

COMPANHIA DE SANEAMENTO BASICO DO ESTADO DE SAO PAULO-SABESP
Form 20-F
May 12, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20 F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

o ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2015

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report _____

Commission file number 001 31317

Companhia de Saneamento Básico do Estado de São Paulo–SABESP
(Exact name of Registrant as specified in its charter)

Basic Sanitation Company of the State of São Paulo SABESP
(Translation of the Registrant's name into English)

Federative Republic of Brazil
(Jurisdiction of incorporation or organization)

Rua Costa Carvalho, 300
05429 900 São Paulo, SP, Brazil
(Address of principal executive offices)

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Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Shares, without par value	New York Stock Exchange
American Depositary Shares, evidenced by American Depositary Receipts, each representing one Common Share	New York Stock Exchange

Not for trading purposes, but only in connection with the registration of American Depositary Shares pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

683,509,869 Shares of Common Stock

Indicate by check mark if the registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow

Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

General

We maintain our books and records in *reais*. We prepare our financial statements in accordance with International Financial Reporting Standards, or “IFRS”, as issued by the International Accounting Standards Board, or the “IASB”. Our financial statements as of December 31, 2015 and 2014 and for the three years ended December 31, 2015 have been audited, as stated in the report appearing herein, and are included in this annual report on Form 20 F.

Certain figures included in this annual report have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

Water Crisis

Our results and operational performance for the fiscal year ended December 31, 2015, were adversely impacted by the most serious drought in our serviced region in 85 years. Both the water conservation measures we implemented to mitigate the effects of the drought on our water supply and a significantly heightened public awareness of the need to conserve water during the current water crisis negatively impacted our revenues. Improved rainfall throughout the rainy season that began in October 2015, the collaborative efforts between us and the population we service and emergency construction conducted by us throughout 2014 and 2015 in order to reduce the impacts of the water crisis resulted in an increase in the volume of water in the reservoirs in our largest market, the São Paulo metropolitan region, at the end of 2015 compared to the end of 2014. As of December 31, 2015, the reservoirs in the São Paulo metropolitan region, where our largest market is located, contained 703 billion liters of bulk water storage for treatment, compared to 301 billion liters available for treatment as of December 31, 2014. Under normal circumstances, we withdraw 6.2 billion liters per day (equivalent to the total water production of 71.4 m³/s in February 2014 for the São Paulo metropolitan region) from the reservoirs. This volume decreased to 4.7 billion liters per day during the drought (equivalent to the total water production of 54.8 m³/s in December 2015 for the São Paulo metropolitan region). Average monthly water production in 2015 was of 52.0 m³/s, compared to 62.2 m³/s in 2014 and 69.1 m³/s in 2013. For more information, see “Item 3.D. Risk Factors—Risks Relating to Our Business—The measures we took to mitigate the effects of the drought resulted in a significant decrease in the volume of water billed and revenues from services we provide, which had a material adverse effect on our company and could continue to do so if the drought escalates in severity” and “Item 4.B. Business Overview—The Current Water Crisis”.

Convenience Translations

We have translated some of the *real* amounts contained in this annual report into U.S. dollars. The rate used to translate such amounts in respect of the year ended December 31, 2015 was R\$3.9048 to US\$1.00, which was the commercial rate for the purchase of U.S. dollars in effect on December 31, 2015, as reported by the Central Bank. The U.S. dollar equivalent information presented in this annual report is provided solely for the convenience of the reader and should not be construed as implying that the *real* amounts represent, or could have been or could be converted into, U.S. dollars at the above rate. See “Item 3.A. Selected Financial Data—Exchange Rates” for more detailed information regarding the Brazilian foreign exchange system and historical data on the exchange rate of the *real* against the U.S. dollar.

Rounding

Some percentages and numbers included in this annual report have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures that precede them.

Other Information

In this annual report, unless the context otherwise requires, references to “we,” “us,” “our,” “Company,” or “SABESP” refer to Companhia de Saneamento Básico do Estado de São Paulo – SABESP.

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In addition, references to:

- “ARSESP” are to the São Paulo State Sanitation and Energy Regulatory Agency (*Agência Reguladora de Saneamento e Energia do Estado de São Paulo*);
- “ADR” or “ADRs” are to American Depositary Receipt or American Depositary Receipts, respectively;
- “ADS” or “ADSs” are to American Depositary Share or American Depositary Shares, respectively;
- “Brazil” are to the Federative Republic of Brazil;
- “Central Bank” are to the Central Bank of Brazil;
- “CVM” are to the *Comissão de Valores Mobiliários*, the Brazilian regulator of securities;
- “federal government” and “Brazilian government” are to the federal government of the Federative Republic of Brazil and “state government” are to the state government of the State of São Paulo;
- “real,” “reais” or “R\$” are to the Brazilian real, the official currency of Brazil;
- “Regional Systems” are to the area where the regional systems’ executive office operates, comprising 326 municipalities in the interior and coastline regions of the state of São Paulo;
- “São Paulo metropolitan region,” with respect to our operations, are to the area where the metropolitan executive office operates, comprising 38 municipalities, including the city of São Paulo;
- “sewage coverage ratio” are to the ratio between the number of residences connected to the sewage collection network, divided by the number of urban residences in a certain area;
- “State” are to the State of São Paulo, which is also our controlling shareholder;
- “U.S. dollars” or “US\$” are to the United States dollar, the official currency of the United States;
- “water coverage ratio” are to the ratio between the number of residences connected to the water supply network, divided by the number of urban residences in a certain area; and
- “water crisis” are to the drought we have experienced from late 2013 throughout most of 2015. This drought is the most serious drought that our service region has experienced in 85 years and primarily affects the Cantareira System, our largest water production system.

Information in this annual report related to liters, water and sewage volumes, number of employees, kilometers, water and sewage connections, population served, operating productivity, water production, water and sewage lines (in kilometers), water loss index and investment in programs has not been audited.

Market Information

We make statements in this annual report about our market share and other information relating to Brazil and the industry in which we operate. We have made these statements on the basis of information from third-party sources and publicly available information that we believe is reliable, such as information and reports from the Brazilian

Institute of Geography and Statistics (*Instituto Brasileiro de Geografia e Estatística*), or IBGE, and the State Data Analysis System Foundation (*Fundação Sistema Estadual de Análise de Dados*), or “SEADE”, among others. We have no reason to believe that any of this information is inaccurate in any material respect.

References to urban and total population in this annual report are estimated based on a research prepared by SEADE: “Projections for the State of São Paulo – Population and Residences until 2025” (*Projeções para o Estado de São Paulo – População e Domicílios até 2025*).

Our contracts and the Municipalities We Serve

Throughout this document, we refer to the 364 municipalities we serve and to our 367 water contracts. This difference results from the fact that we have two partial water contracts with the municipality of Mogi das Cruzes. These contracts are partial because pursuant to them we serve only two neighborhoods of this municipality and, as a result, do not include Mogi das Cruzes in the total of municipalities we serve. Most of our contracts with the municipalities we serve are concession agreements which have a term of 30 years. On August 2, 2015, we signed a water contract with the municipality of Santa Isabel, which only became effective in January 2016. Therefore, we do not include the water contract with Santa Isabel amongst the 364 municipalities we serviced in 2015.

CAUTIONARY STATEMENTS ABOUT FORWARD LOOKING STATEMENTS

This annual report includes forward looking statements, mainly in Items 3 through 5. We have based these forward looking statements largely on our current expectations and projections about future events and financial trends affecting our business. These forward looking statements are subject to risks, uncertainties and assumptions, including, among other factors:

- general economic, political, demographical and other conditions in Brazil and in other emerging market countries;
- changes in applicable laws and regulations, as well as the enactment of new laws and regulations, including those relating to environmental, tax and employment matters in Brazil;
- availability of the water supply, which may continue to be adversely affected by the current water crisis in São Paulo metropolitan region;
- the impact on our business of the water consumption reduction incentive program and other measures we took in 2014 and 2015 and any other measures we may need to take until the water levels of our reservoirs are normalized and sufficient to continuously serve the customers in the São Paulo metropolitan region;
- the impact on our business of lower water consumption practices adopted by our customers during the water crisis, which may remain in place even after the water levels of our reservoirs normalize;
- decisions by the São Paulo State Department of Water and Energy (*Departamento de Águas e Energia Elétrica do Estado de São Paulo*), or “DAEE”, and the National Water Agency (*Agência Nacional de Águas*), or “ANA”, limiting the volume of water that may be extracted from the Cantareira System, the main water system we use to serve the São Paulo metropolitan region, and the measures that we may be required to take to ensure the provision of water to our customers;
- our exposure to probable increases in the frequency of extreme weather conditions, including droughts and intensive rain and other climatic events;
- fluctuations in inflation, interest rates and exchange rates in Brazil;
- the interests of our controlling shareholder;
- our ability to collect amounts owed to us by our controlling shareholder and by municipalities;
- our ability to continue to use certain reservoirs under current terms and conditions;
- our capital expenditure program and other liquidity and capital resources requirements;
- power shortages, rationing of energy supply or significant changes in energy tariffs;
- the effects of the agreement for provision of water and sewage services in the city of São Paulo, which we executed with the State and the city of São Paulo;
- the lack of formal agreements between our company and certain municipalities to which we provide water and sewage services, including cities comprising metropolitan regions, urban conurbations, and the fact that the State and

municipal governments share competency regarding these services;

- the municipalities' ability to terminate our existing concession agreements prior to their expiration date and our ability to renew such agreements;
- our ability to provide water and sewage services in additional municipalities and to maintain the right to provide the services for which we currently have contracts;

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- the size and growth of our customer base and its consumption habits;
- our ability to comply with the requirements regarding water and sewage service levels included in our agreements with municipalities;
- our level of debt and limitations on our ability to incur additional debt;
- our ability to access financing with favorable terms in the future;
- the costs we incur in complying with environmental laws and any penalties for failure to comply with these laws;
- the outcome of our pending or future legal proceedings;
- the delay or postponement in investment in our sewage system;
- our management's expectations and estimates relating to our future financial performance;
- the regulations issued by ARSESP regarding several aspects of our business, including limitations on our ability to set and adjust our tariffs;
- the possibility to be subject to a regulatory agency, other than ARSESP; and
- other risk factors as set forth under "Item 3.D. Risk Factors".

The words "believe," "may," "estimate," "continue," "anticipate," "plan," "intend," "expect" and similar words are intended to forward looking statements. In light of these risks and uncertainties, the forward looking events and circumstances discussed in this annual report might not occur. Our actual results could differ substantially from those anticipated in our forward looking statements. Forward looking statements speak only as of the date they were made and we do not undertake any obligation to update or revise any forward looking statements, whether as a result of new information, future events or otherwise, unless required by law. Any such forward looking statements are not an indication of future performance and involve risks.

Part I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. Selected Financial Data

The following selected financial data should be read in conjunction with our financial statements (including the notes thereto), “Presentation of Financial and Other Information” and “Item 5. Operating and Financial Review and Prospects”.

The selected financial data as of December 31, 2015 and 2014 and for the years ended December 31, 2015, 2014 and 2013 have been derived from our audited financial statements, prepared in accordance with IFRS, and included in this annual report. The selected financial data as of December 31, 2013, 2012 and 2011 and for the years ended December 31, 2012 and 2011 have been derived from our audited financial statements, prepared in accordance with IFRS, which is not included in this annual report.

We have included information with respect to the dividends and/or interest attributable to shareholders’ equity paid to holders of our common shares since January 1, 2011 in *reais* and in U.S. dollars translated from *reais* at the commercial market selling rate in effect as of the payment date under the caption “Item 8.A. Financial Statements and Other Financial Information—Dividends and Dividend Policy—Payment of Dividends”.

The following tables present our selected financial data as of and for each of the periods indicated:

IFRS Summary Financial Data

	For the year ended December 31,				
2015 ⁽³⁾	2015	2014	2013 ⁽⁴⁾	2012 ⁽⁴⁾	2011 ⁽⁴⁾
US\$	R\$	R\$	R\$	R\$	R\$
<i>(in millions, except per share and per ADS⁽¹⁾ data)</i>					

Statement of operations data:

Net operating revenues	2,999.3	11,711.6	11,213.2	11,315.6	10,737.6	9,927.4
Cost of sales and services	(2,115.6)	(8,260.8)	(7,635.6)	(6,816.3)	(6,449.9)	(6,018.7)
Gross profit	883.7	3,450.8	3,577.6	4,499.3	4,287.7	3,908.7
Selling expenses	(153.2)	(598.1)	(736.6)	(637.1)	(697.3)	(619.3)
Administrative expenses	11.5	45.0	(924.4)	(729.1)	(717.4)	(683.6)
Operating profit	779.6	3,044.0	1,910.7	3,138.8	2,843.3	2,512.0
Financial income (expenses), net	(629.1)	(2,456.5)	(635.9)	(483.2)	(295.7)	(633.0)
Net income	137.3	536.3	903.0	1,923.6	1,911.9	1,380.9
Earnings per share – basic and dilute ⁽¹⁾	0.20	0.78	1.32	2.81	2.80	2.02
Earnings per ADS – basic and dilute ⁽¹⁾	0.20	0.78	1.32	2.81	2.80	2.02
Dividends and interest on shareholders' equity per share ⁽²⁾	0.05	0.19	0.32	0.67	0.66	0.43
Dividends and interest on shareholders' equity per ADS ⁽²⁾	0.05	0.19	0.32	0.67	0.66	0.43
Weighted average number of common shares outstanding ⁽²⁾	683,509,869	683,509,869	683,509,869	683,509,869	683,509,869	683,509,869

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(1) ADS - American Depositary Share.

(2) On April 22, 2013, our shareholders approved a stock split, following which each common share represented three new common shares. Therefore, per share information in the selected financial data has been revised to give effect to the stock split retrospective to all periods presented.

(3) Translated at the commercial selling rate at closing for the purchase of U.S. dollars, as reported by the Central Bank, as of December 31, 2015 of R\$3.9048 to US\$1.00.

(4) Data for 2012 and 2011 have been restated in application of IAS 19 – Employee Benefits (as revised in 2011) and IFRS 11 – Joint Arrangements, as described in our audited financial statements for the year ended December 31, 2013. With respect to IAS 19 – Employee Benefits, the principal adjustment is the change in the accounting record method of actuarial gains and losses, such that accumulated differences between actuarial estimates and actual obligations are recognized in Other Comprehensive Income when they occur.

Balance Sheet Data

	As of December 31,					
	2015 ⁽²⁾	2015	2014	2013	2012 ⁽³⁾	2011 ⁽³⁾
	US\$	R\$	R\$	R\$	R\$	R\$
	<i>(in millions, except per share and per ADS⁽¹⁾ data)</i>					
Property, plant and equipment	83.3	325.1	304.8	199.5	196.7	181.6
Intangible assets	7,302.2	28,513.6	25,979.5	23,846.2	21,967.5	20,125.7
Total assets	8,632.1	33,706.6	30,355.4	28,274.3	26,476.1	24,983.2
Current portion of long term loans and financing	390.9	1,526.3	1,207.1	640.9	1,342.6	1,629.2
Long term loans and financing	2,969.5	11,595.3	9,578.6	8,809.1	7,532.7	6,794.1
Interest on shareholders' equity payable	32.6	127.4	214.5	457.0	414.4	247.5
Total liabilities	5,119.3	19,990.0	17,051.0	15,343.5	15,219.4	14,438.3
Equity	3,512.8	13,716.6	13,304.4	12,930.8	11,256.8	10,544.9
Capital stock	2,561.0	10,000.0	10,000.0	6,203.7	6,203.7	6,203.7
Other financial information:						
Cash generated from operating activities	676.4	2,641.4	2,480.3	2,777.2	2,343.2	2,698.6
Cash used in investing activities	(629.9)	(2,459.5)	(2,757.7)	(2,281.5)	(1,996.7)	(1,883.2)
Cash provided by (used in) financing activities	(68.0)	(265.7)	218.5	(629.7)	(572.7)	(661.3)
Purchases of intangible assets and property, plant and equipment as presented in our statement of cash flow	(628.0)	(2,452.1)	(2,748.3)	(2,335.8)	(2,026.1)	(2,068.8)

(1) ADS - American Depositary Share.

