the studies expected to lead to improved technical and commercial management of the cities' water distribution systems, currently run by Algérienne des Eaux.

In 2006, EPAL developed auditing activities in commercial matters, in particular the organisation of means and resources, customer relationships and supporting information systems. The company gathered sufficient data in the process for drafting a commercial reorganisation proposal.

Finally, following the government's Technological Plan guidelines for simplifying public administration, EPAL started to implement a pilot project for switching to electronic invoicing.



Certhia brachydactyla

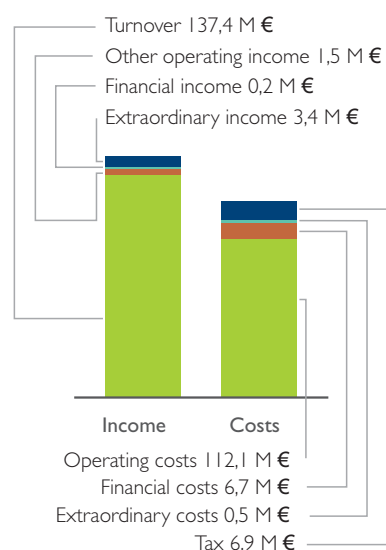


FINANCIAL PERFORMANCE

EPAL's financial performance in 2006 was strongly impacted by the 3% contraction in water consumption, the considerable financial effort with the company's pension plan and several other structural actions.

Following the trend in water sales, total revenues declined by 0.4% to 142.6 million euros.

Total costs amounted to 119.3 million euros, 8.6% up on the year before, primarily as a result of the costs incurred by the changes made to the pension plan and the strategic steps taken, as mentioned above.



Turnover

Turnover reached 137.4 million euros, the same as in 2005.

	2004	2005	2006	Change 06/05	
				Amount	%
Sales	136,464	134,034	134,424	390	0.3
Provision of services	3,092	3,351	2,936	(415)	(12.4)
Turnover	139,556	137,385	137,360	(25)	(0.0)

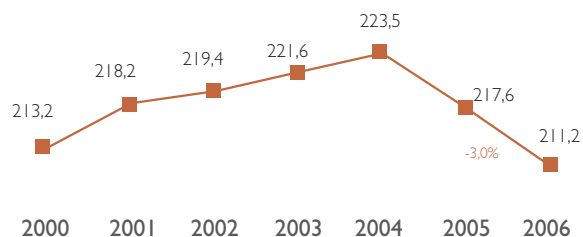
Water sales were stable compared to the year before which was due to lower consumption - 3% down on 2005 and 5.8% on 2004.

In anticipation of the extremely dry weather conditions forecast for 2005, several campaigns promoting the rational use of water were conducted that contributed decisively to lower consumption.

This downward trend in consumption is expected to be reversed in 2007 following the increase in the number of municipalities supplied by EPAL.

Services provided declined by 12.4%, primarily due to lower activity in residential piping repairs and supply planning, which together represent 57.5% of services.

Volume of water sold (Million m³)



Operating costs

Operating costs rose by 7.5%, an increase mainly explained by higher staff costs, current costs and provisions.

thousand euros

Costs	2004	2005	2006	Change 06/05	
				Amount	%
Cost of goods sold	2,774	3,108	2809	(294)	(9.5)
Current costs	34,514	34,715	37,621	2,906	8.4
Taxes	804	875	692	(183)	(20.9)
Staff costs	32,076	32,395	41,703	9,308	28.1
Other operating costs	14	23	23	0	0.0
Depreciation and adjustments	27,292	27,591	28,317	726	2.6
Provisions	8,252	5,598	969	(4,629)	(82.7)
Operating costs	105,726	104,300	112,134	7,834	7.5

Energy costs of 8.9 million euros, incurred primarily by water abstraction and transportation, weighed heavily in current costs with 23.5% of the total. Maintenance and repair expenditure, mainly on productive infrastructure, had a similar weight of 22.8% of the total and amounted to 8.6 million euros.

Emphasis should be placed on the strategic studies for improving the structure of the company and creating the basis for effective asset and cost management. Among these, the update of the Master Plan and the General Network Plan should be mentioned as well as the strategic overhaul and the policies for rationalising costs based on redesigning processes and routines.

Staff costs rose by 28.7% to 41.7 million euros including recognition in the year of 15.1 million euros pertaining to the company's post-employment benefit plan.

Following the joint guidance received from the Finance and Environment Ministries, EPAL is in the process of changing its pension plan from a defined benefit to a defined contribution model, under which the company takes on significant commitments in the transition stage.

Accordingly, the company made a significant financial effort, contributing 3.7 million euros to the pension fund and recognising 7.7 million euros in the year as transition costs.

Provisions were made for an amount of 0.97 million euros, less 4.6 million euros than in 2005. As provisions are made for non-random current or probable liabilities after careful and detailed risk evaluation, the company considers that the accumulated value of its provisions is adequate and sufficient.

Results

Operating results, which reflected the aforementioned circumstances, amounted to 26.8 million euros. Barring the recognition of transition costs for the pension plan and the cost of the strategic consultancy studies, operating results would have been in line with those for the preceding year.

Financial results deteriorated by 30.1% primarily as a result of higher funding costs. The cost of the long and medium-term debt to the European Investment Bank

thousand euros

Results	2004	2005	2006	Change 06/05	
				Amount	%
Net operating income	36,540	35,373	26,773	(8,600)	(24.3)
Net financial income	(4,926)	(4,979)	(6,477)	(1,498)	(30.1)
Net extraordinary income	5,051	2,901	2,969	68	2.3
Profit before tax	36,665	33,295	23,265	(10,030)	(30.1)
Income tax	10,641	9,507	6,935	(2,571)	(27.0)
Net profit for the year	26,024	23,788	16,329	(7,459)	(31.4)

(EIB) rose by 34.4% to 6.3 million euros after the increase in debt outstanding - with loan utilisations amounting to 33 million euros in the year - and the significant rise in interest rates.

EPAL's policy for managing interest rate risk consisted of (i) entering into funding agreements that will minimise the cost of debt by comparing the cost of fixed-rate instruments with the combined cost of floating-rate and hedging instruments and (ii) evenly balancing fixed rate with floating rate instruments.

Extraordinary results were broadly stable and included 2.7 million euros of income recognised in the year and relating to EU investment subsidies received in earlier years.

Income tax amounted to 6.9 million euros, which represented an average tax rate of 29.8%, the same as in previous years.

As a consequence of the aforementioned circumstances, in particular reduced demand, lesser absorption of fixed costs due to the lower level of activity and higher costs with EPAL's pension plan, the net result was 16.3 million euros, less 31.4 % than in the year before.

Financial position

In 2006, EPAL continued to implement its investment strategy for maintaining water quality standards while promoting the efficient use of the resource. Investment spending in the year amounted to 57.2 million euros and covered two important items: the upgrade of abstraction capacity at Castelo do Bode, the company's main source of water, and the planned replacement of the Lisbon network, a key factor in water loss reduction. In order to fund, among other things, capital expenditure of 57.4 million euros, the company borrowed

33 million euros to supplement operating cash flow of 51.3 million.

Abridged cash flow statement	2006
Operating cash flows	51,3
Investing cash flows	(57,4)
Outflows from financing activities	
<i>Dividend payments and bank debt service</i>	(29,5)
Inflows from financing activities	
<i>Drawings in the year</i>	33,0
Change in cash and cash equivalents	(2,6)

Following these expenditure and funding transactions, non-current assets rose by 4.6% and non-current liabilities, including long and medium-term debt and pension and pre-retirement obligations, increased by 11.4%.

Remark: The amounts relating to 2004 and 2005 are not directly comparable with those shown in the annual reports for the respective years, a fact emphasised by the mention "restated".

In the last five-year period, net debt increased by 64.7 million euros or close to 25% of capital expenditure in the period which amounted to 259 million euros. This fact highlights the large contribution of operating cash flow to funding capital expenditure at EPAL.

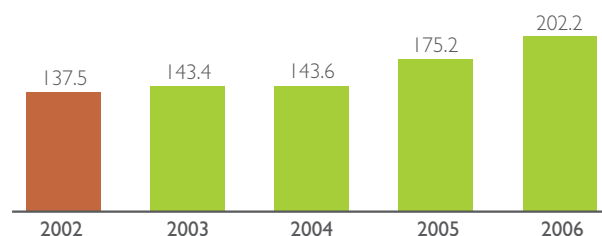
The rise in long-term (non-current) assets by 29.2 million euros combined with an increase in non-current liabilities by 31 million euros provides evidence of a maturity-matching funding policy and a favourable development compared to previous years in spite of a decrease in equity, which was, at 31 December 2006, considerably affected by the distribution of 2005 results in 2006.

thousand euros

Balance sheet	2004 (restated)	2005 (restated)	2006	Change 06/05	
				Amount	%
ASSETS					
Non-current assets	607,695	639,961	669,155	29,194	4.6
Current assets	67,674	47,825	46,030	(1,795)	(3.8)
TOTAL	675,369	687,786	715,185	27,399	4.0
SHAREHOLDERS' EQUITY AND LIABILITIES					
Equity	343,093	345,906	343,780	(2,126)	(0.6)
Non-current liabilities	239,333	272,192	303,168	30,976	11.4
Current liabilities	92,943	69,688	68,237	(1,451)	(2.1)
TOTAL	675,369	687,786	715,185	27,399	4.0

Medium and long-term debt

Million euros



Equity declined 0.6% to 343.8 million euros, compared to the year before, which highlights the level of retained earnings in 2005 - 5 million euros or 19% of net results for 2005.

Current assets declined by 3.8% or 1.8 million euros reflecting lower liquidity towards the end of the year resulting from the settlement of sizable obligations in the amount of 7 million euros including contributions to EPAL's pension fund, payments of income tax and the settlement of equipment suppliers' accounts.

EPAL kept its financial strength and ability to meet short, medium and long-term commitments according to the rating by Companhia Portuguesa de Rating.

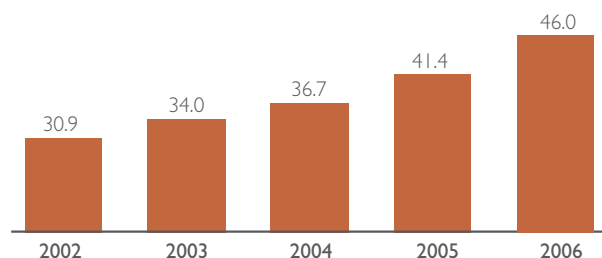
Rating category	Rating
Short-term rating	A-1 +
Medium- and long-term rating	A+

Pension fund

EPAL's pension fund reached 46 million euros at the end of 2006, an 11.1% increase on the year before and a 48.8% rise in the last five years. This increase was partly due to the good performance of the fund but, in particular, to the contributory effort made by the company - 13.2 million euros in the last five years of which 3.7 million in 2006 alone. The contributions impacted the funding of obligations according to the Portuguese Insurance Institute's Minimal Fund, which was slightly above 100% in 2005 and reached 107% in 2006.

EPAL's pension fund

Million euros



Equity holdings

EPAL has equity holdings in the following four companies.

Prolagos, SA (Brasil)	7.5%	R\$ 9.5 million
Clube de Golfe das Amoreiras	100.0%	€ 350,000
Shore, Lda.	7.5%	€ 31,500
Ambelis, SA	1.0%	€ 9,976

Prolagos, SA

EPAL's main equity holding is in the Brazilian company Prolagos of which it owns 7.5% for an amount of R\$ 9.5 million. The balance of Prolagos' share capital is held by Águas de Portugal, SGPS, either directly or indirectly through EBAL - Águas do Brasil, SA.

EPAL is the technical operator for the concession held by Prolagos for the supply of water and treatment of waste in the urban areas of the Cabo Frio, Búzios, São Pedro da Aldeia and Iguaba Grande municipalities and the supply of water to the Arraial do Cabo municipality.

In April 2006, Prolagos raised its share capital by R\$6.8 million and EPAL subscribed to its allotted share of R\$510,000. At year end, the equity holding in Prolagos was valued on EPAL's balance sheet at 5.0 million euros and was totally provided for.

Clube de Golfe das Amoreiras, SA

EPAL is the sole owner of Clube de Golfe das Amoreiras, SA, a company with share capital of 350,000 euros which was created for the development, construction and operation of a golf training ground on the land above the Amoreiras reservoir following a request by the Lisbon municipality for the area to be put to valuable use.

Recently, Supergolf - Amoreiras, the contracted developer, sought new arbitration after EPAL and Clube de Golfe challenged a previous arbitral decision whereby Supergolf was awarded the right to terminate the development contract.

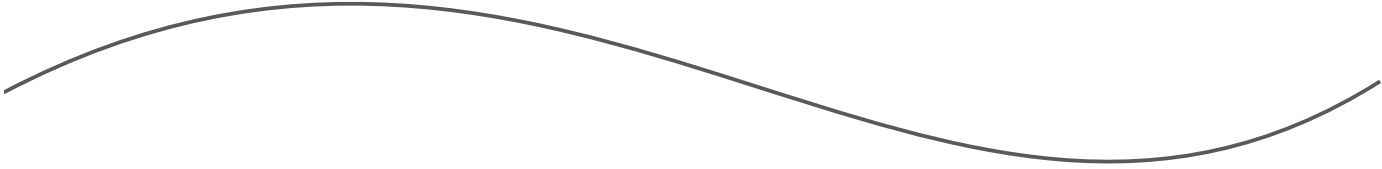
Transactions with related parties

The following table shows the transactions carried out between EPAL and other Águas de Portugal companies and the respective balances at 31 December 2006.

GROUP COMPANY	TRANSACTIONS			BALANCES	
	Revenue	Cost	Capex	Accounts receivable	Accounts payable
ÁGUAS DO CÁVADO	533.70	-	-	-	-
ÁGUAS DE PORTUGAL	405.57	2,279,932.82	-	30,892.43	(1,606,930.05)
ÁGUAS DO SADO	3,490.65	-	-	4,223.69	-
AQUASIS	387.25	71,350.00	12,553.76	-	(195,932.59)
ÁGUAS DO ALGARVE	87,854.73	-	-	53,133.04	-
ADP FORMAÇÃO	811.49	112,638.66	-	35,938.84	(133,322.23)
ADP SERVIÇOS	189,611.90	982,601.78	2,450.00	56,965.17	(348,186.80)
LUSÁGUA	239,856.42	-	-	44,989.63	-
SIMTEJO	241,224.63	-	-	41,810.00	-
ÁGUAS DO ZÊZERE E COA	48.72	-	-	58.95	-
ÁGUAS DO LENA	126,220.67	-	-	67,536.48	-
ADP INTERNACIONAL	34,873.60	-	-	-	-
EGF	-	5,209.83	-	-	-
ÁGUAS DO NORTE ALENTEJANO	18,820.73	-	-	4,104.57	-
ÁGUAS DO OESTE	4,860,401.05	-	-	1,519,468.21	-
ÁGUAS DO CENTRO ALENTEJANO	3,040.53	-	-	131.67	-
	5,807,581.64	3,451,733.09	15,003.76	1,859,252.68	(2,284,371.67)



Turdus philomelos



RISK MANAGEMENT

Financial risks

EPAL's operations are exposed to financial risks which are primarily related to liquidity and interest rates.

In terms of liquidity risk management, the company's policy is to keep reasonable cash balances while ensuring that occasional cash outflows from operating or investing activities are covered by short-, medium- and long-term borrowing arrangements.

For short-term borrowings, EPAL's policy is to secure access to credit lines for flexible use and for the required amount. To this end, the company agreed with two reputable banking institutions the availability of two credit lines for a total value of 12.5 million euros as well as a commercial paper programme for the same amount.

In order to fund capital expenditure, EPAL signed on 16 January 2002 an agreement with the European Investment Bank (EIB) whereby the bank extended the company a long-term loan facility for 185 million euros called EIB EPAL III. The purpose of this facility is to fund 50% of an ongoing investment programme for a total amount of 370 million euros. At year end, 100 million euros had been utilised under the facility.

Interest rate risk arises for EPAL from its floating-rate, long-term borrowings. The company's financial policy rests on (i) entering into the most competitive interest rate regime comparing fixed rates with the sum of floating rates and hedging instruments and (ii) a balanced fixed/floating-rate mix. At year end, indebtedness to EIB was 43.1% at fixed rate and 56.9% at floating rate.

Personal, property and third-party risks

The broad majority of the risks incurred by EPAL in its business activities have been transferred to insurers by means of personal, property and third-party insurance policies covering namely workplace hazards, personal and travelling accidents, road assistance, disease, business multi-risks including foregone income, automotive accidents and third-party liability for operations, pollution and products. EPAL's insurance contracts are valid for one year at a time, mature on each 30th June and may be renewed.

Environmental risks

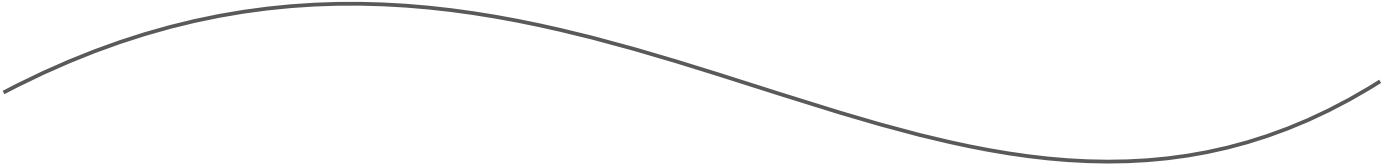
Environmental risks to EPAL derive primarily from downgraded water at abstraction points for reasons out of EPAL's control which may affect the satisfaction of consumer needs. Systematic monitoring and control of abstracted water provides knowledge about occasional events and downgrading trends which may lead to preventing action being taken if the relevant authorities are alerted in a timely fashion.

Environmental hazards following from the company's activities are primarily related to bursts of water mains, particularly large-diameter transport mains. Expenditure on the improvement and replacement of transport and distribution mains contributes to controlling risk as do maintenance and control activities and the implementation of monitoring and control zones and transport monitoring zones.

Supported by its complete and rigorous environmental mapping, EPAL knows the significance of any adverse environmental impacts that may arise from emergency situations in the company's business operations.



Carduelis carduelis



PROPOSED APPROPRIATION OF NET RESULTS

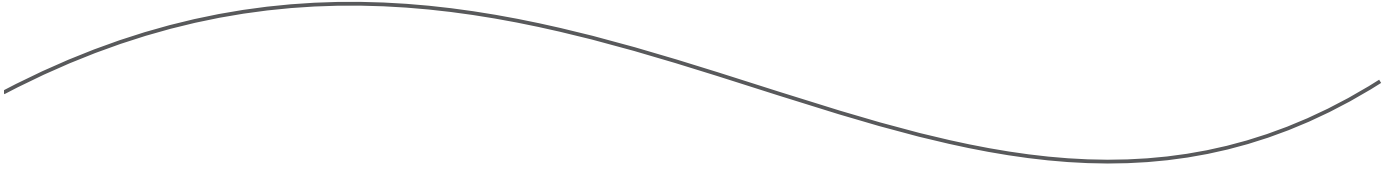
Pursuant to article 21 of the articles of association of EPAL - Empresa Portuguesa das Águas Livres, S.A, the Board of Directors proposes that the net result

of € 16,328,528.05 obtained in financial year 2006 should be appropriated as follows:

- € 1,632,852.81 to legal reserves;
- € 10,769,583.00 to shareholder dividends;
- € 941,221.00 to the employees' profit-sharing plan;
- € 2,984,871.24 to retained earnings.



Hirundo rustica



OUTLOOK

In 2007 some very important investments will be completed, namely the expansion of production capacity at the Asseiceira treatment station from 500,000 to 625,000 m³ per day with the introduction of flotation and intermediate ozonisation techniques in the treatment process.

The following works should also be mentioned: the increased supply capabilities for the Mafra municipality, the doubling of the third Castelo do Bode transport main which is 4.5 km long in the Santarém zone for the purpose of rebalancing the transport main's capacity upstream from Alcanhões, as well as some other new projects such as the pumping station at A-dos-Bispos.

On the Lisbon distribution network, planned investments aim to raise reliability while rationalising capital employed, namely by renewing small- and large-diameter piping and upgrading the pumping station at Olivais.

Starting in the second half of 2007, EPAL will supply nine additional municipalities through the Águas do Oeste multi-municipal company, thus reaching a total of 35 municipalities supplied.

One of the goals for 2007 is to raise to 75 the number of Monitoring and Control Zones (ZMCs) so as to cover 63% of the network and 54% of the clients. Simultaneously, a new software tool that has been developed in-house will be consolidated for controlling events on the ZMCs.

A plan for the extraordinary inspection of large transport mains has been launched and will be a reference for setting investment priorities. This action is part of the implementation of the Integrated Asset Management Model that will in the current year be one of the company's priorities. The model will give management the tools and the ability to make the right decisions on assets throughout their life cycle.

Development and implementation of a Quality Management System for the whole company will proceed.

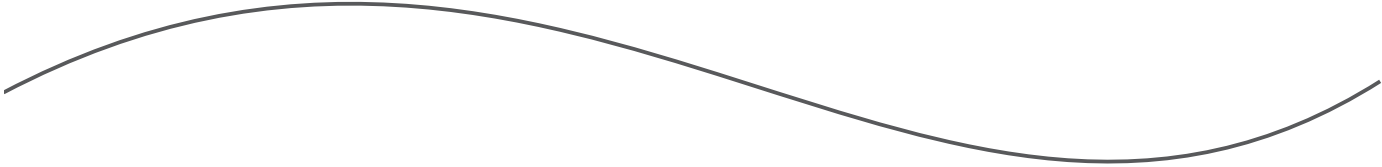
In 2007, the required final licence from the relevant authorities is expected to be obtained that will allow an international tender to be launched for the construction of EPAL's new central laboratory, planned to be the first step in a project leading to centralised functions at Olivais.

The Environment Ministry's launch on 28 December 2006 of PEAASAR II, a strategic plan for water supply and wastewater treatment, has presented new challenges to the company.

In line with the plan's thoughts, EPAL's sole shareholder Águas de Portugal set as a strategic goal for the company to manage, in an integrated way, the urban water cycle in its area of influence. Taking up this challenge will determine the company's continued development in raising client service and enhancing shareholder value.



Parus caeruleus



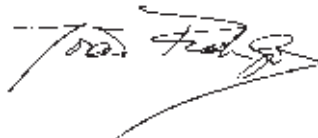
ACKNOWLEDGEMENTS

All those who contributed, directly or indirectly, to the company's progress and activities are hereby acknowledged with appreciation and respect.