(2) Translated at the commercial selling rate at closing for the purchase of U.S. dollars, as reported by the Central Bank, as of December 31, 2015 of R\$3.9048 to US\$1.00.

(3) Data for 2012 and 2011 have been restated in application of IAS 19 – Employee Benefits (as revised in 2011) and IFRS 11 – Joint Arrangements, as described in our audited financial statements for the year ended December 31, 2013. With respect to IAS 19 – Employee Benefits, the principal adjustment is the change in the accounting record method of actuarial gains and losses, such that accumulated differences between actuarial estimates and actual obligations are recognized in Other Comprehensive Income when they occur.

Operating Data

	As of and for the year ended December 31,				
	2015	2014	2013	2012	2011
Number of water connections (in thousands)	8,420	8,210	7,888	7,679	7,481
Number of sewage connections (in thousands)	6,861	6,660	6,340	6,128	5,921
Percentage of population with water connections (in percentages)	99	99	99	99	99
Percentage of population with sewer connections (in percentages)	86	85	84	83	82
Percentage of treated sewer ⁽¹⁾ (in percentages)	78	77	78	77	76
Volume of water billed during period (in millions of cubic meters)	1,914	2,069	2,149	2,094	2,045
Water Billed Loss Index during period (average) (in percentages) ⁽²⁾	16.4	21.3	24.4	25.7	25.6
Water Metered Loss Index during period (average) (in percentages) ⁽³⁾	28.5	29.8	31.2	32.1	32.0
Water loss per connection per day (average) ⁽⁴⁾	258	319	372	392	395
Number of employees	14,223	14,753	15,015	15,019	14,896

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(1) Treated sewage as a percentage of collected sewage.

(2) Includes both physical and non physical water loss. Water Billed Loss Index represents the quotient of (i) the difference between (a) the total volume of water produced plus (b) the total volume of water invoiced minus (c) the volume of water excluded from our calculation of water loss, divided by (ii) the total volume of water produced. For more information, see “Item 4.B. Business Overview—Description of Our Activities—Water Operations—Water Loss”.

We exclude the following from our calculation of water loss: (i) water discharged for periodic maintenance of water transmission lines and water storage tanks; (ii) water supplied for municipal uses such as firefighting; (iii) water we consume in our facilities; and (iv) estimated water loss related to the supply of water to shantytowns (*favelas*).

(3) Includes both physical and non physical water loss. The Water Metered Loss Index represents the quotient of (i) the difference between (a) the total volume of water produced minus (b) the total volume of water measured minus (c) the volume of water that we exclude from our calculation of water loss, divided by (ii) the total volume of water produced. For more information, see “Item 4.B. Business Overview—Description of Our Activities—Water Operations—Water Loss”.

We exclude the following from our calculation of water loss: (i) water discharged for periodic maintenance of water transmission lines and water storage tanks; (ii) water supplied for municipal uses such as firefighting; (iii) water we consume in our facilities; and (iv) estimated water loss related to the supply of water to shantytowns (*favelas*).

(4) Measured in liters/connection per day, this amount is calculated by dividing (i) the average annual water loss by (ii) the average number of active water connections multiplied by the number of days of the year. This calculation method is based on worldwide market practice within the sector. See “Item 4.B. Business Overview—Description of Our Activities—Water Operations—Water Loss”.

We exclude the following from our calculation of water loss: (i) water discharged for periodic maintenance of water transmission lines and water storage tanks; (ii) water supplied for municipal uses such as firefighting; (iii) water we consume in our facilities; and (iv) estimated water loss related to the supply of water to shantytowns (*favelas*).

Exchange Rates

In the past, the Brazilian National Monetary Council (*Conselho Monetário Nacional*), or the “CMN”, has introduced changes to the Brazilian foreign exchange regime, such as unifying the Commercial and Floating Markets and easing the rules governing the ability of Brazilian residents to acquire foreign currency, among others. On March 24, 2010, the CMN and the Central Bank approved Resolution No. 3,844/2010, as amended, which led to a series of measures to consolidate and simplify Brazilian foreign exchange market regulations.

The Brazilian foreign exchange system allows any person or legal entity to purchase or sell foreign currency and make international transfers of *reais*, regardless of the amount, subject to certain regulatory procedures.

The Brazilian currency has experienced frequent and substantial variations in relation to the U.S. dollar and other foreign currencies in recent decades. Between 2003 and mid 2008, the *real* appreciated significantly against the U.S. dollar with the exchange rate reaching R\$1.634 in August 2008. Primarily as a result of the global financial crisis, the *real* depreciated 32.0% against the U.S. dollar during 2008 and closed the year at R\$2.337 per US\$1.00.

The *real* strengthened again by 25.5% in 2009 and 4.3% in 2010, but depreciated against the U.S. dollar by 12.6% in 2011, 8.94% in 2012, 14.63% in 2013, 13.39% in 2014 and 47.01% in 2015. On December 31, 2015, 2014, and 2013, the *real*/U.S. dollar exchange rate was R\$3.9048, R\$2.6562 and R\$2.3426 per US\$1.00, respectively.

Since 1999, following Brazil's implementation of a floating rate regime, the Central Bank has not directly intervened in the exchange market. However, the Central Bank, using financial instruments at its disposal, may buy and sell foreign currency in the market in order to influence the exchange rate and decrease volatility with respect to the Brazilian *real*. We cannot predict whether the Central Bank or the Brazilian government will continue to let the *real* float freely or will intervene in the exchange rate through a currency band system or other procedure. The *real* may fluctuate against the U.S. dollar substantially in the future. For further information on this risk, see "Item 3.D. Risk Factors—Risks Relating to Brazil—Exchange rate instability may adversely affect us and the market price of our common shares or ADSs".

Exchange rate fluctuations will affect the U.S. dollar equivalent of the *real* price of our common shares on the São Paulo Stock Exchange (*BM&FBOVESPA S.A. Bolsa de Valores, Mercadorias e Futuros*), or the “BM&FBOVESPA”, as well as the U.S. dollar equivalent of any distributions we make in *reais* with respect to our common shares.

The following tables set forth the selling rate, expressed in *reais* per U.S. dollar (R\$/US\$), for the periods indicated:

Year ended December 31,	Year end	R\$ per US\$1.00		
		Average⁽¹⁾	High	Low
2011	1.8758	1.6746	1.9016	1.5345
2012	2.0435	1.9550	2.1121	1.7024
2013	2.3426	2.1605	2.4457	1.9528
2014	2.6562	2.3547	2.7403	2.1974
2015	3.9048	3.3387	4.1949	2.5754

Month ended	Period end	R\$ per US\$1.00		
		Average	High	Low
October 31, 2015	3.8589	3.8801	4.0010	3.7386
November 30, 2015	3.8506	3.7765	3.8506	3.7010
December 31, 2015	3.9048	3.8711	3.9831	3.7476
January 31, 2016	4.0428	4.0524	4.1558	3.9863
February 28, 2016	3.9578	3.9734	4.0492	3.8653
March 31, 2016	3.5589	3.7039	3.9913	3.5589
April 30, 2016	3.4508	3.5658	3.6921	3.4508

Source: Central Bank

(1) Average of the exchange rates on the last day of each month.

The following tables set forth the selling rate, expressed in *reais* per Japanese Yen (R\$/¥1.00):

Year ended December 31,	Year end	R\$ per ¥1.00		
		Average⁽¹⁾	High	Low
2011	0.0243	0.0211	0.0249	0.0186
2012	0.0237	0.0245	0.0263	0.0211
2013	0.0223	0.0221	0.0248	0.0196
2014	0.0222	0.0222	0.0239	0.0212
2015	0.0324	0.0276	0.0351	0.0219

Month ended	Period end	R\$ per ¥1.00		
		Average	High	Low
October 31, 2015	0.0320	0.0323	0.0335	0.0311
November 30, 2015	0.0313	0.0308	0.0315	0.0301
December 31, 2015	0.0324	0.0318	0.0329	0.0304
January 31, 2016	0.0333	0.0343	0.0355	0.0333

February 28, 2016	0.0348	0.0347	0.0359	0.0331
March 31, 2016	0.0317	0.0328	0.0351	0.0317
April 30, 2016	0.0323	0.0326	0.0342	0.0317

Source: Central Bank

(1) Average of the exchange rates on the last day of each period.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Risks Relating to Brazil

The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. This influence, as well as Brazilian political and economic conditions, could adversely affect us and the market price of our common shares and ADSs.

The Brazilian government frequently intervenes in the Brazilian economy and occasionally makes significant changes in policy and regulations. The Brazilian government's actions to control inflation and other policies and regulations have often involved, among other measures, changes in interest rates, tax policies, price and tariff controls, currency devaluation or appreciation, capital controls and limits on imports. Our business, financial condition and results of operations, as well as the market price of our common shares or ADSs, may be adversely affected by changes in public policy at federal, state and municipal levels with respect to public tariffs and exchange controls, as well as other factors, such as:

- the regulatory environment related to our business operations and agreements;
- interest rates;
- exchange rates and exchange controls and restrictions on remittances abroad;
- currency fluctuations;
- inflation;
- liquidity of the Brazilian capital and lending markets;
- tax and regulatory policies and laws;
- economic and social instability; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

For example, the Brazilian government may change its tax policy, such as by changing tax rates or imposing temporary taxes. If overall taxes are increased, we may be unable to immediately recover the difference from our consumers, which may have an adverse effect on our financial condition and results of operations.

Uncertainty over whether the Brazilian government will change policies or regulations affecting these or other factors may contribute to economic uncertainty in Brazil and to heightened volatility in Brazilian securities markets and securities issued abroad by Brazilian issuers. On September 9, 2015, Brazil was downgraded below investment grade by Standard & Poor's Financial Services LLC, and received a further downgrade by the same rating agency on February 17, 2016. In addition, on December 16, 2015, Brazil was downgraded below investment grade by Fitch Ratings Inc. and in February 24, 2016 by Moody's Investors Service, Inc.. We cannot assure you that the Brazilian government will continue with its current economic policies, or that these and other developments in Brazil's economy and government policies will not, directly or indirectly, adversely affect our business and results of operations.

Political conditions may have an adverse impact on the Brazilian economy and on our business.

Current political conditions in Brazil may affect the confidence of investors and the public in general as well as the development of the economy. Uncertainty with regard to matters such as the presidential administration's future policies and appointments to influential governmental positions and ongoing investigations into allegations of corruption in state-controlled enterprises may also affect the confidence of investors and the general public. It may also have an adverse impact on the Brazilian economy, our business, financial condition, results of operations and the market price of our common shares and ADSs.

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Currently, Brazilian markets are experiencing heightened volatility due to the uncertainties derived from the ongoing *Lava Jato* investigation, being conducted by the Office of the Brazilian Federal Prosecutor, and its impact on the Brazilian economy and political environment. Certain of these companies are also facing investigations by the Brazilian Securities Commission (*Comissão de Valores Mobiliários*), or CVM, and the U.S. Securities and Exchange Commission, or the SEC. Members of the Brazilian federal government and of the legislative branch, as well as senior officers of large state-owned companies have faced allegations of political corruption, since they have allegedly accepted bribes by means of kickbacks on contracts granted by the government to several infrastructure, oil and gas and construction companies. The profits of these kickbacks allegedly financed the political campaigns of political parties of the current federal government coalition that were unaccounted for or not publicly disclosed, as well as served to personal enrichment of the recipients of the bribery scheme.

The potential outcome of these investigations is uncertain, but they have already an adverse impact on the image and reputation of the implicated companies, and on the general market perception of the Brazilian economy. We cannot predict whether such allegations will lead to further political and economic instability or whether new allegations against government officials will arise in the future. In addition, we cannot predict the outcome of any such allegations nor their effect on the Brazilian economy.

The development of such unethical conduct cases could adversely affect our business, financial condition and results of operations.

Inflation and the Brazilian government's measures to combat inflation may contribute to economic uncertainty in Brazil, adversely affecting us and the market price of our common shares or ADSs.

Inflation and the Brazilian government's measures to combat it have had and may in the future have significant effects on the Brazilian economy and our business. Tight monetary policies with high interest rates may restrict Brazil's growth, the availability of credit and our cost of funding. Conversely, other Brazilian governmental actions, including lowering interest rates, intervention in the foreign exchange market and actions to adjust or fix the value of the *real*, may trigger increases in inflation. The Special Clearing and Settlement System (*Sistema Especial de Liquidação e Custódia*), or "SELIC", the official overnight interest rate in Brazil, equaled 14.15%, 11.65% and 9.90% at the end of 2015, 2014 and 2013, respectively, in line with the target rate set by the Brazilian Committee on Monetary Policy (*Comitê de Política Monetária*).

The Brazilian annual inflation rates, as measured by the Amplified Consumer Price Index (*Índice Nacional de Preços ao Consumidor Amplo*), or "IPCA", the Brazilian annual inflation rates were 10,67%, 6,41% and 5,91%, during 2015, 2014 and 2013, respectively. If Brazil experiences increases in inflation, our costs and expenses may rise, we may be unable to increase our tariffs at the same rate to counter the effects of inflation, and our overall financial performance may be adversely affected. In addition, a substantial increase in inflation may weaken investors' confidence in Brazil, causing a decrease in the market price of our common shares or ADSs.

The devaluation of the real to foreign currencies may adversely affect us and the market price of our common shares or ADSs.

The Brazilian currency experienced frequent and substantial devaluations in relation to the U.S. dollar and other foreign currencies during the decades leading up to the mid-1990s. Throughout this period, the Brazilian government implemented various economic plans and exchange rate policies, including sudden devaluations, periodic mini devaluations (during which the frequency of adjustments ranged from daily to monthly), floating exchange rate systems, exchange controls and dual exchange rate markets. From time to time since that period, there have continued

to be significant fluctuations in the exchange rate between the Brazilian *real* and the U.S. dollar and other currencies. For example, the *real* appreciated 13.8%, 9.5% and 20.7% against the U.S. dollar in 2005, 2006 and 2007, respectively. In 2008, primarily as a result of the global financial crisis, the *real* depreciated 32.0% against the U.S. dollar and closed the year at R\$2.337 per US\$1.00. The *real* strengthened again by 25.5% in 2009 and 4.3% in 2010, but depreciated against the U.S. dollar by 12.6% in 2011, 8.94% in 2012, 14.63% in 2013, 13.39% in 2014 and 47.01% in 2015. On December 31, 2015, 2014 and 2013, the *real*/U.S. dollar exchange rate was R\$3.9048, R\$2.6562 and R\$2.343 per US\$1.00, respectively. There can be no assurance that the *real* will not depreciate further against the U.S. dollar. As of April 30, 2016, the commercial selling rate as reported by the Central Bank was R\$3.4508 per US\$1.00.

Depreciation of the *real* against the U.S. dollar could create inflationary pressures in Brazil and cause increases in interest rates, which could negatively affect the growth of the Brazilian economy as a whole and harm our financial condition and results of operations, curtail our access to financial markets and prompt government intervention, including recessionary governmental policies. Depreciation of the *real* against the U.S. dollar could also lead to decreased consumer spending, deflationary pressures and reduced economic growth.

In the event of a significant devaluation of the *real* in relation to the U.S. dollar or other currencies, our ability to meet our foreign currency denominated obligations could be adversely affected because our tariff revenue and other sources of income are denominated solely in *reais*. In addition, because we have debt denominated in foreign currencies, any significant devaluation of the *real* will increase our financial expenses as a result of foreign exchange losses that we must record. We had a total foreign currency denominated debt of R\$6,617.8 million as of December 31, 2015 and we anticipate that we may incur additional amounts of foreign currency denominated debt in the future. In 2015, our results of operations were negatively affected by the 47.0% depreciation of the *real* against the U.S. dollar, and a depreciation of the *real* against the yen by 46.0% which led to a R\$1,992.0 million negative impact on our foreign exchange result, net. We do not currently have any derivative instruments in place to protect us against a devaluation of the *real* in relation to any foreign currency. A devaluation of the *real* may adversely affect us and the market price of our common shares or ADSs. For more information, see Note 5(a) of our 2015 financial statements.

For further information on exchange rate instability impacts, see “Item 5.B. Liquidity and Capital Resources—Capital Sources—Indebtedness Financing—Financial Covenants”.