- EPAL employees, for their efforts in achieving professional self-fulfilment at the company's service;
- The members of the company's governing bodies, namely the Sole Auditor and the Chartered Accountants, the members of the Environmental Impact Board and the members of the General Meeting Committee;
- Suppliers, contractors and service providers, for their committed response to a variety of challenges;
- Águas de Portugal, a diligent and available shareholder;

- Bankers and insurers, for their trust;
- The Environment and Finance ministries as well as other public bodies such as Instituto Regulador da Água e Resíduos, Direcção-Geral da Empresa, the Water Institute, the Coordination and Regional Development Board for Lisbon and the Tagus Valley and so many others;
- EPAL's clients, from municipal and multi-municipal to residential clients, from business clients to public bodies, for their wishes and expectations, for their trust and relationship with the company.

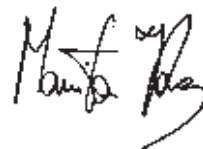
Lisbon, 15 March 2007




João Manuel Lopes Fidalgo
Chairman



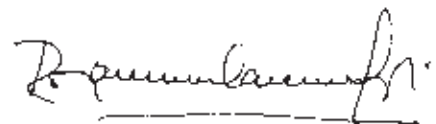
Jorge Luís Ferrão de Mascarenhas Loureiro
Director



José Alfredo Manita Vaz
Director



António Bento Franco
Director



Rui Manuel de Carvalho Godinho
Director



Columba livia

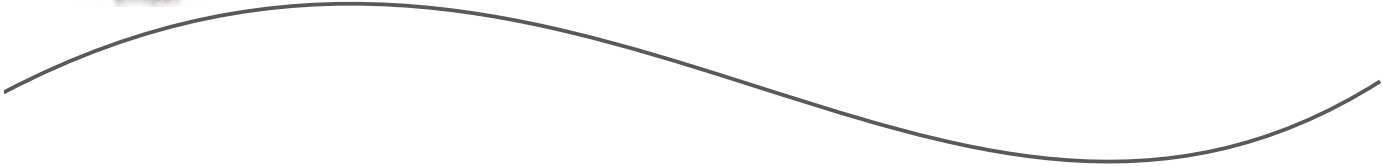




FINANCIAL STATEMENTS
AND NOTES



Picus viridis



Balance sheet

	Notes	2006	2005 (restated)
ASSETS			
Non-current assets			
Intangible fixed assets	5	21,300	21,300
Tangible fixed assets	6	656,749,968	629,164,940
Financial investments	7	369,148	384,173
Deferred tax	8	11,303,607	9,651,826
Clients and other accounts receivable	9	710,979	738,324
		669,155,001	639,960,563
Current assets			
Inventory	10	1,190,293	1,248,442
Clients	11	32,537,286	30,758,019
Public sector	12	5,601,240	6,077,056
Other debtors	13	3,170,141	3,610,087
Cash and cash equivalents	14	3,530,987	6,131,776
		46,029,947	47,825,379
Total assets		715,184,949	687,785,943
SHAREHOLDERS' EQUITY			
Share capital	15	150,000,000	150,000,000
Reserves and other adjustments	16	161,864,948	163,545,694
Retained earnings		15,586,586	8,572,938
Net profit for the year		16,328,528	23,787,526
Total equity		343,780,062	345,906,158
LIABILITIES			
Non-current liabilities			
Provisions	17	18,996,877	18,729,502
Pension obligations	18	25,775,964	18,484,000
Bank loans	19	202,189,795	175,208,185
Deferred tax	8	9,657,055	10,569,344
Investment grants	20	46,548,558	49,201,321
		303,168,249	272,192,351
Current liabilities			
Bank loans	19	6,018,390	5,396,700
Suppliers and other accounts payable	21	43,311,049	44,300,714
Public sector	22	1,205,398	3,442,715
Other creditors	23	17,701,800	16,547,305
		68,236,637	69,687,434
Total liabilities		371,404,886	341,879,785
Total liabilities and shareholders' equity		715,184,949	687,785,943

All amounts are stated in euros
The notes appended to the accounts are an integral part of the financial statements

The Financial Manager and Chief Accountant

Daniela Marina Alves Fernandes Valle Santos

Board of Directors

João Manuel Lopes Fidalgo, *Chairman*
Jorge Luís Ferrão de Mascarenhas Loureiro, *Director*
José Alfredo Manita Vaz, *Director*
António Bento Franco, *Director*
Rui Manuel de Carvalho Godinho, *Director*

Income statement (by nature)

	Notes	2006	2005 (restated)
Sales	24	137,359,980	137,385,292
Cost of sales	25	(2,808,741)	(3,102,836)
Gross margin		134,551,239	134,282,456
Current costs	26	(37,620,821)	(34,714,940)
Staff costs	27	(41,702,518)	(32,394,724)
Depreciation and adjustments for the period	28	(28,317,730)	(27,591,923)
Provisions for the period	29	(968,885)	(5,598,132)
Other operating costs	30	(715,239)	(897,428)
Own work		74,592	179,343
Supplementary income	31	1,390,356	1,981,573
Other operating income and gains	32	81,633	127,276
Net operating income		26,772,628	35,373,501
Financial expense	33	(6,710,712)	(5,199,755)
Financial income	34	233,810	220,264
Net current income		20,295,725	30,394,010
Net extraordinary income	35	2,969,337	2,901,422
Profit before tax		23,265,062	33,295,432
Company income tax	36	(6,936,534)	(9,507,906)
Net profit for the year		16,328,528	23,787,526
(Basic and diluted) earnings per share	15	0.54	0.79

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Income statement (by function)

	Notes	2006	2005
Sales	24	137,359,980	137,385,292
Cost of sales and provision of services		(35,201,821)	(34,537,913)
Gross results		102,158,160	102,847,379
Other operating income		2,518,624	2,731,774
Distribution costs		(31,334,385)	(29,225,097)
Administrative costs		(38,631,587)	(28,723,830)
Other operating cost and income		(4,800,479)	(9,184,735)
Operating results		29,910,333	38,445,491
Income from equity holdings			
Losses on associates	33	(15,025)	(26,835)
Results from equity holdings		(15,025)	(26,835)
Income from other investments			
Losses on other investments		(182,143)	(257,374)
Results from other investments		(182,143)	(257,374)
Net borrowing costs			
Financial losses		(6,497,850)	(4,901,079)
Net borrowing costs		(6,497,850)	(4,901,079)
Current results		23,215,315	33,260,203
Tax on current results		(6,886,787)	(9,472,676)
Net result for the year		16,328,528	23,787,526
Earnings per share		0.54	0.79

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Statement of changes in equity

Item	Share capital	Adjustment	Revaluation reserves	Legal reserves	Others reserves	Retained earnings	Net profit for the year	Total
1 January 2005	150,000,000	(4,064)	101,339,876	20,611,045	22,171,377	22,950,493	26,024,376	343,093,104
Appropriation of 2004 results	-	-	-	2,602,438	-	23,421,939	(26,024,376)	-
Dividend payment - employees	-	-	-	-	-	(1,456,190)	-	(1,456,190)
Dividend payment - shareholder	-	-	-	-	-	(19,518,282)	-	(19,518,282)
Adjustments (Note 16)	-	-	21,430,280	-	-	(21,430,280)	-	-
Realisation of revaluation reserves	-	-	(5,174,177)	-	-	5,174,177	-	-
Realisation of deferred tax on revaluations	-	-	568,919	-	-	(568,919)	-	-
Net profit for 2005	-	-	-	-	-	-	23,787,526	23,787,526
31 December 2005	150,000,000	(4,064)	118,164,897	23,213,483	22,171,377	8,572,938	23,787,526	345,906,158
Appropriation of 2005 results	-	-	-	2,378,753	-	21,408,774	(23,787,526)	-
Dividend payment - employees	-	-	-	-	-	(976,407)	-	(976,407)
Dividend payment - shareholder	-	-	-	-	-	(17,840,645)	-	(17,840,645)
Realisation of revaluation reserves (Note 16)	-	-	(4,968,456)	-	-	4,968,456	-	-
Realisation of deferred tax on revaluations (Note 16)	-	-	546,530	-	-	(546,530)	-	-
Change in the rate of deferred tax on revaluations (Notes 8 and 16)	-	-	362,428	-	-	-	-	362,428
Net profit for 2006	-	-	-	-	-	-	16,328,528	16,328,528
31 December 2006	150,000,000	(4,064)	114,105,399	25,592,236	22,171,377	15,586,586	16,328,528	343,780,062

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Cash flow statement

	Notes	2006	2005
Operating activities			
Receipts from clients		161,781,981	163,113,268
Payments to suppliers		(39,304,732)	(35,612,177)
Payments to the staff		(35,163,499)	(34,672,065)
Cash flow generated from operations		87,313,751	92,829,027
Payment/receipt of company income tax		(11,361,617)	(10,578,127)
Other receipts/payments from/for operating activities		(24,233,500)	(24,275,952)
Cash flow generated before extraordinary items		(35,595,117)	(34,854,079)
Receipts on account of extraordinary items		43,807	168,468
Payments on account of extraordinary items		(466,342)	(355,558)
		(422,535)	(187,090)
Net cash from operating activities (1)		51,296,099	57,787,858
Investing activities			
Receipts from:			
Financial investments		-	6,067
Tangible fixed assets		27,213	30,870
Interest and other similar income		233,717	220,219
		260,930	257,155
Payments on account of:			
Financial investments		(192,143)	(272,374)
Tangible fixed assets		(57,463,990)	(59,027,019)
		(57,656,133)	(59,299,393)
Net cash used in investing activities (2)		(57,395,203)	(59,042,239)
Financing activities			
Receipts from:			
Proceeds from borrowings		33,000,000	103,000,000
		33,000,000	103,000,000
Payments on account of:			
Repayment of borrowings		(5,396,700)	(95,775,010)
Interest and other similar expense		(6,264,341)	(4,945,618)
Dividends		(17,840,645)	(19,518,282)
		(29,501,685)	(120,238,910)
Net cash generated/(used) in financing activities (3)		3,498,315	(17,238,910)
Net decrease in cash and cash equivalents (4)=(1)+(2)+(3)		(2,600,789)	(18,493,291)
Cash and cash equivalents at the start of the year	14	6,131,776	24,625,067
Cash and cash equivalents at the end of the year	14	3,530,987	6,131,776
Change in cash and cash equivalents		(2,600,789)	(18,493,291)

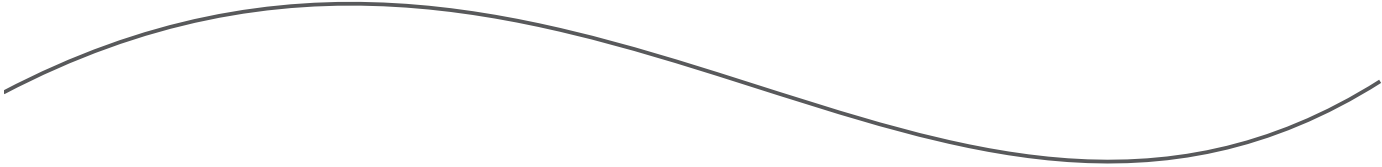
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Toutinegra-de-barrete - *Sylvia atricapilla*



NOTES TO THE FINANCIAL STATEMENTS

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Notes to the financial statements

I. EPAL's business operations

I.1 Introduction

EPAL is a limited liability company whose shares are entirely owned by public bodies and its full name is EPAL - Empresa Portuguesa das Águas Livres, S.A. ("EPAL" or the "Company").

The object of the company is to abstract, treat, transport and distribute water for public consumption as well as to undertake any complementary or related industrial, commercial or research activities or provision of services, namely those related to the water cycle.

I.2 Business operations

EPAL abstracts, transports, treats and distributes water for human consumption and aims to provide a quality service respecting essential social and environmental concerns. Its supply services cover retail distribution in the city of Lisbon and the bulk delivery of water to 23 municipalities in the Greater Lisbon area.