Developments and the perception of risk in other countries, especially in the United States and in emerging market countries, may adversely affect the market price of Brazilian securities, including our common shares and ADSs.

The market price of securities of Brazilian companies is affected to varying degrees by economic and market conditions in other countries, including the United States and other Latin American and emerging market countries. Although economic conditions in these countries may differ significantly from economic conditions in Brazil, investors’ reactions to developments in these other countries may have an adverse effect on the market price of securities of Brazilian issuers. Crises in other emerging market countries or economic policies of other countries may diminish investor interest in securities of Brazilian issuers, including ours. This could adversely affect the market price of our common shares or ADSs, and could also make it more difficult for us to access the capital markets and finance our operations in the future, on acceptable terms or at all.

The global financial crisis has caused significant consequences, including in Brazil, such as stock and credit market volatility, unavailability of credit, higher interest rates, a general slowdown of the world economy, volatile exchange rates, and inflationary pressure, among others, which have and may continue to, directly or indirectly, materially and adversely affect us and the price of securities issued by Brazilian companies, including our common shares and ADSs.

Risks Relating to Our Control by the State of São Paulo

We are controlled by the State of São Paulo, whose interests may differ from the interests of non-controlling, including holders of ADSs.

As it owns the majority of our common shares, the State is able to determine our operating policies and strategy, control the election of a majority of the members of our board of directors and appoint our senior management. As of April 30, 2016, the State owned 50.3% of our outstanding common shares. Both through its control of our board of directors as well as by enacting State decrees, the State has in the past directed our company to engage in business activities and make expenditures that promoted political, economic or social goals, but that did not necessarily

enhance our business and results of operations. The State may direct our company to act in this manner again in the future. These decisions by the State may not be in the interests of our non-controlling, including holders of ADSs. See “Item 5.A. Operating and Financial Review and Prospects—Certain Transactions with Controlling Shareholder”.

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Following the elections for State governor in 2014, the re-elected governor appointed Mr. Jerson Kelman as our Chief Executive Officer in January 2015, and Mr. Benedito Pinto Ferreira Braga Junior, the Secretary of State for the State Secretariat for Sanitation and Water Resources (*Secretaria de Saneamento e Recursos Hídricos do Estado de São Paulo*), was elected our Chairman for the current board of directors' term of two years, ending in April 2016. Mr. Benedito Pinto Ferreira Braga Junior's term was renewed in our annual general shareholder's meeting held on April 29, 2016 for another two years, ending in April 2018. Future changes in policy by State government may cause changes in all or some of the members of our management, which may have a material adverse effect on our business and results of operations.

The State and some State entities owe us substantial unpaid debts. We cannot assure you as to when or whether the State will pay us.

Historically, the State and some State entities have delayed payment of substantial amounts owed to us related to water and sewage services. As of December 31, 2015, the State owed us R\$66.3 million for water and sewage services. Additionally, the State also owes us substantial amounts related to reimbursements of State mandated special retirement and pension payments that we make to some of our former employees for which the State is required to reimburse us.

With respect to payment of pensions on behalf of the State, we had a contested credit amount of R\$855.1 million as of December 31, 2015. We do not record this contested amount as a reimbursement credit for actuarial liability due to the uncertainty of payment by the State. In addition, as of December 31, 2015, we had a provision for an actuarial liability in the amount of R\$2,166.9 million with respect to future supplemental pension payments for which the State does not accept responsibility. On March 18, 2015, we, the State and DAEE, with the intervention of the Department of Sanitation and Water Resources, executed a term of agreement, in the amount of R\$1,012.3 million, of which R\$696.3 million refers to the principal amount and R\$316.0 million refers to the monetary adjustment of the principal through February 2015. For a detailed discussion of this agreement, see "Item 7.B. Related Party Transactions—Agreements with the State of São Paulo" and Note 10 of our 2015 financial statements.

We have entered into agreements with the State to settle the overdue amounts that relate to water and sewage services. For a detailed discussion of these agreements, see "Item 7.B. Related Party Transactions, Agreements with the State of São Paulo" and Note 10 of our 2015 financial statements.

Although the State has complied with agreements negotiated with us in past years, we cannot assure you when or if the State will pay the contested credit amount, which is still under discussion, and the remaining overdue amounts it owes us. The amounts owed to us by the State for water and sewage services and reimbursements for pensions paid may increase in the future.

In addition, certain municipalities and other government entities also owe us payments. See "Risks Relating to Our Business—We may face difficulties in collecting overdue amounts owed to us by municipalities to which we provide water on a wholesale basis and municipal government entities".

EMAE, a State-controlled company that has a concession to produce energy in the Guarapiranga and Billings reservoirs is seeking damages from us for the water we draw from these reservoirs.

Empresa Metropolitana de Águas e Energia S.A., or EMAE, a company also controlled by the State of São Paulo that has a concession to produce hydroelectric energy using water in the Guarapiranga and Billings reservoirs, is seeking compensation from us for the water we draw from these reservoirs. EMAE has commenced various court and arbitration proceedings, alleging that our water use reduces their ability to generate and sell electricity. As stated in an Announcement to the Market that we issued on April 10, 2014, we are negotiating with EMAE regarding a potential

settlement of this water use dispute, although no agreement has yet been finalized.

In addition, the State of São Paulo, which is controlling shareholder of both EMAE and our company, may take action to resolve the dispute in a way that has an adverse effect on our business. On April 11, 2016 we were named in legal proceedings commenced by minority shareholders of EMAE against the State of São Paulo. The plaintiffs in these proceedings are seeking an order to require the State to stop us from drawing water from the reservoirs without paying compensation to EMAE, and to allow EMAE to pump water from the reservoirs for its hydroelectric facility. The plaintiffs in these proceedings allege that the State, in its capacity as controlling shareholder of EMAE, has acted unduly to EMAE's detriment and in favor of our company.

If we were no longer able to draw water from these reservoirs, we would have to transport water from locations farther away, which would increase our water transportation costs and may affect our ability to provide adequate service in the region. In addition, if we are required to pay compensation to EMAE, our cash position and overall liquidity may be adversely affected.

We may be required to pay substantial charges for the use of reservoirs that are not our property.

We use the Billings and Guarapiranga reservoirs in order to provide water services. We are entitled to withdraw water from these reservoirs under a grant from DAEE. We are not currently charged for the use of these reservoirs and are uncertain as to whether we will continue to be able to use the reservoirs without paying charges or what the likely fee scale would be if one were imposed.

We may also be required to pay additional maintenance and operational costs to utilize these reservoirs. If we were required to pay substantial charges or additional maintenance or operational costs for our use of these reservoirs, we could be materially and adversely affected.

Risks Relating to Our Business

The measures we took to mitigate the effects of the drought resulted in a significant decrease in the volume of water billed and revenues from services we provide, which had a material adverse effect on our company and could continue to do so if the drought escalates in severity.

We experience decreases in our water availability from time to time due to droughts. The southeastern region of Brazil, particularly the southern region of Minas Gerais State and the Piracicaba, Capivari and Jundiá river basin, or “PCJ River Basin” (from which we extract most of the water used in the Cantareira System), and the northern area of the São Paulo metropolitan region have experienced below average rainfall since 2012. In the October 2013 – March 2014 rainy season, rain levels and water inflow into the reservoirs reached the lowest levels in 84 years of recorded rainfall in the region, a scenario that continued in the October 2014 – March 2015 rainy season. During the October 2015 – March 2016 rainy season, the level of rainfall in the region returned to the normal levels expected for the period. Improved rainfall in the rainy season that began in October 2015, the collaborative efforts between us and the population we serve and emergency construction conducted by us throughout 2014 and 2015 in order to reduce the impact of the water crisis, resulted in a partial restoration of the water levels of the Cantareira system.

The depletion of water storage is worst in the Cantareira System, the largest system of the São Paulo metropolitan region. As a result of the drought and low water volume in the Cantareira System, DAEE and ANA, since March 2014, have continuously regulated the volume of water we are permitted to extract from this system. The DAEE and ANA determine this amount based on levels of rainfall, water inflow, level of water in our reservoirs and our requests to extract water based on this information, and inform us of the amount we are permitted to extract via monthly notices. As of February 2016, as a result of the return of average rainfall levels to the region, we received authorization to extract 23 cubic meters per second, or m³/s, from the Cantareira System, an increase compared to the 13.5 m³/s we were authorized to extract for the majority of 2015. This figure remains significantly below the water level we were allowed to extract in the period prior to February 2014, when we were allowed to extract up to a total of 33 m³/s.

In order to balance supply and demand despite the restricted water availability, we have adopted and will continue adopting a series of measures, including: (i) using treated water from other production systems to serve consumers originally supplied by the Cantareira system; (ii) to offer discounts (bonus) to consumers that use below average amounts of water, compared to average consumption; (iii) reducing pressure in the water distribution lines in order to decrease leakage; (iv) adjusting the volume of treated water sold to municipalities that operate their own distribution network; and (v) using pumps in order to extract water located below the intakes of the Cantareira system, from the so-called “technical reserve”, which has never before been used to serve the population. See “Item 4.B. Business Overview—The Current Water Crisis”.

Even with the return of normal rainfall levels throughout the October 2015 – March 2016 rainy season, the need to recover the volume of water stored in the reservoirs of the Cantareira system will persist throughout the next rainy season. The Cantareira system's maximum storage capacity, including the technical reserve, is 1,269.5 million m³. Excluding the technical reserve, which is 287,5 million m³, the Cantareira system's maximum storage capacity is 982.0 million m³. The volume of water in the Cantareira system recovered throughout the October 2015 – March 2016 rainy season and was 641.9 million m³ as of March 2016, which represents 50.6% of its maximum storage capacity including the technical reserve.

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We cannot guarantee that we shall be authorized to extract the same volume of water from this system that we extracted prior to the drought to serve the needs of the population we service. In December 2015, 5.3 million inhabitants were serviced by this system, compared to 8.9 million in February 2014. For more information about the water crisis, see “Item 4.B. Business Overview—The Current Water Crisis”.

The drought has prompted a continuous reduction in the volume of water billed and thus a reduction in revenue. In 2014, our water volume billed decreased 3.1% and our gross operational revenue fell by 6.7% compared to 2013. In 2015, our water volume billed decreased 8.0% and our gross operational revenue increased slightly by 0.5% compared to 2014. Therefore, there was and may continue to be a negative impact on our financial ratios linked to revenue, such as the debt to EBITDA ratio. We are required to maintain certain financial ratios at specified levels pursuant to restrictions and covenants of our existing debt agreements and failure to maintain these ratios may lead to a default under such agreements. Breach of any such covenant may result in a default under certain of our debt agreements and, due to customary cross-default provisions, could permit some of our creditors to accelerate our indebtedness unless we are able to renegotiate the terms of these agreements or receive waivers from the affected creditors. If such events were to occur, our financial condition would be adversely affected. See “Item 5.B. Liquidity and Capital Resources—Indebtedness Financing—Financial Covenants”.

We are exposed to risks associated with the provision of water and sewage services.

Our industry is affected by the following risks relating to the provision of water and sewage services:

- We depend on a water right issued by DAEE – ANA in order to extract water from the Cantareira System. The water right was renewed in 2004 and would have expired in August 2014. However, due to current climate conditions, particularly the severe drought, the water right was extended until October 31, 2015 and later extended again until May 2017. The extraction of water throughout 2014 and 2015 was executed according to the specific rules established to combat the water crisis. The terms of this water right will define the volume of water that we will be authorized to extract from the Cantareira System to provide to the São Paulo metropolitan region. The drought that occurred in 2014 and for most of 2015 may influence the decision of ANA and DAEE regarding the volume of water that we will be authorized to extract pursuant to the renewal of the water right in 2017. The volume of water that we have been authorized to extract from the Cantareira System (which includes the PCJ River Basin and Juquerí River Basin) has been communicated to us via monthly notices according to the behavior of rainfall, water inflow, level of water in our reservoirs and our requests to extract water based on this information.
- We are dependent upon energy supplies to conduct our business. Any shortages or rationing of energy may prevent us from providing water and sewage services and may also cause material damage to our water and sewage systems when we resume operations. In 2016, there is no forecast of any shortages or rationing of energy and we estimate an increase of about 15% to 20% in energy expenses compared to 2015. In March 2015, we filed with ARSESP an extraordinary revision request based on the decline in the volume of water due to the water crisis and based on the unexpected increase in electricity tariffs. Our request was approved in May 2015. However, we may not be able to pass on any significant increases in energy tariffs to our customers in the future. See “Item 4.B. Business Overview—Energy Consumption”.
- We are exposed to various weather-related risks, since our financial performance is closely linked to climate patterns. The possible increase in the frequency of extreme weather conditions in the future may adversely affect the water available for abstraction, treatment, and supply. Droughts could adversely affect the water supply systems, resulting in a decrease in the volume of water distributed and billed as well as in the revenue derived from water supply services. An increase in heavy rainfall could impact the regular operation of water sources, including abstraction of water from our dams due to increased soil erosion, silting, and runoff of pollutants that affect the aquatic ecosystems. See “Item 4.B. Business Overview—Environmental Matters—Climate Change Regulation”.

- The increasing degradation of watershed areas may affect the quantity and quality of water available to meet demand from our customers. See “Item 4.A. History and Development of the Company—Capital Expenditure Program” and “—Main Projects of Our Capital Expenditure Program”.
- In addition to the risks discussed under “—The terms of our agreement to provide water and sewage services in the city of São Paulo could have a material adverse effect on us,” we may not be able to increase our tariffs on a timely basis, or at all, in order to pass on increases in inflation or operating expenses, including taxes, to our customers. These constraints may have an adverse effect on our ability to fund our capital expenditure program and financing activities and to meet our debt service requirements. See “Item 5.A. Operating and Financial Review and Prospects—Factors Affecting Our Results of Operations—Effects of Tariff Increases”.
- The state and federal government agencies that manage water resources could impose substantial charges for the abstraction of water from bodies of water and the discharge of sewage. We may not be able to pass these charges on to our customers. See “Item 4.B. Business Overview—Government Regulation—Water Usage”.
- Our water pipes are susceptible to the degradation caused by factors such as age, intense traffic, population density and industrial development, which may provoke accidents in the networks and affect the regular provision of our services, impacting society and the environment. See "Item 4.B Business Overview-Description of Our Activities-Water Distribution" and "Item 4.B Business Overview-Descriptions of Our Activities-Sewage Operations-Sewage System".

Any of the above may have a material adverse effect on us.

Current regulatory uncertainty, especially with regard to implementation and interpretation of the Brazilian Basic Sanitation Law, may have an adverse effect on our business.

Our operations in the state of São Paulo occur both in locations where the planning, monitoring and tariff regulation of basic sanitation services are responsibilities of the municipalities and in locations where such responsibilities are shared between the State and municipalities. The Basic Sanitation Law No. 11,445/2007 went into effect in early 2007, and although Federal Decree No. 7,217/2010 (as modified by Federal Decree No. 8,211/2014) implemented a series of new principles under the Basic Sanitation Law in 2010, the full implementation of a number of its provisions remains subject to regulations that the federal government has not yet published. Moreover, the Basic Sanitation Law requires that the federal government, states and municipalities establish independent regulators who monitor basic sanitation services and regulate tariffs. In compliance with this law, the state of São Paulo established ARSESP in 2007. Currently, our regional and local operations, including tariff regulation, are monitored and regulated by ARSESP, and the remainder of our operations is in the process of negotiating new contractual bases. Regulatory agencies determine tariff increases for our water and sewage services, on which our results of operations and financial condition are highly dependent. As a result, we cannot anticipate all the effects that the Basic Sanitation Law and the decree will have on our business and operations, if any.

In 2009, ARSESP enacted rules regarding the following: (i) general terms and conditions for water and sewage services; (ii) procedures for communication regarding any failure in our services; (iii) penalties for deficiencies in the provision of basic sanitation services; and (iv) procedures for confidential treatment of our customers’ private information. The implementation of these and other more recent rules will particularly impact our commercial and operations processes, and may adversely affect us in ways we cannot currently predict. Implementation of these rules started in 2011 and is expected to continue for the next few years. For more information, see “Item 4.B. Business Overview—Government Regulations Applicable to Our Contracts—Rules Enacted by ARSESP”.

In 2011, ARSESP altered the standard contract that we are required to use in our relationships with retail customers. This alteration requires that invoices be sent to the user of the service rather than the owner of the property. Since 2011, we have implemented several measures and instituted new rules for the update of our client registry. Currently, more than 90% of our water and sewage connections are billed to the user of our services, as foreseen under current regulations. We estimate that this change will affect ongoing legal disputes, particularly those regarding collection procedures, as well as business discussions in general. However, since this change is still being implemented, we are not currently able to predict its impact on our business.

In August 2012, ARSESP issued Resolution No. 346/2012, which established that users should be compensated for any interruptions in water supply. Implementation of this regulation has been suspended pending further technical discussions. In 2013, ARSESP held public consultations that resumed technical discussions on the subject, but the new resolution that will replace Resolution No. 346/2012 has not yet been published.

The Basic Sanitation Law No. 11,445/2007 also allows municipalities to create their own regulatory agencies rather than being regulated by ARSESP. As a result, a number of municipalities have created their own regulatory agencies. If other municipalities create new agencies or retain regulatory powers, we may be subject to their regulation and to any limitations on our services that such agencies may set. We are involved in legal proceedings that dispute the authority of these new agencies to regulate and monitor our local contracts and our operations in metropolitan regions and urban clusters instituted by the State. We cannot foresee any changes that any such new agencies may implement regarding our business. If any such changes are unfavorable, they could materially and adversely affect us.

The State of São Paulo, pursuant to Article 25, Section 3 of the Brazilian Constitution, enacted the State Complementary Law, or “LCE”, creating the metropolitan regions of São Paulo (LCE No. 94/1974), Baixada Santista (LCE No. 815/1996), Campinas (LCE No. 870/2000), Vale do Paraíba and Litoral Norte (LCE No. 1,166/2012), Sorocaba (LCE No. 1,241/2014), and the urban clusters of Jundiaí (LCE No. 1,146/2011) and Piracicaba (LCE No. 1,178/2012). These areas incorporate independent municipalities that modify the exercise of their constitutional competencies, including those related to basic sanitation services, and increase the number of judicial disputes concerning the regulation and oversight of services in areas currently served by us and regulated by ARSESP. We cannot anticipate the result of these judicial disputes and the adverse material effects that may result from them, especially if the rules of regulation and monitoring of services issued by municipal agencies come to coexist with those already published by ARSESP and implemented into our operational and corporate processes since 2011.

For more information on ARSESP regulations, see “Item 4.B. Business Overview—Tariffs—Government Regulations Applicable to Our Contracts—Rules Enacted by ARSESP—Consumer Relations in the State of São Paulo”.

New joint entities have been, and may continue to be, set up to oversee basic sanitation services in metropolitan regions, including the São Paulo metropolitan region. We cannot predict how the shared management of these operations will be carried out in the São Paulo metropolitan region and other metropolitan regions we operate or what effect this may have on our business, financial condition or results of operations.

There are some pending cases before the Brazilian Supreme Court regarding whether the right to execute concession and program agreements in metropolitan regions belongs to the State or the municipal government. On February 28, 2013, the Brazilian Supreme Court decided a then pending case on this matter related to the state of Rio de Janeiro. A majority of the court held that the state of Rio de Janeiro must set up new entities to oversee the planning, regulation and auditing of basic sanitation services in the metropolitan region with the non-partisan participation of all the municipalities located in the metropolitan region.

On March 6, 2013, the court ruled that this holding would come into effect in the state of Rio de Janeiro after a remaining appeal of its holding is decided. The court’s holding represents a new paradigm in the management and provision of services. The Supreme Court has yet to clarify the effects and extension of its decision. The São Paulo metropolitan region (including the municipalities to which we provide water on a wholesale basis), to which a decision on such pending or new cases may apply, accounted for 67.3% of our gross operating revenue from services in 2015 (excluding revenues relating to the construction of concession infrastructure). In January 2015, the Federal Government issued the Metropolitan Bylaws (Law No. 13,089/2015) which establishes general guidelines for the planning, management and performance of public interest projects in metropolitan regions and in urban clusters instituted by the states; the general planning standards for integrated urban development and other international governance instruments; and the criteria to receive federal loans for initiatives related to international governance in the field of urban development.

We cannot predict how the shared management of these operations will be carried out in the São Paulo metropolitan region and other municipalities in which we operate or what effect the shared management may have on our business, financial condition or results of operation.

For more information on services in metropolitan regions, see “Item 4.B. Business Overview - Government Regulations Applicable to Our Contracts – Agreements with Municipalities and Metropolitan Regions”.

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The terms of our agreement to provide water and sewage services in the city of São Paulo could have a material adverse effect on us.

The provision of water and sewage services in the city of São Paulo accounted for 48.2% of our gross operating revenues (excluding revenues relating to the construction of concession infrastructure) in the year ended December 31, 2015.

On June 23, 2010, the State and the city of São Paulo executed an agreement in the form of a *convênio* with our and ARSESP's consent, under which they agreed to manage the planning and investment for the basic sanitation system of the city of São Paulo on a joint basis. In application of the *convênio*, we executed a separate contract dated June 23, 2010 with the State and the city of São Paulo, to regulate the provision of these services for the following 30 years. Among other principal terms of this separate agreement, we must transfer 7.5% of the gross revenues we derive under the *convênio* and subtract (i) COFINS and PASEP taxes and (ii) unpaid bills of publicly owned properties in the city of São Paulo, to the Municipal Fund for Environmental Sanitation and Infrastructure (*Fundo Municipal de Saneamento Ambiental e Infraestrutura*), established by Municipal Law No. 14,934/2009. See "Item 7.B. Related Party Transactions—Agreement with the State and the city of São Paulo" for further discussion of the principal terms of the *convênio* and principal terms of the separate contract we executed in application of the *convênio*.

Because we were not previously required to transfer 7.5% of the gross revenues obtained from providing sanitation services in the municipality of São Paulo to the São Paulo Municipal Fund for Environmental Sanitation and Infrastructure as established under the *convênio*, our existing tariff and adjustment formulas do not account for this requirement. Nonetheless, ARSESP is required to ensure that the tariffs will adequately compensate us for the services we provide, which includes the pass-through to tariffs.

In March 2013, ARSESP issued Resolution No. 407/2013 authorizing us to pass through to the service bill the 7.5% transfer to the São Paulo Municipal Sanitation and Infrastructure Fund as a legal charge, as defined by municipal legislation. However, pursuant to the Program Contracts and the Sewage and Water Supply Service Contracts, this charge must be considered in the tariff revision.

In April 2013, ARSESP issued Resolution No. 413/2013, which suspended Resolution No. 407/2013 until the tariff revision process is concluded, thereby postponing our authorization to pass the charge through to consumers on the service bill. The postponement of Resolution No. 407/2013 was due to a request from the São Paulo State Government to analyze, among other things, methods of reducing the impact on consumers.

In April 2014, ARSESP issued Resolution No. 484/2014, (further ratified by Resolution No. 520, issued November 2014), which establishes the conclusion of the tariff revision. However, the State and the city of São Paulo requested to maintain the suspension of ARSESP Resolution No. 407/2013, postponing our authorization to pass the charge through to consumers on the service bill, until the revision of our contract with the State and city of São Paulo is concluded.

In May 2014, ARSESP issued Resolution No. 488/2014, which maintained the suspension of Resolution ARSESP No. 407/2013 until the results are obtained in the revision of the contract signed between us, the city and the State of São Paulo, thereby delaying the authorization to pass the charge through to consumers on the service bill. We cannot know when we will be able to pass the 7.5% charge on to consumers through the service bill.

As of December 31, 2015, we have transferred approximately R\$1.8 billion to the São Paulo Municipal Fund for Environmental Sanitation and Infrastructure since 2010. We cannot assure you when and how we will recover this amount.

We cannot assure you that this charge will eventually be passed through to customers or that the continued delay in passing this charge through to customers will not further affect our financial condition. For additional information on ARSESP regulations, see “Item 4.B. Business Overview—Tariffs” and “Item 4.B. Business Overview—Government Regulations Applicable to Our Contracts— Agreements with Municipalities and Metropolitan Regions – Rules Enacted by ARSESP”.

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We currently lack formal agreements or concessions with 53 of the municipalities to which we provide service, and 36 of our existing concession agreements will expire between 2016 and 2030. We may face difficulties in continuing to provide water and sewage services in return for payment in these and other municipalities, and we cannot assure you that they will continue to purchase services from us on the same terms or at all.

As of December 31, 2015, we held formal 30 year agreements with 278 municipalities (including the city of São Paulo) of the 364 municipalities we serve. We entered into 4 of these agreements during 2015. The 278 municipalities with which we had formal agreements at year-end accounted for 78.6% of our total revenues for the year ended December 31, 2015, and 68.4% of our intangible assets as of December 31, 2015. Of the 53 served municipalities for which we lacked formal agreements at year-end, we were in the process of actively renegotiating with all municipalities. Together, these 53 municipalities accounted for 12.9% of our total revenues for the year ended December 31, 2015 and 21.6% of our intangible assets as of that same date. Between 2016 and 2030, 36 of our existing concession agreements will expire. These 36 concession agreements accounted for 7.8% of our total revenues for the year ended December 31, 2015 and 7.4% of our intangible assets as of that same date.

We may not be able to continue providing service on current terms, or at all, in the municipalities for which we do not have formal agreements, including the 53 for which we are renegotiating expired agreements. In particular, the lack of formal concessions or contractual rights in these municipalities means that we may not be able to enforce our right to continue to provide services and we may face difficulties in being paid on a timely basis, or at all, for the unamortized assets. If we are successful in renegotiating the expired agreements, or executing formal agreements with the municipalities for which we have never had agreements, those agreements may not contain terms that are as favorable as those under which we currently operate. We cannot make any such assumption because the Basic Sanitation Law prevents us from planning, regulating and monitoring our services and it requires more stringent control by the municipalities or by ARSESP. The municipalities for which we do not have formal agreements may choose to start providing water and sewage services directly themselves, or may run public tenders to select another provider. They may set eligibility requirements for which we do not qualify and, if we do qualify and participate in these tenders, we may not win.

Any of these events could have a material adverse effect on our business, results of operations and financial condition. See “Item 4.B. Business Overview—Our Operations” and “Item 4.B. Business Overview— Government Regulations Applicable to our Contracts - Contracts for the Provision of Essential Basic Sanitation Services in Brazil.”

In the municipalities with which we did not have formal agreements by December 31, 2015, we continued operating with municipal approval or with judicial support.

Municipalities may terminate our concessions before they expire in certain circumstances. The indemnification payments we receive in such cases may be less than the value of the investments we made.

Municipalities have the right to terminate our concessions if we fail to comply with our contractual or legal obligations or if the municipality determines in an expropriation proceeding that early termination of the concession is in the public interest. If a municipality terminates our concession, we are entitled to be indemnified for the unamortized portion of our investments.

The Basic Sanitation Law provides that on early termination of a concession, the entity that provides sanitation services should carry out a valuation of the assets that relate to the services provided, in order to calculate the unamortized portion of its investments. This valuation uses the criteria defined in the service contract or, in the absence of a contract, is based on customary practice with respect to the services for the preceding 20 years. The resulting indemnification payment may be less than the remaining value of the investments the sanitation service provider made. Nonetheless, the indemnification payments may not occur voluntarily by the municipality, creating an

opportunity for judicial dispute. If faced with such a situation, there is the risk that the judicial decision will consider the indemnification as undue or set it at a lower value than that of our investments.

With regard to our operations that lack contracts or have indefinite or overdue timeframes, the Basic Sanitation Law reduced the maximum time period for payment of indemnification in such cases to four years. This provision applies to concession agreements entered into prior to the enactment of the Basic Sanitation Law only to the extent that the concession agreement does not contain a contractual indemnification provision, or we have not otherwise entered into an agreement with the municipality with regard to such early termination. These provisions have not yet been tested by the courts and we are therefore unable to predict the effect of the Basic Sanitation Law on our rights to indemnification for the early termination of any particular concession.

In 1997, the municipality of Santos enacted a law in order to repossess our water and sewage systems in Santos. We adopted the necessary judicial measures to contest this and we filed an ordinary suit against the municipality of Santos, after which the appellate court issued a decision in our favor. The proceedings were terminated and we have continued operations in the municipality. In September 2015, the State of São Paulo and the municipality of Santos entered into a service provision contract, with the intervention and consent of ARSESP. Under this agreement, ARSESP exercises the duties of regulating and supervising the provision of water and basic sanitation services in Santos, while SABESP continues to be responsible for the provision of water and basic sanitation to the municipality of Santos for the next 30 years.

In 1995, the municipality of Diadema terminated its concession agreement with us and did not pay the indemnification for our investments. In March 2014, we entered into an agreement with the municipality of Diadema to resolve water supply-related debt and indemnities. This agreement includes a contract to resume direct supply of water and sewage services to the municipality of Diadema for 30 years with the regulation and supervision of ARSESP. Guarantees are in place if the municipality of Diadema breaches the agreement entered into with us.

Other municipalities may seek to terminate their concession agreements before the contractual expiration date. If this occurs and we do not receive adequate indemnification for our investments, or the indemnification is paid over an extended period, we may suffer material harm to our financial position.

We may face difficulties in collecting overdue amounts owed to us by municipalities to which we provide water on a wholesale basis and municipal government entities.

As of December 31, 2015, our total accounts receivable was R\$4,817.4 million. Of this amount, certain municipalities to which we provide water on a wholesale basis owed us R\$2,311.3 million, and certain municipal government entities owed us R\$710.4 million. Of the total amount owed by municipalities, R\$237.8 million was overdue by between 30 and 360 days and R\$2,047.7 million was overdue by over 360 days.

The Brazilian courts are entitled to obligate us to continue to supply water to these municipalities, even when we have not received payments due to us. We have no way of ensuring that negotiations with these municipalities or legal action taken against the municipalities will result in payments being made. Some entities associated with municipal governments for which we provide services also do not make regular payments. We cannot guarantee if or when these entities will make payments on a regular basis or pay the amounts owed to us. If the municipalities and related entities do not pay the amounts owed to us, we may experience a further material adverse effect on our financial position.

Aiming to revolve existing debts with the municipalities to which we provide water on a wholesale basis, in 2015 we intensified the process of collecting the debts for the provision of water and basic sanitation through the Single Registry of Debtors of São Paulo (*Cadastro Único de Devedores de São Paulo*), or State CADIN. With regard to three municipalities to which we provide water on a wholesale basis, Santo André, Guarulhos and Mauá, in October 2015 and January 2016 we had executed Protocols of Intentions with each of them, to prepare studies and evaluations aimed at resolving commercial relations and exiting debts between these municipalities and us.

For more information on wholesale operations, see “Item 4.B. Business Overview—Our Operations—Description of Our Activities—Wholesale Operations”.

Any failure to obtain new financing may adversely affect our ability to continue our capital expenditure program.

Our capital expenditure program will require resources of approximately R\$12.5 billion in the period from 2016 through 2020. In 2015 we recorded R\$3.5 billion in capital expenditures.

In addition to cash generated by our operations, we have funded and intend to continue funding these capital expenditures with issuances of debt securities in the domestic and international capital markets as well as borrowings in Brazilian *reais* and foreign currencies. A significant portion of our financing needs is obtained through long term financing at attractive interest rates from Brazilian federal public banks, multilateral agencies and international governmental development banks. If the Brazilian government changes its policies regarding the financing of water and sewage services, or if we fail to obtain long term financing at attractive interest rates from domestic and international multilateral agencies and development banks in the future, we may not be able to meet our obligations or finance our capital expenditure program, which could have a material adverse effect on our business and financial condition.

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Furthermore, Brazilian public and private financial institutions are legally limited up to a certain percentage of their shareholder's equity to provide loans to public sector entities, including, for example, us. These limitations could adversely affect our ability to continue our capital expenditure program.

Our debt includes financial covenants that impose indebtedness limits on us. Our failure to comply with these covenants could seriously impair our ability to finance our capital expenditure program, which could have a material adverse effect on us. For further information on these covenants, see "Item 5.B. Liquidity and Capital Resources—Capital Sources—Indebtedness Financing—Financial Covenants".

Compliance with environmental laws and environmental liability payments could have a material adverse effect on us.