EPAL's water pricing regime is regulated by a government decree (Decreto-Lei nº 230/91 of 21 June 1991) that provides for an agreement to be reached between EPAL and the Portuguese state as represented by the Ministry of Economy's Direcção Geral da Empresa.

I.3 Approval of the financial statements

The reported financial statements have been approved in a meeting of the board of directors on 15 March 2007. The board's opinion is that they reflect in a reliable way EPAL's operations, financial position and performance and cash flows.

2. Accounting policies and valuation criteria

a) Bases of presentation

EPAL's financial statements for 2006 consisting of the balance sheet, income statement - by nature and by function - cash flow statement, statement of changes in equity and respective notes, have been prepared on a going concern assumption, on the basis of the company's books and accounting records, kept in accordance with accounting principles that are generally accepted in Portugal except for a waiver on Accounting Guideline nº 19 following the company's adoption in previous years of the "corridor" method as set out in IAS 19 for recording the obligations arising from its post-employment benefit plan (Note 2).

The company's balance sheet at 31 December 2006 and the income statement by nature for the financial year ended on that date are presented in a format that is different from the one provided in the official accounting plan (Plano Oficial de Contabilidade), with the notes presented in sequential order for the balance sheet and the income statement. Despite this difference, the accounts and notes contain, together with the statement of changes in equity, the information required by the Plano Oficial de Contabilidade; likewise, the total asset and equity amounts at 31 December 2006 and the net result for the year ended on that date are equal to those resulting from the presentation of the balance sheet and the income statement by nature according to the format required by the Plano Oficial de Contabilidade. These are also attached in the section "Documents required by the Plano Oficial de Contabilidade".

Considering this change in the presentation of the balance sheet at 31 December 2006 and the income statement by nature for the year ended on that date, the balance sheet at 31 December 2005 and the income statement by nature for the year ended on that date were restated for comparative purposes according to the format differing from the one provided by the aforementioned Plano Oficial de Contabilidade. As a result, the total asset and equity amounts at 31 December 2005 and the net result for the year ended on that date were found to be equal to those contained in the balance sheet and income statement by nature approved by the AGM of 20 March 2006.

The preparation of financial statements in accordance with accounting principles generally accepted in Portugal requires the use of estimates, assumptions and judgement in the application of policies to be adopted by EPAL as these affect the amounts reported as assets or liabilities as well as revenue and cost items for the reporting period.

Although these estimates are based on management experience and best estimates relating to current and future events and actions, present and future outcomes may, in the final analysis, differ from those estimates. The areas involving a higher degree of judgement or complexity and those where assumptions or estimates are significant for the financial statements are presented in Note 4.

Unless otherwise indicated, all amounts are stated in euros.

b) Intangible fixed assets

The amount entered under this heading relates to a right to part of third-party land that is crossed by EPAL's transport mains. Because it is an unlimited usage right, it is not depreciated in the accounts.

c) Tangible fixed assets

Tangible fixed assets are recorded at acquisition cost or at revaluation according to legal provisions. Depreciation charges are calculated using the straight-line method and the estimated economic life of the asset (Notes 6 and 16).

Depreciation rates used are generally equal to the maximum rates that are accepted for tax purposes and are the following:

Items	Depreciation range
Buildings and other constructions	2% - 10%
Production equipment	2% - 25%
Transportation equipment	6.2% - 25%
Tools	10% - 25%
Office equipment	10% - 25%
Containers	14.28%
Other tangible fixed assets	6.66% - 12.5%

Transport mains, which are entered under Production equipment (Equipamento Básico) or assets used for the company's main activities, are depreciated at the rate of 2% as their economic life is estimated to be 50 years. The use of this rate has been authorised for tax purposes by the relevant authorities.

Expenses incurred for current maintenance are charged to the year's results.

Tangible fixed assets that have not been fully depreciated are charged to the year's results if no future economic benefits are expected from either their use or disposal. Whenever an asset's book value is greater than its recoverable value, the value is brought down to the asset's estimated recoverable value.

Gains or losses arising from write-offs or disposals are determined by the difference between the proceeds from the disposal and the asset's book value and are recognised on the income statement as income or expense. When goods that

have been revalued are sold, the amount entered in the revaluation reserve account (Reserva de Reavaliações) is transferred to the retained earnings account (Resultados Transitados).

d) Impairment of fixed assets

Assets under depreciation are tested for impairment whenever any events or changes in circumstances suggest that the amount at which they are carried on the financial statements may not be recoverable.

An impairment loss is recognised for the excess of the carrying amount of an asset over its recoverable amount. The recoverable amount is the higher of an asset's fair value less selling costs and its value in use. If it is not possible to determine the recoverable amount for a particular asset, it should be aggregated with other assets for the joint generation of independent cash flows and, thus, the set-up of a cash-generating unit (CGU).

An impairment loss is recognised through income statement in the year the circumstances arise for its record. Annually, it is added or reversed, in total or in part, whenever the circumstances having given rise to its initial record shall change or cease to exist.

e) Financial assets

Group companies and associates

Investments in equity holdings in group companies or associates are recorded at cost and valued according to the equity method. According to this method, gains and losses obtained by these companies are recorded, for the proportional stake held, as financial results.

Other investments

Other financial investments in securities or other placements are valued at cost after deduction of any adjustments for estimated losses on their disposal.

f) Accounts receivable

Third-party debts are recognised at nominal value except when their receipt has been deferred beyond one year, in which case they are recognised for the present value of their future cash flows.

Adjustments to doubtful debts are calculated on the basis of a specific economic evaluation of the total or partial losses that are estimated from the failure to collect receivables from clients or other debtors after considering the existence of collateral or any other form of security (Note 11).

g) Inventory

Inventory for EPAL's productive process includes primarily (i) reagents such as liquid chlorine, aluminium sulphate, carbon dioxide and other products used for water treatment and (ii) hydraulic equipment for civil construction.

Inventories are valued at the lower of acquisition cost (including all expenses until inventories are stored) and net realisable value (NRV). NRV is determined as the estimated selling price in the company's normal course of business, after deduction of any variable selling expenses. When NRV is lower than the carrying amount, a write-down is made for the difference.

Inventories sold are valued at average cost.

h) Liquidity

Liquidity includes cash and cash equivalents, bank deposits, other highly liquid, short-term investments maturing in up to one year and overdraft facilities. Overdraft facilities are presented on the balance sheet under current liabilities, "Debts to credit institutions - Short term", and are also considered in the preparation of the cash flow statement.

Marketable securities are valued at the lower of acquisition cost and market value.

i) Share capital

Ordinary shares are classed under shareholders' equity.

j) Employee benefits - Pensions

A defined benefit plan is a pension plan that defines the benefit amount in respect of the complement to the pension the employee will receive at retirement, usually depending on one or more factors such as age, length of service and remuneration.

The company has in force a system of social benefits for its employees (defined benefits) involving the payment of complements to retirement pensions (for long service or disability) while additionally sustaining the obligations arising from early retirement.

The obligations arising from the benefit plan in force are calculated annually by independent actuaries using the Projected Unit Credit Method. The present value of obligations is determined by discounting future benefit payments using the yield on high-quality corporate bonds denominated in the currency in which the benefits will be paid, with a term to maturity close to the term of the actual obligations.

The costs incurred by these obligations are recognised in accordance with IAS 19 (Note 18).

k) Provisions

Provisions are only recognised when there is a present obligation resulting from past events for whose settlement an outflow of internal resources is probable and whose amount can be estimated reliably. Whenever one of these criteria is not met or the obligation's existence is subject to the occurrence (or non-occurrence) of a future event, EPAL will disclose such fact as a contingent liability, except when the possibility of an outflow of resources for settlement of the obligation is considered to be remote.

When there are a large number of similar obligations, the probability for an outflow of internal resources to occur is determined in combination. The provision is recognised even though the probability of outflow of internal resources in respect of a particular item in the class may be reduced.

Provisions are not recognised for future operating losses.

l) Investment grants

Investment grants are recognised when there is reasonable assurance that the grant will be received and EPAL will comply with the conditions attached to its receipt.

Investment grants for the acquisition of tangible fixed assets are recorded as non-current liabilities and are credited to the income statement using the straight-line method for the expected remaining life of the related assets.

Other grants are deferred and recognised in the income statement in the same period as the expenses they are designed to offset.

m) Suppliers and other accounts payable

Suppliers and other accounts payable are carried at nominal value to the extent they are payable in the short term.

n) Deferred tax

Deferred taxes are recognised using the balance sheet liability method whereby such temporary differences are considered that arise from the difference between the tax base of assets and liabilities and their carrying amounts.

Deferred taxes are not recognised that arise from the initial recognition of an asset or liability other than in a business combination which, at the time of the transaction, does not affect either the accounting or the taxable profit.

Deferred taxes arising from temporary differences following from the application of the equity method are recognised only when it is probable that the reversal will occur in the foreseeable future.

Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised or when the reversal of a deferred tax asset is expected for the same time and the same authority.

Deferred taxes are measured at the tax rates that have been enacted or substantively enacted by the balance sheet date and that are expected to apply when the deferred tax is reversed. The differences that may arise from expected changes in the rates at which the temporary taxable differences will be reversed are considered in the income statement.

The annual entries in deferred tax assets or liabilities are made against the same accounts where the transactions or events that originated them have been recorded. The revaluation reserve amount in shareholders' equity is carried net of the related deferred tax liability (Note 16).

Deferred tax assets and liabilities are not offset against each other.

o) Recognition of revenue and other income and expense

Revenue consists of the fair value of the sale of goods and provision of services, net of taxes and discounts, and is recognised as follows:

Water sales and service fee

The sale of water and service fee is supported by contracts signed with the clients whereby the price is clearly defined by means of a duly approved price grid.

During the year, revenue arising from the sale of water is recognised on the basis of metered consumption or, when consumption has not been metered, estimated consumption. At the end of the year, according to the matching principle, accrued income is recognised for the consumption estimated but not metered or invoiced. At the end of each financial year, the amount recorded as water sales relates to actual consumption in the year as measured by the quantities metered and, in the cases this is not feasible, reliable consumption estimates (Note 11).

Interest expense

Interest payable on obtained loans is recognised as a cost for the year in which interest payments fall due, even when the purpose of the loans is to fund the acquisition of fixed assets (Note 23).

Other income and expense

Other income and expense is recorded in the year when it has been generated or incurred, regardless of the moment for its receipt or payment, in accordance with the matching principle. The differences between received or paid amounts and the related income or expense are recorded as accruals or deferrals.

p) Dividend payable

Dividend payable is recognised in the year when the payment has been approved by the shareholder meeting.

q) Revaluation reserves

The amounts entered in the "Revaluation reserves" account are initially recorded for the net asset increase resulting from revaluations performed in accordance with the law (Note 6) and annually transferred to the "Retained earnings" account as the assets are realised through sale, write-off or amortisation.

3. Policies for managing financial risk

Financial risk factors

EPAL's operations are exposed to a variety of financial risk factors: liquidity risk and cash flow risk linked to interest rates.

Liquidity risk

Management of liquidity risk requires readily available funds to be kept at a reasonable level, the consolidated fluctuating debt to be supported by an adequate amount of credit facilities and market positions to be closed selectively. EPAL aims to ensure flexibility of the fluctuating debt and to maintain, to that end, available credit lines. EPAL manages liquidity risk by securing from financial institutions committed credit lines and funding facilities that provide immediate access to funds under flexible terms.

Cash flow risk and fair value risk linked to interest rates

As EPAL does not earn significant income on its assets, profit and operating cash flows are substantively independent from changes in market interest rates.

EPAL's interest rate risk arises primarily from its long-term borrowings. In this context, loans obtained at floating interest rates expose EPAL to cash flow risk while loans obtained at fixed interest rates expose EPAL to fair value risk linked to interest rates. EPAL's policy is to keep a balance between fixed-rate and floating-rate loans.

4. Estimates and judgements

Estimates and judgements with an impact on EPAL's financial statements are continually evaluated and represent, at each reporting date, management's best estimate considering historic performance, accumulated experience and expectations about future events which, under the circumstances, are believed to be reasonable.

The very nature of estimates may lead to actual outcomes that may differ, for financial reporting purposes, from the estimated amounts.

The estimates and judgements presenting a significant risk of material adjustments to the carrying amount of assets and liabilities in the ensuing financial year are the following:

Provisions

EPAL reviews periodically obligations arising from past events that should be the subject of recognition or disclosure.

The subjectivity that is inherent to determining the probability and amount of the outflow of internal resources required for the settlement of obligations may lead to significant adjustments either because the assumptions have changed or because previously disclosed contingent liabilities will be recognised in the future as provisions.

Impairment of assets

At the date for presentation of EPAL's financial statements for the year ended on 31 December 2006, the existence of any situation of impairment of reported assets is not considered as probable.

5. Intangible fixed assets

Intangible fixed assets of 21,300 euros are exclusively related to a right to third-party owned land that is crossed by EPAL's transport mains. As it is an unlimited usage right, it is not depreciated.

In 2006 no new entries were made to either intangible fixed assets or their depreciation.

6. Tangible fixed assets

Tangible fixed assets net of depreciation have the following composition:

	2006	2005
Land and natural resources	49,247,566	49,247,566
Buildings and other constructions	27,337,027	29,664,938
Production equipment	500,763,655	479,982,956
Transportation equipment	5,911	14,352
Tools	1,348,860	1,861,943
Office equipment	1,303,798	940,214
Containers	1,095	1,440
Other tangible fixed assets	2,489,221	2,944,047
Fixed assets in progress	74,252,834	62,801,147
Advances on account of tangible fixed assets	-	1,706,336
	656,749,968	629,164,940

At the end of 2006, the "Production equipment" account included assets in third parties' possession, namely water meters in the distribution network for an amount of 10,447,705 euros.

Entries in tangible fixed assets and their accumulated depreciation in 2006 are shown below:

Item	2005	Increase	Transfer.	Write-offs and disposals	2006
Gross fixed assets					
Land and natural resources	49,247,566	-	-	-	49,247,566
Buildings and other constructions	97,495,050	2,165	562,212	-	98,059,427
Production equipment	831,070,940	752,124	43,198,467	(106,701)	874,914,831
Transportation equipment	1,935,912	-	-	(280,163)	1,655,748
Tools	10,043,221	97,703	(1,598)	(54,672)	10,084,654
Office equipment	16,652,936	220,410	692,501	(1,705,748)	15,860,099
Containers	8,134	-	-	-	8,134
Other tangible fixed assets	10,144,726	21,266	196,809	(1,467)	10,361,334
Fixed assets in progress	62,801,147	54,393,742	(42,942,055)	-	74,252,834
Advances for tangible fixed assets	1,706,336	-	(1,706,336)	-	-
	1,081,105,969	55,487,411	-	(2,148,752)	1,134,444,628
Accumulated depreciation					
Buildings and other constructions	67,830,112	2,892,288	-	-	70,722,400
Production equipment	351,087,984	23,169,892	-	(106,701)	374,151,176
Transportation equipment	1,921,560	8,441	-	(280,163)	1,649,837
Tools	8,181,278	605,812	-	(51,296)	8,735,794
Office equipment	15,712,723	549,327	-	(1,705,748)	14,556,301
Containers	6,694	346	-	-	7,040
Other tangible fixed assets	7,200,679	672,901	-	(1,467)	7,872,113
	451,941,029	27,899,007	-	(2,145,375)	477,694,661
		(Note 28)			

New investments in tangible fixed assets in the year amounted to 57.2 million euros consisting of the "Increases" column total (55.5 million euros) and the 1.7 million euros resulting from the conversion into new investment of the amounts paid in advance for tangible fixed assets in the preceding year. The most significant investments in 2006 were the network's renewal and the works for expansion of the Castelo do Bode system.

The "Production equipment" account includes primarily the distribution network, transport mains, reservoirs, water and electricity facilities, hydraulic works and meters.

The works related to the expansion of the Castelo do Bode system represent the bulk of the amount under "Fixed assets in progress".

Revaluations

Tangible fixed assets have been revalued in previous years pursuant to the following pieces of legislation:

- Decreto-Lei n.º 430/78, as amended by Decreto-Lei n.º 24/82 of 30 January 1982
- Decreto-Lei n.º 219/82 of 2 June 1982
- Decreto-Lei n.º 399-G/84 of 28 December 1984
- Decreto-Lei n.º 118-B/86 of 27 May 1986
- Decreto-Lei n.º 111/88 of 2 April 1988
- Decreto-Lei n.º 49/91 of 25 January 1991
- Decreto-Lei n.º 264/92 of 24 November 1992
- Decreto-Lei n.º 31/98 of 11 February 1998

Historic acquisition costs for tangible fixed assets and related revaluations at 31 December 2006 net of accumulated depreciation are detailed below:

	Historic Costs a)	Revaluations a) b) (Note 16)	Revalued amounts a)
Tangible fixed assets			
Land and natural resources	12,575,508	33,102,726	45,678,234
Buildings and other constructions	8,125,151	5,120,391	13,245,542
Production equipment	112,631,543	85,485,678	198,117,221
Other tangible fixed assets	5,255	949	6,204
	133,337,457	123,709,743	257,047,200

a) Net of depreciation

b) Include past revaluations

7. Financial investments

Financial investments at 31 December 2006 and 2005 were as follows:

	2006	2005
Equity holdings in group companies	250,000	265,025
Equity holdings in other investees	5,013,150	4,831,007
Securities and other financial investments	109,172	109,172
Adjustments to financial investments	(5,003,174)	(4,821,031)
	369,148	384,173

Group companies

Equity holdings in group companies that were accounted for according to the equity method, as well as related equity and results, were the following at 31 December 2006:

Company	Head office	% Equity holding	Equity	Net Profit	Carrying amount	Adjustments	Net amount
Clube de Golfe das Amoreiras	Lisbon	100%	238,171	(26,854)	250,000	-	250,000

a) represents supplementary capital

At 31 December 2006, Clube de Golfe das Amoreiras presented negative equity of 11,829 euros excluding supplementary capital. Under applicable accounting rules, EPAL ceased to use the equity method when accumulated losses by the associate exceeded the financial investment on the balance sheet. Accordingly, the company recognised as cost for the year only the portion of the year's loss incurred by the associate up to that limit. The cost of 15,025 euros is reflected on the "Losses with associates" account (Note 33).

EPAL is the sole owner of Clube de Golfe das Amoreiras, SA, a company with share capital of 350,000 euros which was created for the development, construction and operation of a golf training ground on the land above the Amoreiras reservoir following a request by the Lisbon municipality for the area to be put to valuable use.

Recently, Supergolf - Amoreiras, the contracted developer, sought new arbitration after EPAL and Clube de Golfe challenged a previous arbitral decision whereby Supergolf was awarded the right to terminate the development contract.

Investee companies

Financial investments in other companies at 31 December 2006 and 2005 were as follows:

Company	Head office	% Equity holding	Equity	Net Profit	Carrying amount	Adjustments	Net amount
Prolagos	Rio de Janeiro	7.5%	18,238,887	(3,292,608)	4,971,674	4,971,674	-
Shore	Madeira	7.5%			31,500	31,500	-
Ambelis	Lisboa	1%			9,976	-	9,976
					5,013,150	5,003,174	9,976

b) amounts relate to 31 December 2005

EPAL's main equity holding is in the Brazilian company Prolagos of which it owns 7.5% for an amount of CR\$9.5 million. The balance of Prolagos' share capital is held by Águas de Portugal, SGPS directly or indirectly through EBAL - Águas do Brasil, SA.

EPAL is the technical operator for the concession held by Prolagos for the supply of water and treatment of waste in the urban areas of the Cabo Frio, Búzios, São Pedro da Aldeia and Iguaba Grande municipalities and the supply of water to the Arraial do Cabo municipality.

Securities and other financial investments

At 31 December 2006 and 2005 the company held the following securities:

	2006	2005
Amounts available to a court of law	89,415	89,415
Portuguese government bonds	18,428	18,428
Other securities issued by the Portuguese state	1,328	1,328
	109,172	109,172

Changes in the year

Changes in financial investments and related adjustments were as follows:

	2005	Increases	Reductions	2006
Equity holdings in group companies (Note 33)	265,025	-	(15,025)	250,000
Equity holdings in other investees	4,831,007	182,143	-	5,013,150
Securities and other financial investments	109,172	-	-	109,172
Adjustments to financial investments (Note 33)	(4,821,031)	(182,143)	-	(5,003,174)
	384,173	-	(15,025)	369,148

The increase in "Equity holdings in other investee companies" was related to EPAL's subscription and payment for new shares in Prolagos, an investment that was entirely adjusted in the year.

The reduction in "Equity holdings in group companies" resulted from application of the equity method.

8. Deferred tax

For the measurement of the final balances of deferred tax, the rate contained in the state budget for 2007 was used. This is a state income tax of 25% to which a local tax at the rate of 1.5% on taxable profit is added, resulting in an aggregate tax rate of 26.5%. Changes in deferred tax in 2006 were the following:

Item	2005	Increase	Reversal	Change in tax rate	2006
Provisions above tax limits	33,046,670	11,870,544	(4,228,956)	-	40,688,258
Reversal of taxed income	2,050,879	-	(84,018)	-	1,966,861
Tax base	35,097,549	11,870,544	(4,312,974)	-	42,655,119
Tax rate:					
State income tax (25%)	8,774,387	2,967,636	(1,078,243)	-	10,663,780
Local income tax (a)	877,439	296,764	(107,824)	(426,551)	639,827
Deferred tax assets	9,651,826	3,264,400	(1,186,068)	(426,551)	11,303,607
Revaluation of fixed assets	38,230,190	-	(1,987,383)	-	36,242,807
Amount net of reinvested capital gains	203,788	-	(4,877)	-	198,912
Tax base	38,433,978	-	(1,992,259)	-	36,441,719
Tax rate:					
State income tax (25%)	9,608,494	-	(498,065)	-	9,110,430
Local income tax (a)	960,849	-	(49,806)	(364,417)	546,626
Deferred tax liabilities	10,569,344	-	(547,871)	(364,417)	9,657,055

(a) The impact on deferred tax of the change in the method for calculating local tax was directly recognised in the income statement, except for the effect on unrealised revaluation reserves whose impact was recognised as a direct change in "Revaluation reserves" (Note 16). The change in the method for calculating local tax resulted in the following entries:

Tax for the year	(424,562)	(Note 36)
Revaluation reserves	362,428	(Note 16)
Net impact	(62,134)	

9. Clients and other accounts receivable - non-current

The balances of this account at 31 December 2006 and 2005, for 710,979 and 738,324 euros, respectively, relate entirely to "Other debtors", namely a debt receivable and timely serviced in accordance with an annual instalment schedule with final maturity in 27 years. The debt is carried at its present value.

10. Inventories

At the end of 2006 and 2005, the balances of this account were 1,190,293 and 1,248,442 euros, respectively, and consisted exclusively of intermediate and consumption raw materials.