We are subject to extensive Brazilian federal, state and municipal laws and regulations relating to the protection of human health and the environment. These laws and regulations set potable water standards and limit or prohibit the discharge or spillage of effluent produced in our operations, particularly raw sewage. We occasionally suffer accidents such as leakages or breaks in pipes that could lead to liability for damages under environmental law. We could be subject to various types of criminal, administrative and civil proceedings for non-compliance with environmental laws and regulations that could expose us to penalties and criminal sanctions, such as fines, closure orders and significant indemnification obligations. The scope and enforcement of environmental laws in Brazil are becoming more stringent, and our capital expenditures and environmental compliance costs may increase substantially as a result. These expenses may lead us to reduce expenditure on strategic investments, which could harm our business. In addition, Brazilian courts are enforcing environmental laws more stringently than in the past, which may result in fines or liability for damages that are significantly higher than those we currently anticipate. We are party to various environmental proceedings that could have a material adverse impact on us, including civil processes and investigations relating to the release of untreated sewage into waterways and the disposal of sludge generated by treatment plants. We are also involved in proceedings challenging the extraction of water resources in the face of the current water crisis. Any unfavorable judgment in relation to these proceedings, or any material unforeseen environmental liabilities, may have a material adverse effect on us. For further information on these proceedings, see "Item 8.A. Financial Statements and Other Financial Information—Legal Proceedings". For further information on investments in environmental programs, see "Item 4.A. History and Development of the Company—Main Projects of our Capital Expenditure Program", "Item 4.B. Business Overview—Sewage Treatment and Disposal", "Item 4.B Business Overview—Environmental Matters" and "Item 4.B. Business Overview—Environmental Regulation". For further information on the Water Crisis, see "Item 4.B. Business Overview—The Current Water Crisis".

New laws and regulations relating to climate change and changes in existing regulation, as well as the escalation of the physical effects of extreme weather events, may result in increased liabilities and increased capital expenditures, which could have a material adverse effect on us.

Current federal, state and municipal laws and regulations on climate change establish global goals, which we will have to meet, concerning greenhouse gas emissions and this may require us to increase our investments in order to comply with these laws. Currently, such goals have not yet been established for the sanitation sector, however, if we increase our capital expenditures for this purpose, we may be required to reduce expenditures on other strategic investments.

In addition, climate change may lead to increased frequency of extreme weather events such as droughts or torrential rain, which may affect our ability to deliver our services and require us to strengthen our actions such as:

- investing in seeking new water sources located further from major consumer centers;

- investing in new technologies;
- improvement of water conservation practices and demand management alternatives such as economic mechanisms or educational programs; and
- increasing the capacity of our water reserves.

Extreme weather events such as torrential rain may also cause impacts to our installations that can lead to negative impacts to the environment and society.

A rise in sea level could result in increased salinity in the river estuaries where we abstract water, which could affect water treatment in these areas. Rising sea levels could also cause damage in our sewage collection network.

Additionally, increases in air temperature could affect demand for water. Increased frequency of extreme weather events may also further reduce water levels in the reservoirs that power hydroelectric power plants in Brazil, which may cause energy shortages and increase electricity prices, which may adversely affect our costs and operations.

We cannot predict all of the effects of extreme weather events, therefore making it difficult to predict necessary investments. We have not provisioned any funds for climate change events as current technology and scientific understandings of climate change make it difficult to predict potential expenses and liabilities.

We may be required to adopt new norms to improve our energy use efficiency and minimize the release of greenhouse gases when we renew the environmental licenses for the systems already in operation or when we obtain environmental licenses for new enterprises.

We may need to make substantial new expenditures, either to comply with new environmental regulations linked to climate change or to prevent or correct the physical effects of extreme weather events, any of which could have a material adverse effect on our results of operations.

For more information, see “Item 4.B. Business Overview—Environmental Matters—Climate Change Regulations: Reduction of Greenhouse Gases (GHG) Emissions” and “Item 4.B. Business Overview—Energy Consumption”.

Any substantial monetary judgment against us in legal proceedings may have a material adverse effect on us.

We are party to a number of legal proceedings involving significant monetary claims. These legal proceedings include, among others, civil, tax, labor, corporate and environmental issues. As of December 31, 2015, the total value of all outstanding claims against us was R\$47,936.8 million (net of R\$386.3 million in escrow deposits). A substantial monetary judgment against us in one or more of these legal proceedings may have a material adverse effect on our financial condition. We have provisioned a total aggregate amount of R\$1,082.2 million (net of escrow deposits) as of December 31, 2015 to cover probable losses related to legal proceedings. This provision does not cover all legal proceedings involving monetary claims filed against us and it may be insufficient to cover our liabilities related to these claims. Any unfavorable judgment in relation to these proceedings may have a material adverse effect on us. For more information, see “Item 8.A. Financial Statements and Other Financial Information—Legal Proceedings”.

Risks Relating to Our Common Shares and ADSs

We may not always be in a position to pay dividends or interest on shareholders’ equity and ADSs.

Depending on our future results, our shareholders may not receive dividends or interest on own capital if we do not generate a profit. Despite the requirement to distribute a minimum of 25% of our annual net income to shareholders, our future financial position may not permit us to distribute dividends or pay interest on own capital.

The relative volatility and illiquidity of the Brazilian securities markets may substantially limit your ability to sell our common shares underlying the ADSs at the price and time you desire.

Investing in securities from emerging markets such as Brazil involves greater risk than investing in securities of issuers in major securities markets, and these investments are often considered to be more speculative in nature. The Brazilian securities market is substantially smaller, less liquid, more concentrated and can be more volatile than major securities markets. Accordingly, although you are entitled to withdraw the common shares underlying the ADSs from the depositary at any time, your ability to sell the common shares underlying the ADSs at a price and time at which you wish to do so may be substantially limited. There is also significantly greater concentration in the Brazilian securities market than in major securities markets. The ten largest companies in terms of market capitalization represented approximately 51% of the aggregate market capitalization of the BM&FBOVESPA as of December 31, 2015.

Investors who exchange ADSs for common shares may lose their ability to remit foreign currency abroad and obtain Brazilian tax advantages.

The Brazilian custodian for the common shares underlying our ADSs must obtain a certificate of registration from the Central Bank in order to be entitled to remit U.S. dollars abroad for payments of dividends and other distributions relating to our common shares or upon sales of our common shares. If an ADR holder decides to exchange ADSs for the underlying common shares, the holder will be entitled to continue to rely on the custodian's certificate of registration for five business days from the date of exchange. After that period, the holder may not be able to obtain and remit U.S. dollars abroad upon sale of our common shares, or distributions relating to our common shares, unless he or she obtains his or her own certificate of registration or registers the investment under CMN Resolution No. 4,373/2014, dated September 29, 2014, which entitles registered foreign investors (the "4,373 Holder") to buy and sell on a Brazilian stock exchange. If the holder does not obtain a certificate of registration or register under Resolution No. 4,373/2014, the holder will generally be subject to less favorable tax treatment on gains with respect to our common shares.

If a holder attempts to obtain his or her own certificate of registration, the holder may incur expenses or suffer delays in the application process, which could delay his or her ability to receive dividends or distributions relating to our common shares or the return of his or her capital in a timely manner. The custodian's certificate of registration or any foreign capital registration obtained by a holder may be affected by future legislative changes, and additional restrictions applicable to the holder, the disposition of the underlying common shares or the repatriation of the proceeds of disposition may be imposed in the future.

A holder of common shares or ADSs may face difficulties in protecting his or her interests as a shareholder because we are a Brazilian mixed capital company.

We are a mixed capital company (*sociedade de economia mista*) organized under the laws of Brazil, and all of our directors and officers and our controlling shareholder reside in Brazil. All of our assets are located in Brazil. As a result, it may not be possible for a holder to effect service of process upon us or these other persons within the United States or other jurisdictions outside Brazil or to enforce against us or these other persons judgments obtained in the United States or other jurisdictions outside Brazil. Because judgments of U.S. courts for civil liabilities based upon the U.S. federal securities laws may only be enforced in Brazil if certain requirements are met, a holder may face more difficulty in protecting his or her interests in the case of actions by our directors, officers or our controlling shareholder than would shareholders of a corporation incorporated in a state or other jurisdiction of the United States. In addition, under Brazilian law, none of our assets which are essential to our ability to render public services are subject to seizure or attachment. Furthermore, the execution of a judgment against our controlling shareholder may be delayed, since the State may only be able to pay a judgment if it is provided for in its budget in a subsequent fiscal year. None of the public property of our controlling shareholder is available for seizure or attachment, either prior to or after judgment.

Mandatory arbitration provisions in our bylaws may limit the ability of a holder of our ADSs to enforce liability under U.S. securities laws.

Under our bylaws, any disputes among us, our shareholders and our management with respect to the *Novo Mercado* rules, Law No. 6,404 of December 15, 1976, as amended ("Brazilian Corporate Law") and Brazilian capital markets regulations will be resolved by arbitration conducted pursuant to the BM&FBOVESPA Arbitration Rules in the Market Arbitration Chamber. Any disputes among shareholders and ADR holders, and any disputes between us and our shareholders and ADR holders, will also be submitted to arbitration. As a result, a court in the United States might require that a claim brought by an ADR holder predicated upon the U.S. securities laws be submitted to arbitration in accordance with our bylaws. In that event, a purchaser of ADSs would be effectively precluded from

A holder of our common shares and ADSs might be unable to exercise preemptive rights and tag along rights with respect to the common shares.

U.S. holders of common shares and ADSs may not be able to exercise the preemptive rights and tag along rights relating to common shares unless a registration statement under the U.S. Securities Act of 1933, as amended, or the Securities Act, is effective with respect to those rights or an exemption from the registration requirements of the Securities Act is available. We are not obligated to file a registration statement with respect to our common shares relating to these rights, and we cannot assure you that we will file any such registration statement. Unless we file a registration statement or an exemption from registration is available, an ADR holder may receive only the net proceeds from the sale of his or her preemptive rights and tag along rights or, if these rights cannot be sold, they will lapse and the ADR holder will receive no value for them.

Holders of our ADSs do not have the same voting rights as our shareholders.

Holders of our ADSs do not have the same voting rights as holders of our shares. Holders of our ADSs are entitled to the contractual rights set forth for their benefit under the deposit agreements. ADS holders exercise voting rights by providing instructions to the depositary, as opposed to attending shareholders meetings or voting by other means available to shareholders. In practice, the ability of a holder of ADSs to instruct the depositary as to voting will depend on the timing and procedures for providing instructions to the depositary, either directly or through the holder's custodian and clearing system. The deposit agreement also provides that if the depositary does not receive any instructions from a holder of ADRs, the ADR holder may be deemed to have given a discretionary proxy to a person designated by our company and the underlying shares may be voted by such person. However, we have chosen not to designate any person to exercise these deemed proxy rights with respect to any annual or special general meetings, and ADSs for which no specific voting instructions were received by the Depositary were therefore not voted at that meeting.

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Overview

Companhia de Saneamento Básico do Estado de São Paulo – SABESP is a mixed capital company (*sociedade de economia mista*) with limited liability. We were incorporated on September 6, 1973 under the laws of the Federative Republic of Brazil. We are registered with the Commercial Registry of the State of São Paulo (*Junta Comercial do Estado de São Paulo*) under registration number NIRE 35300016831. Our principal executive offices are located at Rua Costa Carvalho, 300, 05429 900 São Paulo, SP, Brazil. Our telephone number is +55 11 3388 8000. Our agent for service of process in the United States is CT Corporation System, with offices at 818 West Seventh Street – Team 1, Los Angeles, CA 90017. We are allowed to operate, in a subsidiary form, in other Brazilian locations and abroad. See “Item 4.B. Business Overview— Government Regulations Applicable to Our Contracts—Contracts for the Provision of Essential Basic Sanitation Services in Brazil”.

We believe we are one of the largest water and sewage service providers in the world (based on the number of customers in 2013, according to the 14th edition of the *Pinsent Masons Water Yearbook 2012-2013*, the most recent edition released of this study). We operate water and sewage systems in the state of São Paulo, which includes the

city of São Paulo, Brazil's largest city. According to the IBGE, the state of São Paulo is Brazil's most populous state and the state with the highest gross domestic product, or GDP, in Brazil. For the year ended December 31, 2015, we generated net revenue of R\$11,711.6 million and net income of R\$536.3 million. Our total assets amounted to R\$33,706.6 million and our total shareholders' equity amounted to R\$13,716.6 million as of December 31, 2015.

As of December 31, 2015, we provided water and sewage services to a broad range of residential, commercial, industrial and governmental customers in 364 of the 645 municipalities in the state of São Paulo, including the city of São Paulo. Substantially all of our concessions or program agreements have 30 year terms. At year-end 2015 we lacked formal agreements for 53 of the municipalities we serve, each of which we are currently in the process of renegotiation. From January 1, 2016 through 2030, 36 further concessions will expire, and we will seek to replace them with program agreements. In addition to the 364 municipalities we served, we also provided water service to the municipality of Mogi das Cruzes, pursuant to two partial water contracts under which we service only certain neighborhoods of that municipality. See "Presentation of Financial and Other Information—Other Information—Our Contracts and the Municipalities We Serve".

We also supply water on a wholesale basis to 5 municipalities in the São Paulo metropolitan region in which we do not operate water distribution systems (together covering a total estimated urban population of approximately 3.1 million). 4 of these municipalities also utilize our sewage treatment services. For the year ended December 31, 2015, the São Paulo metropolitan region (including the municipalities to which we provide water on a wholesale basis) accounted for 67.3% of our gross operating revenue (excluding revenues relating to the construction of concession infrastructure), while the Regional Systems accounted for 32.7%.

As of December 31, 2015, we provided water services through 8.4 million water connections to approximately 25.5 million people, representing approximately 60% of the urban population of the state of São Paulo, and had a water coverage ratio of approximately 99% in respect of all regions. As of that date, we provided sewage services through 6.9 million sewage connections to approximately 22.8 million people and had an effective sewage coverage ratio of 86%. As of December 31, 2015, we operated using 71,705 kilometers of water pipes and water transmission lines and 48,774 kilometers of sewer lines.

We also provide water and/or sewage services to 4 other municipalities through special purpose companies. In addition, we provide consulting services regarding the rational use of water and financial, commercial and operational management in Panama, Honduras and Nicaragua. We serve Panama and Honduras through an agreement with the consultancy firm Latin Consult. We also have two partnerships with other companies: Aquapolo Ambiental S.A., a joint venture with a private sanitation services operator, and Attend Ambiental S.A., a joint venture with Estre Ambiental S.A. Aquapolo Ambiental S.A. commenced operations in the second half of 2012 and operates the largest water recycling facility in the southern hemisphere. Aquapolo Ambiental S.A. has the capacity to supply up to 1,000 liters per second to industries in the Capuava petrochemical cluster of the São Paulo metropolitan region. Attend Ambiental commenced operations in the second half of 2014 to operate a pre-treatment plant for non-domestic effluent in the São Paulo metropolitan region.

The State of São Paulo, our controlling shareholder, is required by State Law No. 11,454/2003 to own at least 50% plus one of our common shares. As of April 22, 2016, the State owned 50.3% of our outstanding common shares. As a mixed capital company, we are an integral part of the State governmental structure. Our strategy and major policy decisions are formulated in conjunction with the State Secretariat for Sanitation and Water Resources as part of the State's overall strategic planning. The majority of the members of our board of directors and our board of executive officers are nominated by the State government.

In addition, our capital expenditure budget is subject to approval by the State legislature and is approved in conjunction with the budget of the State Secretariat for Sanitation and Water Resources as a whole. Our financial statements and accounting records are subject to review by the State Accounts Tribunal (*Tribunal de Contas*), as are all accounts of the State.