11. Clients

The composition of the "Clients" account at 31 December 2006 and 2005 was as follows:

	2006	2005
Clients, current account	22,449,544	20,671,180
Clients, doubtful debtors	2,741,795	2,312,232
Adjustments for doubtful debtors	(2,076,701)	(1,760,123)
Subtotal, clients	23,114,637	21,223,289
Accrued income on account of water to be invoiced	7,373,361	7,528,920
Accrued income on service fee to be invoiced	1,941,492	1,886,239
Accrued income on services provided, to be invoiced	107,796	119,571
	32,537,286	30,758,019

Changes in the year

Changes in the balances for doubtful debtors and related adjustments in 2006 were the following:

	2005	Increases	Decreases	2006
Doubtful debtors	2,312,232	517,386	(87,823)	2,741,795
Adjustments to doubtful debtors (Notes 28 and 32)	(1,760,123)	(387,341)	70,763	(2,076,701)
	552,109	130,045	(17,060)	665,094

Increases in the balances of and adjustments to Doubtful debtors follow from the evaluation of collection risk to client receivables.

Decreases result primarily from the recovery of previously provided claims.

The balance of Doubtful debtors amounts to 2,741,795 euros and is composed of 2,076,701 euros where collection risk is borne by the company and entirely provided for and 665,094 euros relating to treatment fee and addition where the risk is borne by third parties.

12. Claims on public-sector entities

At 31 December 2006 and 2005, claims receivable from the state and other public-sector entities for 5,601,240 and 6,077,056 euros, respectively, related entirely to requests for value-added tax (VAT) refunds.

13. Other debtors

At 31 December 2006 and 2005 "Other debtors" had the following composition:

	2006	2005
Associates	1,333,246	1,323,246
Staff	60,148	64,729
Other debtors, miscellaneous	1,059,636	1,551,222
Adjustments to other doubtful debtors	(634,907)	(614,395)
Subtotal	1,818,123	2,324,801
Other accrued income	35,070	18,502
Deferred cost for prepaid insurance premiums	901,093	767,599
Other deferred costs	415,855	499,185
	3,170,141	3,610,087

Associates

The amount recorded under "Group companies and associates" is exclusively related to shareholder loans extended to Clube de Golfe das Amoreiras, S.A.

Changes in "Adjustments to other doubtful debtors"

Changes in the year were as follows:

	2006	2005
Opening balance	614,395	585,981
Increase / Period charges (Note 28)	31,383	32,851
Reversal (Note 32)	(10,871)	(4,436)
Ending balance	634,907	614,395

14. Cash and cash equivalents

At 31 December 2006 and 2005 "Cash and cash equivalents had the following composition:

	2006	2005
Bank deposits	26,050	35,568
Cash on hand	3,504,937	2,696,208
Subtotal	3,530,987	2,731,776
Other treasury investments	-	3,400,000
	3,530,987	6,131,776

15. Share capital

Share capital of 150 million euros consists of 30 million shares of 5 euros each and is fully paid up.

Shareholders

At 31 December 2006, the company was entirely owned by AdP - Águas de Portugal, SGPS, S.A..

Earnings per share

	2006	2005
Net profit for the year	16,328,528	23,787,526
Average number of shares	30,000,000	30,000,000
(Basic and diluted) earnings per share	0.54	0.79

16. Reserves and other adjustments

At the end of the year, reserves and other adjustments were as follows:

	2006	2005
Adjustments to equity holdings in associates	(4,064)	(4,064)
Revaluation reserves	114,105,399	118,164,897
Legal reserves	25,592,236	23,213,483
Free reserves	22,171,377	22,171,377
	161,864,948	163,545,694

Note: View together with the statement of changes in equity

The change in "Revaluation reserves" in 2006 was as follows:

	2005	Transfers	Other	2006
Revaluation reserves				
Revaluation reserves, booked	256,514,383	-	-	256,514,383
Revaluation reserves, realised	(127,836,183)	(4,968,456)	-	(132,804,640)
(Note 6)	128,678,200	(4,968,456)	-	123,709,743
Related deferred tax				
Deferred tax, booked	(21,042,483)	-	-	(21,042,483)
Deferred tax, realised	10,529,180	546,530	362,428	11,438,139
(Note 8)	(10,513,302)	546,530	362,428	(9,604,344)
Net amount of revaluation reserves	118,164,897	(4,421,926)	362,428	114,105,399

Transfers: Amounts in the "Transfers" column relate to the transfer to "Retained earnings" of the portion of revaluation reserves realised through amortisation, disposal or write-off of the related fixed assets and deferred taxes in 2006.

Legal reserve: Commercial law stipulates that at least 5% of net profit for the year - EPAL's articles of association raise this level to 10% - should be allocated to increasing legal reserves until these represent at least 20% of share capital. These reserves may not be distributed unless the company is liquidated but may be used to cover losses after the other reserves have been used or to issue a stock dividend.

Appropriation of net profit: Pursuant to a resolution at the shareholder meeting of 20 March 2006, the company appropriated net profit of 23,787,526 for the year ended 31 December 2005 as follows:

Transferência:	
Para reservas legais	2,378,753
Para resultados transitados	2,591,721
	4,970,474
Distribuição:	
De dividendos à holding	17,840,645
De lucros ao pessoal	976,407
	18,817,052
	23,787,526

Additional explanatory note to the Statement of changes in equity: In the year ended 31 December 2005 an accounting adjustment was made for 21,430,279.58 as a result of the analysis conducted on the amount of unrealised revaluation reserves at 1 January 2005. After this adjustment and the annual transfer of the revaluation reserves realised during 2005, the amount of 118,164,897 euros represented the amount of unrealised revaluation reserves, net of deferred taxes, at 31 December 2005.

17. Provisions

At 31 December 2006 and 2005 the composition of provisions was the following:

	2006	2005
Litigation in progress	7,377,774	7,152,891
Workplace accidents	230,357	275,865
Other risks and charges	11,388,746	11,300,746
	18,996,877	18,729,502

Changes in "Provisions" in 2006 are broken down as follows:

	2005	Increases (Note 29)	Reductions	2006
Litigation in progress	7,152,891	768,385	(543,501)	7,377,774
Workplace accidents	275,865	-	(45,508)	230,357
Other risks and charges	11,300,746	200,500	(112,500)	11,388,746
	18,729,502	968,885	(701,509)	18,996,877

The company conducted a careful and thorough review of the situation regarding commitments, present, probable or contingent obligations, lawsuits, unsettled tax cases and complaints or contentious issues. On the basis of this review and after a careful risk analysis, the company considered that the 18,996,877 euros in "Provisions" at 31 December 2006 is an adequate amount to provide against the identified risks.

The "Reductions" column total of 701,509 euros includes 656,001 euros recorded as extraordinary income (Note 35) and 45,508 euros recorded as staff costs.

18. Pension obligations

EPAL has a social benefit plan for its employees entailing a commitment to pay a complement to the retirement pension (for long service or disability) granted by the Social Security. Additionally, the company bears the obligations arising from early retirement.

Obligations deriving from the pension plan are funded by EPAL's pension fund, set up in November 1990, while early retirement is borne directly by the company.

The company's overall obligations are covered by the pension fund's assets and a specific provision recorded as a liability.

At 31 December 2006 and 2005 the obligations for past service linked to the social benefit plan were the following:

Change in obligations	2006	2005
Obligations at start of period	95,475,448	89,752,258
Current-service cost	2,262,000	2,003,446
Interest cost	4,394,000	4,510,919
Actuarial (gains)/losses	(909,708)	5,099,030
Benefits paid	(5,757,036)	(5,890,206)
Obligations at end of period	95,464,704	95,475,448

The obligations in the above table were calculated on the basis of the following actuarial and financial assumptions:

	2006	2005
Mortality table	TV 88/90	TV 88/90
Disability table	EVK 80	EVK 80
Annual discount rate	4.75%	4.75%
Annual rate of return	4.75%	4.75%
Salary growth rate	2.50%	2.50%
Salary growth rate, Social Security	2.50%	2.50%
Growth rate of pre-retirement contributions	2.50%	2.50%

The fund's assets progressed as follows:

Pension fund	2006	2005
Amount at start of period	41,383,875	36,676,983
Effective return	2,576,422	2,866,892
EPAL contribution	3,726,602	3,559,717
Benefits paid	(1,726,602)	(1,719,717)
Amount at end of period	45,960,297	41,383,875

As a complement to the fund's assets, the company recognised at 31 December 2006, as a liability, a provision for pension obligations for an amount of 25.8 million euros.

The overall situation is summed up in the following table:

	2006	2005
Obligations at end of period	95,464,704	95,475,448
Asset value at end of period	45,960,297	41,383,875
Provision for pensions	25,775,964	18,484,000
Deferred actuarial losses	23,728,443	35,607,573
Prior service cost	2,650,036	11,887,000
Losses within the 10% corridor	9,546,470	9,547,545
Losses in excess of the 10% corridor	11,531,937	14,173,028

In the year ended 31 December 2006, the company's board of directors sponsored a change in the present, defined benefit, pension plan, implying significant funding commitments. Considering the estimated probability of success of the proposed change, the company increased the provisions for pensions and recognised as period cost the portion of prior service costs not yet recognised as a cost in previous years, equivalent to the charges inherent to the adoption of the plan changes for an approximate amount of 7.7 million euros. In this way, the overall cost of post-employment benefits amounted in 2006 to 15,049,000 euros, as follows:

	2006	2005
Current service cost	2,262,000	2,003,000
Interest cost	4,393,000	4,510,758
Expected return on the assets	(1,978,000)	(1,916,000)
Recognition of prior service cost	9,236,000	1,556,000
Recognition of deferred actuarial losses	1,136,000	902,000
Cost for the period (Note 27)	15,049,000	7,055,758

Deferred actuarial losses exceeding the higher of the 10% limit of the value of the funds allocated to covering the company's obligations and 10% of the value of obligations for past service are recognised for the period between the active population's average age and retirement age.

Following the proposed change to the present pension plan and the company's continued goal of raising its funding level, the company contributed in 2006 a robust 3.7 million euros to the fund.

19. Bank loans

Bank loans at 31 December 2006 and 2005 are detailed as follows:

	2006			2005		
	Maturing in 1 year	Maturing in 1 to 5 yrs	Maturing in after 5 yrs	Total Medium and long term	Commercial paper	Total Medium and long term
Banco Europeu do Investimento (BEI)	6,018,390	38,251,752	163,938,043	202,189,795	5,396,700	175,208,185

In 2006, the company turned, occasionally and for very short periods, to commercial-paper funding for an overall amount of 33 million euros. These utilisations were entirely repaid by the end of 2006. In the cash flow statement for the year, these movements of funds have been cleared against each other.

20. Investment grants

At 31 December 2006 and 2005 liabilities relating to investment grants are detailed as follows:

	2006	2005
Investment grants	87,798,859	87,798,859
Recognised income	(41,250,301)	(38,597,538)
	46,548,558	49,201,321

The change of 2,652,763 euros in the year (Note 35) relates to the annual proportion of the grants recognised in the income statement.