Our results of operations and financial condition are generally affected (i) by our ability to raise tariffs, control costs and improve productivity, (ii) the general economic conditions in Brazil and abroad; and (iii) climate conditions. In order to supply water to the São Paulo metropolitan region, we use water from eight systems, most of which were affected by the most severe drought in our service region in the last 85 years, of which the Cantareira System, our largest water system, was the most affected. As a result of the drought and the low water inflow in the Cantareira System, DAEE and ANA, since 2014, have continuously regulated the volume of water we are permitted to extract from this system, authorizing us to extract between 13 m³/s and 14 m³/s in the most drastic moments of the crisis. Until the renewal of our water right which shall occur in May 2017, the volume of water that we have been authorized to extract from the Cantareira System has been communicated to us via monthly notices according to the behavior of rainfall, water inflow, level of water in our reservoirs and our requests to extract water based on this information. Due to the return of normal rainfall levels beginning in October 2015, as of February 2016 we have been allowed to extract 23 m³/s of water.

In order to balance supply and demand despite the restricted water availability, we adopted throughout 2014 and 2015 a series of initiatives, amongst which including: (i) using treated water from other production systems to serve consumers originally supplied by the Cantareira system; (ii) to offer discounts (bonus) to consumers that use below average amounts of water, compared to average consumption; (iii) reducing pressure in the water distribution lines in order to decrease leakage; (iv) adjusting the volume of water sold to municipalities that operate their own distribution network; and (v) using pumps in order to extract water located below the intakes of the Cantareira system, from the so-called “technical reserve”. Due to the return of normal rainfall levels in the rainy season beginning in October 2015, as of January 2016 it was no longer necessary to pump water out of the technical reserve of the Cantareira system and we modified the rules for obtaining discounts (bonus) in February 2016. In addition, as of December 2015, the time period during which water is pumped out at reduced pressure in the water distribution lines is returning to the normal nighttime period, as it was prior to the water crisis. In March 2016, as a result of the increased level of rainfall and increased predictability of the level of water in our reservoirs, we requested to ARSESP the cancellations of our Water Consumption Reduction Incentive Program and of the Contingency Tariff. ARSESP approved our requests in the end of March 2016 and the aforementioned policy changes shall be applied to water meter readings recorded as of May 1, 2016.

For further information on the water crisis see “Item 4.B. Business Overview—The Current Water Crisis”.

Our Strengths

We believe that our strong business position and future prospects derive from the following strengths:

Well established business with significant size, scale and know how to operate in complex urban settings. We believe we are one of the largest water and sewage service providers in the world. We provide water services directly to approximately 25.5 million people and supply water on a wholesale basis to an additional urban population of approximately 3.1 million people. As of December 31, 2015, we had an effective water coverage ratio of approximately 99% in respect of all regions in which we operate. We also provide sewage services directly to approximately 22.8 million people, achieving an effective sewage coverage ratio of 86% in respect of all regions in which we operate as of December 31, 2015. Our significant size and scale have required us to operate in complex urban settings such as shantytowns (*favelas*) and environments without urban planning, thereby enabling us to develop well trained personnel, skills for operating in adverse conditions that we believe our competitors lack.

Operations in Brazil’s most populous and wealthy state. The state of São Paulo, which is located in the most developed and economically active region of Brazil, is the most populous state in Brazil, with an estimated total population of 45 million as of December 31, 2015. The city of São Paulo had an estimated total population of 11.1 million as of the same date, while the São Paulo metropolitan region had a total population of 21.4 million. Based on its GDP, the state of São Paulo is the wealthiest state and largest economy in Brazil. The GDP of the state of São Paulo was approximately R\$1.7 trillion in 2013, representing approximately 32.1% of Brazil’s total GDP, according to the most recent data collected by the IBGE. The state of São Paulo generates more revenue from water and sewage services than any other Brazilian state.

Strong Base of Contracted Business. Between January 1, 2007 and December 31, 2015, we executed 30 year agreements with 278 of the 364 municipalities we serve, including an agreement with the city of São Paulo, in June 2010, and Santos in September 2015. For the year ended December 31, 2015, income from these 30 year agreements accounted for 78.6% of our gross operating revenues (including revenues relating to the construction of concession infrastructure).

Access to low cost and diverse sources of financing. Our strong cash flow generation from operations and our role as an essential public service provider places us in a privileged position in our industry to obtain low cost, long term

financing from Brazilian public banks, and domestic and international multilateral agencies and development banks. We do not depend on a limited number of sources of financing, but instead have access to various funding alternatives in the Brazilian and international markets to fund our working capital needs and our capital expenditure programs.

Strong corporate governance practices. In 2002, we joined the *Novo Mercado* segment of the BM&FBOVESPA, which is the listing segment in Brazil with the highest corporate governance requirements. As a result, we are committed to certain corporate governance standards that are not otherwise required by Brazilian law, which provides heightened protection to our shareholders and enhances the quality of information we disclose to the market. From December 1, 2007 until 2015, we were part of the BM&FBOVESPA Corporate Sustainability Index, or ISE. Due to the need to focus the attention of all our departments to overcome the water crisis, we decided not to participate in the selection process to be a part of the ISE in 2016.

High quality operations. We believe that we adhere to high standards of service and employ the best available technology in the sanitation business to control the quality of the water we abstract, process and distribute. Of our 16 laboratories in total, our central laboratory and 13 of our regional laboratories are accredited by the National Institute of Metrology, Quality and Technology, Standardization and Industrial Quality, or INMETRO, and comply with the ABNT NBR ISO IEC 17025 standard, thereby assuring the quality and accuracy of our test results. Moreover, our laboratories and field teams use the latest equipment to detect substances controlled by regulations and have highly trained teams to handle contingencies and customer complaints. We believe our technology enhances the efficiency and quality of our operations.

Our Strategy

Our mission is to provide water and sewage services, contributing to improvements in quality of life and the environment and our goal for the future is to become a global reference in the provision of basic sanitation services in a sustainable, competitive and innovative manner, focused on the needs of our clients. To this end, our strategic objectives are based upon the guiding principles of water safety, quality in the provision of services, sustainability, integration and fostering relationships, innovation and technology, valorization of our personnel and increasing sewage treatment. Our strategic objectives also focus on our political and institutional relationships as well as on our commitment to the market to increase shareholder value. Due to changes in macroeconomic conditions, the water crisis and consequent impacts on our business, our strategy is currently under revision. Commencing in late 2015 and continuing in 2016, this revised strategy will determine our objectives and targets for the next decade. We seek to implement these guiding principles through the following strategies:

Continue to seek growth while improving our financial results by reducing operating costs, increasing productivity and profitability and prudently managing our levels of indebtedness. We aim to apply our principles of financial growth and sustainability to each business unit, assigning goals and setting clear responsibilities to each unit so as to strengthen our financial results. To achieve this goal, we intend to use our best efforts to reduce operating costs and increase productivity and profitability. We plan to improve the management of our assets, as well as to continue to reduce our total operating expenses by automating some of our facilities, streamlining operational processes, implementing integrated planning and further investing in internal technological research and development. We also plan to continue our efforts to improve our collection of overdue accounts receivable from municipalities to which we provide services, from the State and from other governmental entities, including by exploring opportunities to offset these outstanding debts against certain possessory or property rights over utilities relating to water and sewage systems. We intend to continue to fund our working capital needs and estimated capital expenditure programs with diversified sources of financing, such as domestic and international development banks and multilateral agencies. We will continue to seek market opportunities for low cost financing and restructuring of our indebtedness if and when advantageous and appropriate.

Improve operating efficiency and reduce water loss. We seek to reduce both physical water loss, which results mainly from leakage; non physical water loss, which results primarily from inaccurate water meters installed at customers' premises and at our water treatment facilities; and clandestine and illegal water use. In order to achieve more consistent long term results, we have developed a comprehensive 12 year program to reduce our water loss rate. The first four years of the program from 2009 to 2012 were funded by *Banco Nacional de Desenvolvimento Econômico e Social*, or "BNDES". From 2013 to 2019, part of the program will be funded by a loan granted by the government of Japan through the Japan International Cooperation Agency, or "JICA". In October, 2015, we asked JICA for a term extension in order conclude construction work that is within the scope of financing, due to changes in economic conditions in Brazil. The exchange rate changed significantly last year, with the depreciation of *real*. This situation, combined with the negative impact of the current water crisis on our revenue for 2015 and the need to prioritize investment in water production, impacted our ability to invest, resulting in the need to increase the term of JICA loan. Therefore, the period the program will be funded by the JICA loan will extend until 2019. For more

information on the program to reduce water loss, see “Item 4.B. Business Overview— Corporate Program for Reduction of Water Loss”.

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Ensure the quality and availability of our services in our existing service area. Our goal is to maintain an effective water coverage ratio of around 100%, coupled with a high standard of quality and availability, and meet the expected population growth by adding 816 thousands water connections between 2016 and 2020. We also intend to increase our sewage coverage ratio to 95% by 2020 by adding 1.19 million sewage connections. In addition, we are also developing short, medium and long term marketing strategies, such as client segmentation and tailor made solutions for different types of clients, which we believe will help us increase our customer base. We also seek to improve our customer support strategies by modernizing our telephone-based and internet based customer support and to continuously measure the level of satisfaction of our clients.

Maintain and continue to expand our existing service areas. We intend to maintain and expand our operating base by executing new agreements. To this end, we are actively seeking to develop closer relationships with the municipal governments that we currently serve in order to increase customer loyalty and thereby renew all or substantially all our concession agreements as they expire. In June 2010, we entered into a 30 year agreement with the State and city of São Paulo for the provision of water and sewage services in the city of São Paulo, which in the year ended December 31, 2015 accounted for 48.2% of our gross operating revenues (excluding revenues relating to the construction of concession infrastructure). Between January 1, 2007 and December 31, 2015, we entered into agreements with 278 municipalities (including our services agreement with the city of São Paulo), of which 4 were entered into in 2015. These 278 municipalities accounted for 78.6% of our total revenues for the year ended December 31, 2015 and 68.4% of our intangible assets as of the same date. As of December 31, 2015, 53 of our concessions had expired and are currently being renegotiated. These 53 municipalities accounted for 12.9% of our total revenues for the year ended December 31, 2015 and 21.6% of our intangible assets as of the same date. From January 1, 2016 through 2030, 36 concession agreements, accounting for 7.8% of our revenues for the year ended December 31, 2015 and 7.4% of our intangible assets as of the same date, will expire.

In 2015 we invested R\$3.5 billion and between 2016 and 2020 we plan to invest an additional R\$12.5 billion to improve and expand our water and sewage system, increase water security, and meet the growing demand for water and sewage services in the state of São Paulo, thereby encouraging these customers to continue using our services. We also regularly explore the possibility of executing agreements for the provision of water and sewage services in municipalities in the state of São Paulo in which we currently have no operations or to which we currently supply water and provide sewage treatment solely on a wholesale basis, which together represent a total population of approximately 17 million. We evaluate possible expansion opportunities in terms of proximity to our existing service areas to maximize return on investment and improve our financial performance. We also intend to study and take advantage of opportunities in other Brazilian states and in other countries to expand our services and increase our market share.

Expand our water and sewage services. We had an effective sewage coverage ratio of 86% as of December 31, 2015 and plan to increase this ratio to 95% by 2020 by adding over 1.19 million sewage connections and sewage treatment from 78% to 95% by 2020. These investments are necessary to restore the quality of the rivers and lakes, providing new sources for water supply. In addition, there are municipalities in the state of São Paulo representing a total population of approximately 17 million to which we currently do not provide water or sewage services, or to which we currently supply water solely on a wholesale basis. Our strong presence in the State and experience in providing water and sewage services places us in a privileged position to expand our sewage services to these additional municipalities in the state of São Paulo as well as to other Brazilian states and abroad. Furthermore, we seek to deepen our relationships with strategic clients that consume high volumes of water (more than 500 cubic meters per month) by applying special tariffs to these clients. For more information, see “Item 4.B. Business Overview—Description of our Activities—Sewage Operation” and “Item 4.B. Business Overview—Competition” and “Item 4.B. Business Overview—Tariffs”.

Seek selective opportunities to expand our business. In accordance with our bylaws, our activities comprise water supply, sanitary sewage services, urban rainwater management and drainage services, urban cleaning services, solid waste management services, and also related activities, including the planning, operation, maintenance and commercialization of energy, and the commercialization of services, products, benefits and rights that directly or indirectly arise from our assets, operations and activities. We are allowed to act, in a subsidiary form, in other Brazilian locations and abroad. Since 2008, we have expanded into activities that complement water and sewage services in which we may leverage our know how, size, scale and profitability. These activities include consulting and management of sanitation systems.

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The following services have already been completed:

- Under an agreement with Latin Consult, we provided consulting services to seven municipalities in Honduras to implement a new commercial and operational management model.
- We worked with the basic sanitation company of the state of Alagoas to provide technology for the reduction of water loss in the city of Maceió. Under this type of contract, we were remunerated based on our success rate, or more specifically, we profited based on the reduction of water loss achieved in the city of Maceió.
- We developed the sanitation plan for the municipality of Barro Alto in the state of Goiás.
- We concluded the implementation and the customization of our Aqualog software in the Sanitation Company of Espírito Santo (*Companhia Espírito Santense de Saneamento's - CESAN*) water treatment plant in the municipality of Nova Venécia in the state of Espírito Santo.
- Attend Ambiental S.A., a joint venture with Estre Ambiental S.A., commenced operation of a pre treatment and processing plant for non-domestic effluent in the São Paulo metropolitan region during the second half of 2014.

The following services are still in the process of completion:

- An agreement with Latin Consult, we are providing consulting services to the *Instituto de Acueductos y Alcantarillados Nacionales*, the company responsible for water and sewage services in Panama, to assist with sustainable water use and implement a new model for commercial, financial and operational planning and management. The contract is expected to end in 2016.
- Since 2014, we have been working in Nicaragua, focusing on consulting and training in management and in the reduction of water loss. This work is scheduled to end in 2016 and is part of an agreement between Brazil and Japan, in which a bilateral technical cooperation agreement was formalized between us and *Empresa Nicaragüense de Acueductos y Alcantarillados (ENACAL)* in Nicaragua.
- We formed Paulista Geradora de Energia, a joint venture with *Servtec Investimentos e Participações Ltda.* and *Tecniplan Engenharia e Comércio Ltda.*, in which we will install two small hydroelectric power plants with a total capacity of 7 MW. One of the hydroelectric power plants will be built in our water treatment plant in Guaraú. The plants are scheduled to begin operating in the second half of 2017.

Establish efficient and competitive ways of attracting, retaining and motivating our personnel. We intend to become a reference in human resource management, providing our personnel with growth opportunities and recognition. We seek to raise workplace satisfaction levels by establishing programs for the professional and personal development of our employees, setting competitive benefit packages and creating a healthy and collaborative work environment.

Streamline internal processes. We are implementing plans to increase our speed and productivity in responding to regulatory changes; to strengthen and streamline our financial, commercial and administrative structure; to provide a solid and integral base of information to support the decision-making process; and to increase the efficiency of our operations while also reducing costs. To this end, we invest in information technology to guarantee the resiliency of our business, thus providing an environment of agile, dynamic and secure information technology, capable of absorbing the demand elasticity of our mission-critical systems and of guaranteeing its continuity in case of datacenter failure (including systematic, technological and infrastructure remodeling) and procedures to conform to the best information technology and corporate governance practices.

Additionally, in 2012 we began implementing an enterprise resourcing planning, or “ERP system”, to replace our commercial and management information systems. We contracted through a bidding process the Águas Claras Consortium, currently Consórcio Nascente, which consists of Accenture and Engineering and which will provide us with SAP’s ERP system and the Net@suite system. We estimated that the ERP system would have been implemented in 2014 and the Net@suite in 2015, but during the test phase we concluded that some important system functionalities should have been adjusted and exhaustively tested before being implemented in order to minimize risks to our business which led us to postpone the implementation to 2016 and 2017, respectively.

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Manage the current adverse climate conditions and mitigate their negative impact. Our goal is to consistently meet the needs of our consumers with our services, and in 2014 and 2015, we managed to do so despite the water crisis. In 2014 and 2015, we invested approximately R\$730 million to mitigate the impacts of the water crisis and provide the São Paulo metropolitan region with better access to water sources, more robust production and transport capacity of treated water and increase treated water capacity. Furthermore, we have planned a series of short-term and medium-term measures that we expect will increase the ability of our immediate water supply to cope with the water crisis and significantly improve future water security by the end of the decade. For more information, see “— Business Overview—The Current Water Crisis”.

We believe that our overall strategy will enable us to meet the demand for high quality water and sewage services in the state of São Paulo as well as in other Brazilian states and abroad, while creating shareholder value and strengthening our results of operations and our financial conditions.