21. Suppliers and other accounts payable

At 31 December 2006 and 2005, the balances of "Suppliers and other accounts payable" had the following composition:

	2006	2005
Suppliers, current account	21,117,867	19,432,795
Suppliers, invoices received and under processing	217,664	241,231
Suppliers of fixed assets	20,452,879	22,504,050
Accrued costs	1,522,639	2,122,638
	43,311,049	44,300,714

22. Debts to the state and other public-sector entities

At 31 December 2006 and 2005 debts to the state and other public-sector entities were as follows:

	2006	2005
State company income tax (IRC)		
Estimate of IRC	9,138,175	11,430,401
Advance payments	(8,674,124)	(8,698,224)
Withholdings	(59,130)	(54,718)
Provision for additional payment of IRC	-	650
Subtotal IRC	404,921	2,678,110
State personal income tax (IRS)	289,542	264,428
Social Security	498,985	487,997
Stamp duty	11,950	12,180
	1,205,398	3,442,715

23. Other creditors

At 31 December 2006 and 2005 balances of "Other creditors" were as follows:

	2006	2005
City of Lisbon		
Treatment rate (Portaria 399/85)	11,354,736	10,754,782
Additional rate (Portaria 309/84)	1,227,892	1,109,735
Holidays and holiday allowance	3,751,693	3,469,947
Interest payable	1,090,453	841,552
Insurance premiums payable	125,605	79,789
Staff	4,092	4,002
Miscellaneous creditors	147,329	287,499
	17,701,800	16,547,305

24. Sales and provision of services

In 2006 and 2005 sales and the provision of services were broken down as follows:

	Domestic market
Financial year ended 31 December 2006	
Sales of water and service fee	134,424,191
Services provided	2,935,789
	137,359,980
Financial year ended 31 December 2005	
Sales of water and service fee	134,033,957
Services provided	3,351,336
	137,385,292

25. Cost of sales

In 2006 and 2005 the cost of sales was broken down as follows:

	2006	2005
Inventory at start of period	1,248,442	1,136,922
Purchases	2,741,069	3,216,261
Adjustments to inventory (Note 35)	9,523	(1,905)
Inventory at end of period	1,190,293	1,248,442
	2,808,741	3,102,836

26. Current costs

In 2006 and 2005 current costs were detailed as follows:

	2006	2005
Electricity	8,855,666	8,776,896
Maintenance and repairs	8,587,755	8,095,325
Specialist works	6,659,741	5,249,876
Communications	1,349,259	1,270,183
Rents	1,218,429	1,177,158
Insurance premiums	1,162,401	1,085,768
Sub-contracts	1,083,742	920,963
Fuels	520,233	481,834
Other current costs	8,183,595	7,656,938
	37,620,821	34,714,940

The main suppliers to the company (for higher amounts than 5% of total current costs) in 2006 are presented in the following table:

Name	Amount
EDP Distribuição de Energia, SA	7.627.462,48
AdP - Águas de Portugal, SGPS, SA	2.807.920,50
CME - Construção, Manutenção Electromecânica, SA	2.313.929,38
Câmara Municipal de Lisboa	2.299.429,50
ELESA-Empresa Lisbonense de Empreitadas	2.233.337,45
ENDESA ENERGIA, SA	1.930.176,56

27. Staff costs

In 2006 and 2005 staff costs were detailed as follows:

	2006	2005
Remuneration	20,300,548	19,356,650
Pensions (Note 18)	15,049,000	7,055,758
Other	6,352,970	5,982,315
	41,702,518	32,394,724

Remuneration of governing bodies

Remunerations earned by the governing bodies in 2006 were the following:

Board of directors	521.582
Chartered accountant	17.912
	<u>539.494</u>

Average number of employees

The average number of employees at the company's service at 31 December 2006 and 2005 was as follows:

	2006	2005
Governing bodies	4	4
Permanent employees and others	813	814
	817	818

28. Depreciation and adjustments in the year

Depreciation and period adjustments in 2006 and 2005 are detailed as follows:

	2006	2005
Depreciation of tangible fixed assets (Note 6)	27,899,007	27,189,402
Adjustments to accounts receivable (Note 11)	387,341	369,670
Adjustments to accounts receivable (Note 11)	31,383	32,851
	28,317,730	27,591,923

29. Provisions for the period

Provisions in 2006 and 2005 are detailed as follows:

	2006	2005
From litigation	768,385	373,132
From other risks and charges	200,500	5,225,000
(Note 17)	968,885	5,598,132

30. Other operating costs

Other operating costs in 2006 and 2005 are detailed as follows:

	2006	2005
Taxes and levies	692,213	874,611
Other operating costs	23,026	22,817
	715,239	897,428

31. Additional revenues

Additional revenues in 2006 e 2005 are detailed as follows:

	2006	2005
Treatment charges	316,356	327,617
Aquamatrix service	273,317	533,971
Laboratory analyses	155,985	190,897
Rents	88,146	87,826
Legal help with expropriations	87,823	85,932
Royalties	86,345	64,341
Tender specifications	77,800	158,750
Meter repairs	54,797	30,200
Social services	11,869	11,592
Other	237,919	490,447
	1,390,356	1,981,573

32. Other operating revenues and gains

Other operating revenues and gains in 2006 and 2005 are detailed as follows:

	2006	2005
Subsidies to operations	-	3,281
Reversals of adjustments to clients (Note 11)	70,763	119,559
Reversals of adjustments to other debtors (Note 13)	10,870	4,436
	81,633	127,276

33. Financial costs

Financial costs in 2006 e 2005 are detailed as follows:

	2006	2005
Interest paid	6,383,340	4,760,101
Adjustments to financial investments (Note 7)	182,143	257,374
Losses on associates (Note 7)	15,025	26,835
Unfavourable exchange differences	303	130
Other financial costs and losses	129,902	155,316
	6,710,712	5,199,755

34. Financial income

Financial income in 2006 and 2005 is broken down as follows:

	2006	2005
Interest received	216,044	200,776
Favourable exchange differences	356	28
Cash discounts obtained	177	1,849
Reversals and other financial income and gains	17,232	17,610
	233,810	220,264

35. Extraordinary results

The statement of extraordinary results for 2006 and 2005 is as follows:

	2006	2005
Donations	34,688	58,406
Losses on inventory (Note 25)	1,688	2,128
Losses on fixed assets	3,377	21,373
Fines and penalties	44,841	1,043
Corrections to previous years' accounts	5	10,468
Other extraordinary costs and losses	386,808	285,640
Total costs and losses	471,406	379,059
Gains on inventory (Note 25)	11,211	223
Gains on fixed assets	27,213	19,958
Reductions in provisions (Note 17)	656,001	34,669
Corrections to previous years' accounts	340	345
Investment grants (Note 20)	2,652,763	3,021,933
Other extraordinary income and gains	93,214	203,352
Total income and gains	3,440,743	3,280,481
	2,969,337	2,901,422

36. Taxes

At 31 December 2006, the company was liable for company income tax at the standard rate of 25% which may be increased by up to 10% by local tax, resulting in an aggregate tax rate of 27.5%.

According to the law, tax returns may be reviewed and corrected by tax authorities for a period of four years (ten years for Social Security up to and including year 2000 and five years from 2001) except when there have been tax losses, tax benefits granted, ongoing tax audits or claims filed, in which cases, according to the circumstances, standard terms are extended or suspended. As the company's tax returns for the years up to and including 2003 have been audited, returns for the years from 2004 to 2006 may still be audited. The company's board understands that corrections, if any, that may result from tax audits will not have a significant effect on the financial statements at either 31 December 2006 or 2005.

Income tax (IRC) recorded as period cost for the years ended 31 December 2006 and 2005 is corrected by the accounting of deferred taxes in accordance with Accounting Guideline n° 28.

At 31 December 2006 and 2005 the nominal tax rate is reconciled with the effective tax rate as follows:

	2006	2005
Profit before tax	23,265,062	33,295,432
Tax base	23,265,062	33,295,432
Tax @ 27,50%	6,397,892	9,156,244
Effect of permanent differences	(10,179)	245,283
Separate taxation	124,259	121,820
Effect of the change in the aggregate tax rate (Note 8)	424,562	-
Other	-	(15,442)
Tax charge	6,936,534	9,507,906
Current tax	9,138,175	11,430,401
Deferred tax	(2,201,641)	(1,922,495)
Effective tax rate	29.82%	28.56%

37. Contingent liabilities and guarantees provided

Contingent liabilities

The company has carefully evaluated its risks and contingencies whereupon provisions were made that, in the face of the identified risks, were considered to be adequate. The said evaluation did not identify, beyond the recorded provisions, any other contingent obligations that should be disclosed as liabilities.

Guarantees

At 31 December 2006 and 2005 the company had obligations on account of guarantees provided as follows:

	2006	2005
European Investment Bank	18,489,220	28,270,432
Municipalities	15,086,260	12,275,079
Courts of law	5,433,496	6,308,617
Other	478,459	543
	39,487,436	46,854,670

38. Note to the income statement by function

At 31 December 2006, the main items of the income statement by function were as follows:

a) Cost of sales and provision of services

The item "Cost of sales and provision of services" included 37,469,064 euros relating to operating costs for the Production business area less 2,267,243 euros in income from the annual transfer of investment grants for assets allocated to the Production area.

The allocation of 2,652,763 euros in annual income from investment grants to the various items in the income statement by function in 2006 and 2005 is as follows:

	2006	2005
Cost of sales and provision of services	2,267,243	2,636,414
Distribution costs	381,779	381,779
Other operational costs and losses	3,741	3,741
	2,652,763	3,021,933

b) Distribution costs

This item amounted in 2006 to 31.3 million euros and reflected primarily operating costs in the Distribution business area which amounted in the year ended 31 December 2006 to 31,405,111 euros.

c) Administrative costs

At 31 December 2006, this item included mainly operating costs from all supporting areas in the company.

d) Net borrowing cost

This item includes interest on bank loans for an amount of 6,381,803 euros and costs of 116,048 euros incurred with bank guarantees for EIB loans.

e) Tax on current results

Reconciliation between tax in the income statement by nature and tax in the income statement by function is as follows:

	2006	2005
Total taxes for the period	6,936,534	9,507,906
Excess tax estimate	49,747	(35,229)
	6,986,281	9,472,676



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ACCOUNTING DOCUMENTS REQUIRED
BY THE OFFICIAL ACCOUNTING PLAN

Balance sheets at 31 December 2006 and 2005

ASSETS	Years			
	2006		2005	
	Gross assets	Depreciation and adjustments	Net assets	Net assets
FIXED ASSETS				
Intangible fixed assets				
Industrial property and other rights	21,300	-	21,300	21,300
Total	21,300	-	21,300	21,300
Tangible fixed assets				
Land and natural resources	49,247,566	-	49,247,566	49,247,566
Buildings and other constructions	98,059,427	70,722,400	27,337,027	29,664,938
Production equipment	874,914,831	374,151,176	500,763,655	479,982,956
Transportation equipment	1,655,748	1,649,837	5,911	14,352
Tools	10,084,654	8,735,794	1,348,860	1,861,943
Office equipment	15,860,099	14,556,301	1,303,798	940,214
Containers	8,134	7,040	1,095	1,441
Other tangible fixed assets	10,361,334	7,872,113	2,489,221	2,944,047
Fixed assets in progress	74,252,834	-	74,252,834	62,801,147
Advances on account of tangible fixed assets	-	-	-	1,706,336
Total	1,134,444,628	477,694,661	656,749,968	629,164,940
Financial investments				
Equity holdings in associates	5,263,150	5,003,174	259,976	275,001
Securities and other financial investments	109,172	-	109,172	109,172
Total	5,372,322	5,003,174	369,148	384,173
DEBTORS, MEDIUM- AND LONG-TERM				
Other debtors	710,979	-	710,979	738,324
Total	710,979	-	710,979	738,324
CURRENT ASSETS				
Inventory				
Raw materials, intermediate and ready to use	1,190,293	-	1,190,293	1,248,442
Total	1,190,293	-	1,190,293	1,248,442
Debtors, short-term				
Clients, current account	22,449,544	-	22,449,544	20,671,180
Clients, doubtful debtors	2,741,795	2,076,701	665,093	552,109
Associates	1,333,246	-	1,333,246	1,323,246
Public sector	5,601,240	-	5,601,240	6,077,056
Other debtors	1,119,784	634,907	484,877	1,001,555
Total	33,245,609	2,711,609	30,534,000	29,625,145
Marketable securities				
Other treasury investments	-	-	-	3,400,000
Total	-	-	-	3,400,000
BANK DEPOSITS AND CASH ON HAND				
Bank deposits	3,504,937	-	3,504,937	2,696,208
Cash on hand	26,050	-	26,050	35,568
Total	3,530,987	-	3,530,987	2,731,776
ACCRUALS AND DEFERRALS				
Accrued income	9,457,719	-	9,457,719	9,553,232
Deferred costs	1,316,949	-	1,316,949	1,266,784
Deferred tax assets	11,303,607	-	9,651,826	-
Total	22,078,274	-	22,078,274	20,471,843
Total depreciation and adjustments		485,409,444		
Total assets	1,200,594,392		715,184,949	687,785,943