State of São Paulo

The state of São Paulo is one of 26 states that, together with the Federal District of Brasília, constitute the Federative Republic of Brazil. The state of São Paulo is located in the southeastern region of the country, which also includes the States of Minas Gerais, Espírito Santo and Rio de Janeiro, and which is, according to IBGE, the most developed and economically active region of Brazil. The state of São Paulo is located on the Atlantic coast of Brazil and is bordered by the states of Rio de Janeiro and Minas Gerais to the north, the state of Paraná to the south and the state of Mato Grosso do Sul to the west.

The state of São Paulo occupies approximately 3.0% of Brazil’s land mass and encompasses an area amounting to approximately 96,000 square miles. According to the SEADE, the state of São Paulo had an estimated total population of 45 million as of December 31, 2015. The city of São Paulo, capital of the state of São Paulo, had an estimated total population of 11.1 million, with a total population of 21.4 million inhabitants in the São Paulo metropolitan region, as of December 31, 2015. The São Paulo metropolitan region encompasses 39 municipalities and is the largest metropolitan region in the Americas and the fourth largest metropolitan region in the world, according to the United Nations’ World Urbanization Prospects, 2014 Revision, with approximately 47% of the total population of the state of São Paulo as of December 31, 2015.

According to the most recent data collected by the IBGE, the GDP of the state of São Paulo was approximately R\$1.7 trillion in 2013, representing approximately 32.1% of Brazil’s total GDP, and making it the largest economy of any state in Brazil based on GDP. According to the IBGE, the state of São Paulo is also the leading Brazilian state in terms of manufacturing and industrial activity, with a strong position in car manufacturing, pharmaceuticals, computer manufacturing, steel making and plastics, among other activities, as well as a leading position in the banking and financial services industries. The state of São Paulo is the leading export state in Brazil, according to the Brazilian Ministry of Development, Industry and Foreign Trade (*Ministério do Desenvolvimento, Indústria e Comércio Exterior*).

History

Until the end of the nineteenth century, water and sewage services in the state of São Paulo were generally provided by private companies. In 1875, the Province of São Paulo granted a concession for the provision of water and sewage services to Cantareira Water and Sewage Company (*Companhia Cantareira de Água e Esgotos*). In 1893, the government of the Province of São Paulo assumed responsibility for the provision of water and sewage services from Cantareira Water and Sewage Company and formed the Office of Water and Sewers (*Repartição de Água e Esgotos*), a government agency. Since that time, water and sewage services in the São Paulo metropolitan region have been administered by the State government. Historically, water and sewage services in substantially all other municipalities

of the State were administered directly by the municipalities, either by municipal water and sewage departments or through *autarquias* of the municipal government. *Autarquias* are relatively autonomous public bodies with separate legal standing, assets and revenues, created by law to carry out the administration of public services where the government deems that a decentralized administrative and financial structure would be advantageous.

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In 1954, in response to dramatic population growth in the São Paulo metropolitan region, the State government created the Department of Water and Sewers (*Departamento de Águas e Esgotos*) as an *autarquia* of the State. The Department of Water and Sewers provided water and sewage services to various municipalities in the São Paulo metropolitan region.

A major restructuring of the entities providing water and sewage services in the state of São Paulo occurred in 1968, with the creation of the Water Company of the São Paulo metropolitan Region (*Companhia Metropolitana de Água de São Paulo*), or the “COMASP”, the purpose of which was to provide potable water on a wholesale basis for public consumption in the various municipalities of the São Paulo metropolitan region. All assets relating to the production of potable water for the São Paulo metropolitan region previously owned by the Department of Water and Sewers were transferred to COMASP. In 1970, the State government created the Superintendence of Water and Sewers of the City of São Paulo (*Superintendência de Água e Esgoto da Capital*), or the “SAEC”, to distribute water and collect sewage in the city of São Paulo. All assets relating to water services previously owned by the Department of Water and Sewers were transferred to the SAEC. Also in 1970, the State created the Basic Sanitation Company of the São Paulo metropolitan Region (*Companhia Metropolitana de Saneamento de São Paulo*), or the SANESP, to provide sewage treatment services for the São Paulo metropolitan region. All assets relating to sewage services previously owned by the Department of Water and Sewers were transferred to the SANESP. The Department of Water and Sewers was subsequently closed.

On June 29, 1973, pursuant to State Law No. 119/1973, COMASP, SAEC and SANESP merged to form our Company with the purpose of implementing the directives of the Brazilian government set forth in the National Water Supply and Sanitation Plan (*Plano Nacional de Saneamento*). We were incorporated under the laws of Brazil as a limited company (*sociedade anônima*), for indefinite duration. The National Water Supply and Sanitation Plan was a program sponsored by the Brazilian government, which financed capital investments in, and assisted in the development of, state controlled water and sewage companies. Since our formation, other State governmental and State controlled companies involved in water supply and sewage collection and treatment in the state of São Paulo have been merged into our company. The State has always been our controlling shareholder, as required by State Law No. 11,454/2003. We have therefore been integrated into the State governmental structure and our strategies have been formulated in conjunction with the strategies of the State Department of Water Resources and Sanitation. Additionally, a majority of the members of our board of directors and our management are appointed by the State Government.

Our capital expenditure budget is subject to approval by the State legislative chamber. This approval is obtained simultaneously with the approval of the budget of the São Paulo Secretariat for Sanitation and Water Resources (*Secretaria de Saneamento e Recursos Hídricos do Estado de São Paulo*). We are also subject to supervision from the Court of Audit of the State of São Paulo (*Tribunal de Contas do Estado de São Paulo*), with regard to our accounting, financial and budgetary activities and our operating assets.

We provide water and sewage services directly to a large number of residential, commercial and industrial private consumers, as well as to a variety of public entities, in 364 of the 645 municipalities in the State, including in the city of São Paulo. We also supply water on a wholesale basis to 5 municipalities in the São Paulo metropolitan region in which we do not operate water distribution systems, and 4 of these municipalities also utilize our sewage treatment services. According to the 14th edition of the *Pinsent Masons Water Yearbook* (2012–2013), the most recent edition released of this study, we are the 5th largest water and sewage service company in the world in terms of number of clients.

In 1994, we were registered with the CVM as a publicly-held company and are therefore subject to the CVM’s rules, including those relating to the periodic disclosure of extraordinary facts or relevant events. Our common shares have been listed on the BM&FBOVESPA under the ticker “SBSP3” since June 4, 1997.

In 2002, we joined the *Novo Mercado* segment of the BM&FBOVESPA, which is the listing segment in Brazil with the highest corporate governance requirements. In the same year, we registered our common shares with the Securities and Exchange Commission, or SEC, and started trading our shares in the form of ADR – level III on the New York Stock Exchange, or NYSE.

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In 2004, the State of São Paulo carried out a secondary offer of common shares of our company in the Brazilian and international markets.

In December 2007, Law No. 1,025/2007, which provided for the creation of regulatory agencies for the supervision of water and sewage services, created ARSESP, the regulatory agency that regulates and supervises the services we provide.

Corporate Organization

We currently have six management divisions, each of which is supervised by one of our executive officers.

Our board of directors allocates responsibilities to our executive officers following an initial proposal made by our Chief Executive Officer, in accordance with our bylaws. The Chief Executive Officer is responsible for coordinating all management divisions in accordance with the policies and directives established by our board of directors and board of executive officers, including the coordination, evaluation and control of all functions related to the Chief Executive Officer's office and staff, integrated planning, business management and corporate organization, communication, audit, regulatory affairs and ombudsman. The Chief Executive Officer represents our company before third parties and certain powers can be granted to attorneys in fact. The executive officers described below report to the Chief Executive Officer:

- the Corporate Management Officer, who is responsible for marketing (commercial processes), human resources, quality and social responsibility, legal affairs, information technology, asset management, supplies, contracts and new business ventures;
- the Chief Financial and Investor Relations Officer, who is responsible for financial planning, costs and tariffs, raising capital and allocating financial resources to divisions of our company, conducting capital markets and other debt incurrence transactions and managing debt levels, controller, accounting, corporate governance and investor relations, is part of the committee on regulatory matters and is responsible for implementing the committee's guidelines with the support of our division responsible for regulatory matters;
- the Technology, Enterprises and Environment Officer is responsible for environmental management, technological and operational development, quality control of water and sewage, the development, coordination and execution of special investment programs, projects, research and innovation; and
- the Chief Operating Officer for the São Paulo metropolitan region Division and the Chief Operating Officer for the Regional Systems Division, who are responsible for managing the operation, maintenance, execution of planning and works for water and sewage supply systems (including for the services that we provide on a wholesale basis), sales and call center services, and have overall responsibility for the financial and operational performance of their divisions. Moreover, the Chief Operating Officers are part of the committee on regulatory matters and implemented the committee's guidelines in their respective management teams with the support of our division on regulatory matters. The Chief Operating Officers are also responsible for sanitation advisory services to independent municipalities and for mediation and negotiation with communities and local governments, aimed at aligning our interests with the interests of our clients.

Capital Expenditure Program

Our capital expenditure program is designed to improve and expand our water and sewage system and to increase and protect our water sources in order to sustain water security, meet the growing demand for water and sewage services in the state of São Paulo and improve the overall environmental impact of our activities. Our capital expenditure

program has four specific goals with respect to the municipalities we serve:

- (I). to continue to meet the maximum demand for treated water;
- (II). to expand the percentage of households connected to our sewage system;

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- (III). to increase the treatment of sewage collected; and
- (IV). to increase operating efficiency and reduce water loss.

We have budgeted investments in the total amount of R\$12.5 billion from 2016 through 2020. We invested R\$3.5 billion, R\$3.2 billion and R\$2.7 billion in 2015, 2014 and 2013, respectively.

The following table sets forth our planned capital expenditures for water and sewage infrastructure for the years indicated:

	Planned Capital Expenditures					Total
	2016	2017	2018	2019	2020	
	<i>(in millions of reais)</i>					
Water	1,170	1,208	1,119	852	935	5,284
Sewage Collection	466	917	1,044	1,040	1,061	4,528
Sewage Treatment	164	429	571	704	771	2,639
Total	1,800	2,554	2,734	2,596	2,767	12,451

Our capital expenditure program from 2016 through 2020 will continue to focus on achieving our targets by making regular investments to maintain and expand our infrastructure and to reduce water loss in the 364 municipalities we served as of December 31, 2015 and in the municipality of Santa Isabel, with which we signed a water contract that became effective in 2016.

The recent drought has prompted a continuous reduction in the volume of water billed and thus a reduction in revenue. Due to the drought and the need to prioritize construction to mitigate the effects of the water crisis and increase water security in the Metropolitan Region of São Paulo, in 2015 we had to adjust our investment programs for subsequently modify the scheduled amounts of investments for the next few years.

Main Projects of Our Capital Expenditure Program

The following is a description of the main projects in our capital expenditure program.

Metropolitan Water Program

Demand for our water services has grown steadily over the years in the São Paulo metropolitan region and has at times exceeded the capacity of our water systems. On account of the high demand, prior to September 1998, a portion of our customers in this region received water only on alternate days of the week. We refer to this as “water rotation”. In order to address this situation, we implemented the Metropolitan Water Program (*Programa Metropolitano de Água*) to improve regular water supply to the entire São Paulo metropolitan region. This program terminated in 2000 and the water rotation measure was eliminated, but still we have maintained our investment plans for the region.

Since 2000, the Metropolitan Water Program has increased the production capacity in 8.1 m³/s, 5 m³/s of which can be attributed to the Public Private Partnership, or “PPP”, conducted in the Alto do Tietê concluded in 2011, and 2.1 m³/s of which can be attributed to increased production in Guarapiranga System, concluded in 2015.

Aiming to improve the provision of water to the São Paulo Metropolitan Region, we plan on increasing treated water production capacity by approximately 7 m³/s until 2018, with an emphasis on the construction of the São Lourenço System, which shall increase production capacity by approximately 6.0 m³/s. By the end of 2017, we shall also

conclude the interconnection of the Jaguari (part of the Paraíba do Sul Basin) and Atibainha (part of the PCJ Basin) reservoirs.

In 2015, we invested approximately R\$378.1 million in the Metropolitan Water Program. Between 2016 and 2020, we predict investments of over R\$1.2 billion in the Metropolitan Water Program, with a special emphasis on the interconnection of the Jaguari and Atibainha.

Interconnection of Jaguari and Atibainha Reservoirs

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We are interconnecting the Jaguari and Atibainha reservoirs, which is a strategic and priority works project to guarantee secure access to water for the metropolitan region of São Paulo. With investments of R\$555 million in 2016 and 2017, this construction will allow the transfer of up to 8.5 m³/s and an average 5.13 m³/s of water from the Jaguari reservoir of the Paraíba do Sul Basin to the Atibainha reservoir of the Cantareira System, the largest system that provides water to the metropolitan region of São Paulo. In the future, the transfer of water shall also work in the opposite direction, from the Atibainha reservoir to the Jaguari reservoir, optimizing the reservation capacity of both reservoirs, and benefitting the population of the Paraíba Valley. The construction work on the interconnection began in February 2016 and is expected to be concluded in 2017.

Other emergency actions to increase the São Paulo metropolitan region's water security supply are also being implemented. For more information, see “—Business Overview—The Current Water Crisis”.

São Lourenço Project

The metropolitan region lacks water sources, which requires us to obtain water from increasingly distant sources. In order to address this situation, we are, under a PPP contract, currently developing a new supply system called São Lourenço, which will expand our production capacity by 6.4 m³/s and should be able to benefit a population of almost 1.5 million people. The PPP contract was executed in August 2013 and construction began in April 2014. The project is being undertaken by Sistema Produtor São Lourenço S.A., which is a special purpose company controlled by the construction companies Camargo Corrêa Construtora S.A. and Andrade Gutierrez S.A. The new system is expected to begin operation in late 2017. For more information on Public Private Partnerships, see “—Business Overview—Public Private Partnerships”.

The contract amounts to approximately R\$6.0 billion (the estimated amount monetarily restated through December 31, 2015 is approximately R\$7.5 billion) and it has a 25-year term, four years of which will be dedicated to the construction, while the other 21 years will be dedicated to service delivery. These services include the operation and maintenance of the sludge treatment system of the water treatment station and disposal of the waste thus generated; electromechanic and civil maintenance of the untreated water pumping stations, of the water treatment station and the untreated water pipeline; preservation and cleaning, surveillance and property security.

Tietê Project

The Tietê river crosses the São Paulo metropolitan region and receives most of the region's run off and wastewater. The environmental status of the river reached a critical level in 1992. In an effort to reverse the situation, the State of São Paulo created a recovery program designed to reduce pollution of the Tietê river by installing sewage collection lines along the banks of the Tietê river and its tributaries. These lines collect raw sewage and deliver it to our sewage treatment facilities.

We carried out the first phase of the program between 1992 and 1998, when we completed the construction of three additional sewage treatment facilities. This involved total investment of US\$1.1 billion financed by the Inter American Development Bank, or “IADB”, *Caixa Econômica Federal* and us.

The second phase of the project, which was carried out from 2000 through 2008, continued to expand and optimize the sewage system in the São Paulo metropolitan region, focusing primarily on improvements to expand the delivery of raw sewage to the sewage treatment facilities that were built in the first phase. Upon the conclusion of the second phase of the project in 2008, we were able to collect approximately 5,000 liters of raw sewage per second and send it to the five sewage treatment plants in our integrated system for treatment. Total investments in this phase amounted to approximately US\$500 million, financed by the IADB, and BNDES, directly and indirectly

The first and second phases of the Tietê Project contributed to an increase from 70.0% to 84.0% in the sewage collection rate and an increase from 24.0% to 70.0% in the treatment of sewage collected in the São Paulo metropolitan region. As a result, the sewage collection system covered a total of 15.8 million people (5.1 million more than the number of people served when the Tietê Project was initiated), and the sewage treatment system covered 11.1 million people (8.5 million more than the number of people served when the Tietê Project was initiated). The five principal sewage treatment facilities in the São Paulo metropolitan region have an aggregate installed capacity of 18 cubic meters of sewage per second and currently treat an aggregate of 16 cubic meters of sewage per second.