The notes to the financial statements are an integral part of the balance sheet at 31 December 2006

The Financial Manager and Chief Accountant
Daniela Marina Alves Fernandes Valle Santos

The board of directors
João Manuel Lopes Fidalgo, *Chairman*
Jorge Luís Ferrão de Mascarenhas Loureiro, *Director*
José Alfredo Manita Vaz, *Director*
António Bento Franco, *Director*
Rui Manuel de Carvalho Godinho, *Director*

SHAREHOLDERS' EQUITY AND LIABILITIES	Exercícios	
	2006	2005
SHAREHOLDERS' EQUITY		
Share capital	150,000,000	150,000,000
Adjustments to equity holdings in subsidiaries and associates	(4,064)	(4,064)
Revaluation reserves	114,105,399	118,164,897
Reserves:		
Legal reserves	25,592,236	23,213,483
Other reserves	22,171,377	22,171,377
Retained earnings	15,586,586	8,572,938
Sub-Total	327,451,534	322,118,632
Net profit for the year	16,328,528	23,787,526
Total shareholders' equity	343,780,062	345,906,158
LIABILITIES		
Provisions for risks and charges		
Other provisions for risks and charges	18,996,877	18,729,502
Total	18,996,877	18,729,502
Indebtedness to third parties - Medium- and long term		
Indebtedness to credit institutions	202,189,795	175,208,185
Total	202,189,795	175,208,185
Indebtedness to third parties - Short-term		
Indebtedness to credit institutions	6,018,390	5,396,700
Suppliers, current account	21,117,867	19,432,795
Suppliers - Invoices received in progress	217,664	241,231
Suppliers of fixed assets, current account	20,452,879	22,504,050
Public sector	1,205,398	3,442,715
Other creditors	12,726,431	12,130,983
Total	61,738,628	63,148,473
ACCRUALS AND DEFERRALS		
Cost accruals	32,272,235	25,021,254
Deferred income	46,550,296	49,203,028
Deferred tax liabilities	9,657,055	10,569,344
Total	88,479,587	84,793,626
Total liabilities	371,404,886	341,879,785
Total shareholders' equity and liabilities	715,184,949	687,785,943

The notes to the financial statements are an integral part of the balance sheet at 31 December 2006

The Financial Manager and Chief Accountant

Daniela Marina Alves Fernandes Valle Santos

The board of directors

João Manuel Lopes Fidalgo, *Chairman*
 Jorge Luís Ferrão de Mascarenhas Loureiro, *Director*
 José Alfredo Manita Vaz, *Director*
 António Bento Franco, *Director*
 Rui Manuel de Carvalho Godinho, *Director*

Income statement by nature for the years ended on 31 December 2006 and 2005

COSTS AND LOSSES	Years			
		2006		2005
Cost of goods sold				
Materials		2,808,741	2,808,741	3,102,836
Current costs			37,620,821	34,714,940
Staff costs:				
Remuneration		20,300,548		19,356,650
Social charges				
Pensions		3,726,602		3,559,717
Other		17,675,367	41,702,518	9,478,357
Depreciation of tangible and intangible fixed assets		27,899,007		27,189,402
Adjustments		418,724		402,520
Provisions		968,885	29,286,615	5,598,132
Tax		692,213		874,611
Other operating costs and losses		23,026	715,239	22,817
	A		112,133,933	104,299,983
Interest and similar costs		6,710,712	6,710,712	5,199,755
	C		118,844,646	109,499,738
Extraordinary costs and losses			471,406	379,059
	E		119,316,052	109,878,798
Tax on profit for the year			6,936,534	9,507,906
	G		126,252,586	119,386,703
Net profit for the year			16,328,528	23,787,526
			142,581,114	143,174,229
INCOME AND GAINS				
Sales:				
Products		134,424,191		134,033,957
Services provided		2,935,789	137,359,980	3,351,336
Own works		74,592		179,343
Supplementary income		1,390,356		1,981,573
Subsidies to operations		-		3,281
Reversals of depreciation and adjustments		81,633	1,546,581	123,995
	B		138,906,561	139,673,484
Interest and similar income		233,810	233,810	220,264
	D		139,140,371	139,893,748
Extraordinary income and gains			3,440,743	3,280,481
	F		142,581,114	143,174,229
SUMMARY				
Net operating income:	(B) - (A) =		26,772,628	35,373,501
Net financial income:	(D - B) - (C - A) =		(6,476,902)	(4,979,491)
Net current income:	(D) - (C) =		20,295,725	30,394,010
Profit before tax:	(F) - (E) =		23,265,062	33,295,432
Net profit for the year:	(F) - (G) =		16,328,528	23,787,526

The notes to the financial statements are an integral part of the income statement by nature for the year ended 31 December 2006

The Financial Manager and Chief Accountant

Daniela Marina Alves Fernandes Valle Santos

The board of directors

João Manuel Lopes Fidalgo, *Chairman*

Jorge Luís Ferrão de Mascarenhas Loureiro, *Director*

José Alfredo Manita Vaz, *Director*

António Bento Franco, *Director*

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Appended notes

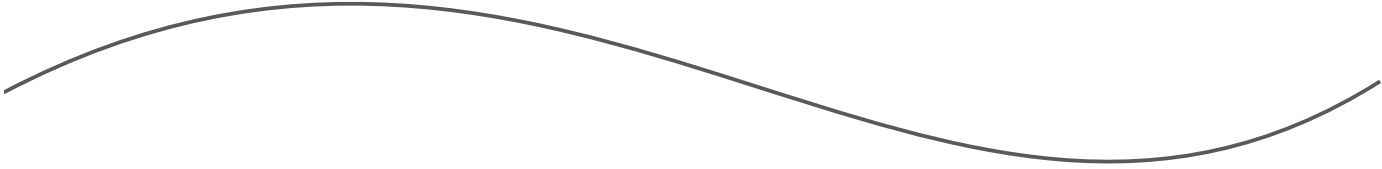
The numbering of the appended notes as required by the Official Accounting Plan is reconciled with the numbering of the presented notes as follows:

Note POC	Description	Notes appended
1.	POC rules waived in the period	2
2.	Comparability	n.a
3.	Bases of presentation and main valuation criteria	2
4.	Share prices	n.a
5.	Tax benefits relevant for the period	n.a
6.	Income tax	36
7.	Average number of employees	27
8.	Note to the accounts for establishment costs and research and development	n.a
9.	Explanation for depreciating establishment transmission value beyond five years	n.a
10.	Changes in fixed assets and related depreciation and adjustments	5,6,7 e 28
11.	Funding of fixed assets booked for the period	n.a
12.	Revaluation of tangible fixed assets (legislation)	6
13.	Table detailing revaluations	6
14.	Fixed assets in third parties' possession	6
15.	Goods used under financial leases	n.a
16.	Equity holdings in group companies and associates	7
17.	Shares and parts of the Marketable securities account exceeding 5% of current assets	n.a
18.	Breakdown of account 4154 - Funds	n.a
19.	Materially relevant differences between market prices and valuation of current assets	n.a
20.	Valuation of current-asset items below market prices	n.a
21.	Adjustments	11 e 13
22.	Inventory in third parties' possession	n.a
23.	Doubtful debts	11 e 13
24.	Loans extended to governing body members	n.a
25.	Debts to and claims on company staff	13 e 23
26.	Debts materialised by balance sheet items but not reported on the balance sheet	n.a
27.	Dated and undated bonds issued by the company	n.a
28.	Overdue amounts on the Public sector account	n.a
29.	Debts to third parties maturing after five years	19
30.	Debts to third parties backed by collateral	n.a
31.	Commitments not reported on the balance sheet	18
32.	Guarantees provided	37
33.	Difference between debts payable and related amounts	n.a
34.	Provisions	17
35.	Equity increases and reductions	n.a
36.	Composition of the share capital	15
37.	Identification of legal persons owning more than 20% of the share capital	7
38.	Shares and parts subscribed in the period	n.a
39.	Change in revaluation reserves in the period	16
40.	Changes in Shareholders' equity	Statement of changes in equity
41.	Statement of cost of goods sold	25
42.	Statement of change in production	n.a
43.	Remuneration of governing bodies	27
44.	Breakdown of sales and services provided	24
45.	Statement of net financial income	33 e 34
46.	Statement of net extraordinary income	35
47.	Disclosures required by law	n.a
48.	Other relevant disclosures	12,13,14,19, 22 e 23

n.a. - not applicable



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AUDIT REPORT

Introduction

1. We have examined the appended financial statements of EPAL - Empresa Portuguesa das Águas Livres, S.A. consisting of the balance sheet at 31 December 2006 that evidences a total of 715,184,949 euros, equity of 343,780,062 euros including a net result of 23,787,526.20 euros, the income statements by nature and function, the statement of changes in equity, the cash flow statement for 2006 as well as the relevant notes.

Responsibilities

2. It is the board of directors' responsibility to prepare such financial statements that shall, in a true and appropriate manner, present the financial position of the company, the result and cash flows of its operations, as well as adopt adequate accounting principles and policies and maintain an appropriate internal control system. Our responsibility consists of expressing a professional and independent opinion based on our examination of the aforementioned financial statements.

Scope

3. Our examination has been conducted in accordance with the Technical Standards and the Auditing Guidelines of the Institute of Chartered Accountants, which require the examination to be planned and executed in such a manner that an acceptable confidence level can be obtained that the financial statements do not contain materially relevant distortions. This examination has involved, on a sampling basis, checking the basis for the amounts and information disclosed in the financial statements, evaluating the estimates used for their preparation, based on judgements and criteria defined by the board of directors, assessing whether the adopted accounting principles and their disclosure are adequate in view of the circumstances, checking the applicability of the continuity principle and judging the overall adequacy of the financial statements' presentation. We consider that our examination provides an acceptable basis for our opinion.

Opinion

4. In our opinion, the financial statements referred to in paragraph 1 present in a true and appropriate manner, in all materially relevant respects, the financial position of EPAL - Empresa Portuguesa das Águas Livres, S.A. at 31 December 2006 as well as the result and the cash flows of its operations in 2006, in accordance with generally accepted accounting principles in Portugal.

Emphasis

5. The balance sheet and the income statement by nature (which have been, as mentioned in in Note 2.a), restated in order to be presented in a different format from the one called for by Plano Oficial de Contabilidade), the income statement by function and the cash flow statement for the year ended 31 December 2005, which are presented for comparative purposes, have been audited by another firm of chartered accountants, whose report of 10 March 2006 does not contain any qualifications.

Lisbon, 16 March 2007

DELOITTE & ASSOCIADOS, SROC S.A.

Represented by João Luís Falua Costa da Silva

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