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The third phase of the Tietê Project, initiated in 2010, aims to expand collection levels to 87.0% and sewage treatment levels to 84.0% in the São Paulo metropolitan region. The total estimated cost of the third phase is approximately US\$2 billion, financed by the IADB, BNDES, *Caixa Econômica Federal*, and us.

Following completion of the third phase of the Tietê Project, the sewage collection system, will serve an additional 1.5 million people and the sewage treatment system will serve an additional 3.0 million people. We have invested approximately R\$1.9 billion in the third phase, R\$355.9 million of which was invested in 2015.

Continuing our efforts to eliminate the disposal of *in natura* sewage in the bodies of water of the São Paulo metropolitan region near the areas we serve, we have structured the fourth phase of the Tietê Project. The total estimated cost of this phase is approximately US\$2 billion.

We continued to work on items from the third phase and began in 2014 to implement measures related to the fourth phase, which resulted in approximately R\$377.9 million in total investments in 2015.

Corporate Program for Reduction of Water Loss

The objective of the Corporate Program for Reduction of Water Loss (*Programa Corporativo de Redução de Perdas de Água*) is to reduce water loss by efficiently integrating and expanding existing initiatives in our business units.

This program has a 12 year term that began in 2009. We have invested R\$3.4 billion in this project so far, including R\$525.9 million invested in 2015, and we anticipate total investments of approximately R\$5.5 billion throughout the term of the program. Funding for the program will come from our own resources as well as from credit facilities provided by JICA, *Caixa Econômica Federal* and BNDES.

The program aims to reduce the incidence of water loss from 436 liters per connection per day in December 2008 to 258 liters per connection per day by 2020, which is equivalent to reducing the Water Billed Loss Index from 27.6% in December 2008 to 18.2% in 2020 and to reducing the Water Metered Loss Index (based on measured consumption) from 34.1% in December 2008 to 27.6% in 2020. In 2015, our water loss measured 258 liters per connection per day. In 2015, our Water Billed Loss Index was 16.4% and our Water Metered Loss Index averaged 28.5%.

It is worth noting that the reduction in the water loss indicators in 2015 was due to the intensification of pressure management in the supply systems, an operational practice designed to manage the current water shortage by reducing its impact on the supply of water available to the population. This operational practice has been implemented to serve the current temporary and atypical situation. We note that, when the water supply system returns to being operated as it was prior to the water shortage, there shall be an increase in the pressure in the distribution network which might make it possible for there to be an increase in the loss indicators.

For more information on the measure we have adopted to confront the water crisis, see “—Business Overview—The Current Water Crisis”.

Water Source Program

The Water Source Program (*Programa Mananciais*), created in 2009, consists of various projects that focus on the preservation and improvement of water sources in the São Paulo metropolitan region, especially in the Guarapiranga and Billings reservoirs. The program’s investments are directed mostly towards the creation of infrastructure to collect sewage and transport it to treatment plants in order to reduce the discharge of effluent into water sources. The program also includes the protection of green spaces and the urbanization of shantytowns (*favelas*) and is expected to directly benefit 58,000 families. In 2015, R\$84.2 million was invested in the Water Source Program.

Clean Stream Program

The Clean Stream Program (*Programa Córrego Limpo*), an agreement between the State, acting through our company, and the municipality of São Paulo, aims to decontaminate urban streams in the city of São Paulo by eliminating the discharge of sewage into streams and rainwater runoff routes, cleaning streams and banks, and removing and relocating low income households located on the banks of streams.

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Since 2007, 148 urban streams have been decontaminated, benefiting approximately 2.2 million people. In 2015, we had invested R\$3.8 million in the Clean Stream Program. Part of the investment related to the Tietê Program benefit the Clean Stream Program.

The effects and the consequences of the drought, as well as the difficulty of the state government to remove and relocate low-income households in risk areas, led us to revise the goals of this program. We are currently negotiating with the municipality of Sao Paulo on new goals for 2017 and beyond, taking into account the future budgets of the institutions involved.

Regional Systems Investment Programs

We currently have a number of projects in progress and planned for our Regional Systems. These relate to the abstraction of water as well as to the collection, removal and disposal of sewage. The main projects of the Regional Systems are the following:

Clean Wave Program

The main goals of the Clean Wave Program (*Programa Onda Limpa*) are to improve and expand the sewage systems in the municipalities comprising the Baixada Santista metropolitan region on the southern coast of the state, increasing the sewage collection rate to 95% and treating 100% of this collected sewage, thereby improving the bathing water quality at 82 beaches in the region by the end of the decade. This project is being carried out in two phases, the first of which has already begun and the second of which is in the planning phase. The first phase, which aims to increase the sewage collection rate to 88%, is expected to be completed by 2020. The funds will come from our own resources as well as from loan agreements entered into with JICA and from the Government Severance Indemnity Fund for Employees (*Fundo de Garantia por Tempo de Serviço*), or “FGTS”.

In 2015, we invested R\$172 million in the Clean Wave Program. As a result of our investments, sewage collection in the Baixada Santista metropolitan region increased since the beginning of the program has increased from 53% in 2007 to 71% in 2015. All of the sewage that was collected was also treated.

Towards the goal of increasing sewage collection, and given that we have already installed sewage networks, we are now prioritizing strengthening the connection of our customers to the sewage network. As of December 31, 2015, we completed approximately 94.6 thousand sewage connections. By 2018, we will complete an additional 23 thousand sewage connections.

Under the program’s first phase, we plan to execute by 2020 the expansion and renovation of the Oceanic Sewage Disposal System in the city of Praia Grande, located in the Baixada Santista metropolitan region, is expected to be concluded by 2019.

The second phase of the Clean Wave Program is in planning for the period between 2019 and 2025. We estimate investments of approximately R\$1.8 billion in order to enlarge and implement sewage collection and treatment systems and complete 57 thousand new connections. The goal of the second phase is to provide full coverage of sewage services in the Baixada Santista metropolitan region.

Northern Coast Clean Wave Program

The Northern Coast Clean Wave Program (*Programa Onda Limpa Litoral Norte*) aims to expand the collection and treatment of sewage on the northern coast of the state of São Paulo, intending to benefit 800 thousand people, including the local population as well as tourists that visit the region each year. The program aims to increase the

sewage collection rate in the region from 36.0% in 2008 to 85.0% in 2016, thereby improving the health and well-being of the population and stimulating economic development through an increase in tourism. As of 2015, the sewage collection rate was 56%. In 2015, we invested R\$7 million in this Program.

Coastal Water Program

The Coastal Water Program (*Programa Água no Litoral*) combines various long term activities to expand water production capacity in the Baixada Santista metropolitan region and the southern coast of the state of São Paulo. The program aims to benefit approximately three million people, including both the local population and tourists. It aims to increase the level of reliability of the local systems, eliminating existing and potential deficiencies and irregularities in the water supply. Through this program we aim to increase the availability of treated water and improve the quality of water available to the population. The fund will come from our own funds and financing from *Caixa Econômica Federal*.

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During the first phase of this program, we have focused mainly on increasing water production in order to satisfy demand and improve water quality in the Baixada Santista metropolitan region. In order to reach this goal, we built two water treatment stations, which started operations in 2013: Mambu/Branco, with water treatment capacity of 1.6 m³/s, and Jurubatuba, with water treatment capacity of 2 m³/s.

In 2015, we invested R\$68.3 million in the Coastal Water Program. The second phase of the program is in planning, with the goal of increasing even further the availability of treated water for the local population and tourists and improving the quality of the water available to the population in the Baixada Santista metropolitan region in the coming years.

Other Policies and Programs

Nossa Guarapiranga

In December 2011, we launched the Nossa Guarapiranga project, the main objective of which is to improve the water quality in the Guarapiranga basin, a water source for the São Paulo metropolitan region. The basin serves one million people directly in the areas near Guarapiranga and indirectly serves a further two million people who consume the water from the basin. Our actions in this project were carried out on three fronts: (i) we installed drains to collect residue from rivers in the Guarapiranga basin; (ii) we have developed diagnosis and control services for the withdrawal of water plants that obstruct water extraction; and (iii) we have removed and disposed deposit garbage at the bottom of the basin's dam.

Pró Conexão

In 2012, the State of São Paulo approved a project to subsidize connections to the sewage system for low income families. Initially intended to last 8 years, the project involves capital expenditures of up to R\$349.5 million of which 80% will be provided by the State government and 20% by us. In this period we expect that this program will create 192 thousand new sewage connections benefiting approximately 800 thousand people.

As of December 2015 we completed approximately 23 thousand sewage connections under the *Pró-Conexão* program. We believe that this program will increase the efficiency of our other sewage collection programs and help improve water quality in the region's rivers and basins as well as improve quality of life for low income families.

For more information see "Item 7.B. Major Shareholders and Related Party transactions—Related Party transactions—Agreements with the State

Water is Life

The Water is Life program, established in November 2011, aims to provide water and sewage services to low income and isolated communities in the regions of Alto Paranapanema and Vale do Ribeira. We have expected to cover 81 communities in 30 municipalities, benefiting approximately 15 thousand people. In this project we are responsible for supplying water and for offering technical support to the municipalities, which with financing from the state government, will include installing Individual Sanitary Units (*Unidades Sanitárias Individuais*), a technology better suited for isolated communities. As of December 31, 2015, we concluded projects in 16 communities and we are currently working in 8 others. We executed more than 83 kilometers of networks and pipelines and we began to operate 24 new wells in these communities.

A large part of this work was executed by our own personnel, which considerably reduced the need for investment.

B. Business Overview

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Our Operations

As of December 31, 2015, we provided water and sewage services to 364 municipalities in the state of São Paulo under concession agreements, program agreements, other forms of legal arrangements or without formal agreements. We also supply treated water on a wholesale basis to 5 municipalities located in the São Paulo metropolitan region and urban conurbations. The majority of these concessions have 30 year terms. Due to court orders, we temporarily suspended our services in 3 other municipalities (Cajobi, Iperó e Macatuba). For more information, see “Item 8.A. Financial Statements and Other Financial Information—Legal Proceedings”. Between January 1, 2007 and December 31, 2015, we entered into agreements with 278 municipalities (including our services agreement with the city of São Paulo) in accordance with the Basic Sanitation Law, of which 4 were entered into in 2015. As of December 31, 2015, these 278 municipalities accounted for 78.6% of our gross operating revenues (including revenues relating to the construction of concession infrastructure). In addition to the contracts that have 30 year terms, the municipalities entered into cooperation contracts with the State of São Paulo, delegating the regulation and monitoring of the provision of services to ARSESP. As of December 31, 2015, 53 of our agreements or concessions had expired but we continued to provide water and sewage services to these municipalities and were in negotiations with these municipalities to execute program agreements to substitute the expired concessions. From January 1, 2016 through 2030, 36 concessions will expire.

For more information on laws and regulations related to our concession operations, see “Item 4.B. Business Overview—Government Regulations Applicable to our Contracts”.

Description of Our Activities

As set forth in Article 2 of our bylaws, we are permitted to render basic sanitation services with the goal of providing basic sanitation services to the entire population in the municipalities where we conduct our activities without harming our long term financial sustainability. Our activities comprise water supply, sanitary sewage services, urban rainwater management and drainage services, urban cleaning services, solid waste management services and related activities, including the planning, operation, maintenance and commercialization of energy, and the commercialization of services, products, benefits and rights that directly or indirectly arise from our assets, operations and activities. We are allowed to act in a subsidiary form in other Brazilian locations and abroad. See “—Government Regulations Applicable to Our Contracts—Establishment of ARSESP”. For a description of our operating segments please see Note 24 to our financial statements as of and for the year ended December 31, 2015.

Operating segments are presented in our annual report in a manner consistent with the internal reporting provided to management, comprised of the board of directors and the board of executive officers, pursuant to IFRS 8. Under Brazilian GAAP, prior to our conversion to IFRS, the financial information for construction services was not separately presented and construction costs related to concessions were capitalized within property, plant and equipment. As a result, our management did not review the results of this business. Following our conversion to IFRS, our management decided to continue to exclude the construction results from the management reporting of our revenues and expenses, thus not basing his decisions on discrete financial information for that business. The characteristics described in paragraph 5(b) of IFRS 8 for separate operating segments are thus not fulfilled for this particular business. Nonetheless, after our conversion to IFRS and for IFRS financial statement purposes only, we started to record such results separately as construction revenue and costs under IFRIC 12. Although such information is available discretely, however, it is not analyzed by our management as such and is not the basis for operational decisions.

We set forth below a description of our activities.

Wholesale Operations

B. Business Overview

Wholesale Water Services

We provide water services on a wholesale basis to 5 municipalities located in the São Paulo metropolitan region (Guarulhos, Mauá, Mogi das Cruzes, Santo André e São Caetano do Sul). Agreements to provide water services on a wholesale basis must comply with the Basic Sanitation Law, which designates these services as “interdependent activities” and regulates each stage of the service. The law requires that the service be supervised by an independent agency, stipulates registration of the cost of the service, and requires assurance of payment among the several service providers in order to continue the provision of the services, in accordance with the rules to be published by ARSESP. Our agreements currently comply with the provisions of the Basic Sanitation Law. In 2015, the revenues from wholesale water services were R\$66.6 million. For more information, see “Item 3.D. Risk Factors—Risks Relating to Our Business—We may face difficulties in collecting overdue amounts owed to us by municipalities to which we provide water on a wholesale basis and municipal government entities”.

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Wholesale Sewage Services

Currently, we provide sewage services on a wholesale basis to the municipalities of Mauá, Mogi das Cruzes, Santo André e São Caetano do Sul. We also provided these services to the municipality of Diadema, but in March 2014, we executed a contract to resume direct supply of water and sewage services to the municipality of Diadema. Our agreement with Santo André for these services was executed with the intervention of the Public Prosecution Office. Our agreements with the other municipalities resulted from our environmental efforts and municipal authorities' awareness of environmental issues. Through these agreements, in 2015 we treated approximately 30.6 million cubic meters of sewage from these municipalities. We believe this illustrates our commitment to social and environmental responsibility. In 2015, our revenues from wholesale sewage services were R\$26.5 million.

In December 2008, we entered into a five year agreement for the collection and treatment of 20% of the sewage generated by the city of Guarulhos. We have not yet started to provide these services, and such services will only commence when the works on linking the Guarulhos sewage to our sewage system are finalized. These works are the responsibility the Guarulhos sanitation company.

Water Operations

Our supply of water to our customers generally involves abstraction of water from various sources, subsequent treatment and distribution to our customers' premises. In 2015, we produced approximately 2,466.6 million of cubic meters of water. The São Paulo metropolitan region (including the municipalities to which we supply water on a wholesale basis) currently is, and has historically been, our core market, accounting for approximately 67.9% of water invoiced by volume in 2015.

The reduction in the volume of water produced in 2015, as compared to 2014, is a result of the water crisis that affects our area of operation. For more information, see "Item 3.D. Risk Factors—Risks Relating to Our Business: The measures we took to mitigate the effects of the drought resulted in a significant decrease in the volume of water billed and revenues from services we provide, which had a material adverse effect on our company and that may worsen if the drought escalates in severity" and "—The Current Water Crisis". The following table sets forth the volume of water that we produced and invoiced for the periods indicated:

	Year ended December 31,		
	2015	2014	2013
	<i>(in millions of cubic meters)</i>		
Produced:			
São Paulo metropolitan region	1,679.4	2,001.1	2,220.6
Regional Systems	787.2	839.3	832.0
Total	2,466.6	2,840.4	3,052.6
Invoiced:			
São Paulo metropolitan region	1,084.3	1,172.4	1,206.9
Wholesale	215.5	256.8	299.0
Regional Systems	613.9	639.4	628.1
Total	1,913.7	2,068.6	2,134.0

The difference between the volume of water produced and the volume of water invoiced generally represents both physical and non physical water loss. See "—Water Loss". In addition, we do not invoice:

- water discharged for periodic maintenance of water transmission lines and water storage tanks;

- water supplied for municipal uses such as firefighting;
- water consumed in our own facilities; and

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- estimated water loss associated with water we supply to shantytowns (*favelas*).

Seasonality

Although seasonality does not affect our results in a significant way, in general, higher water demand is observed during the summer and lower water demand during the winter. The summer coincides with the rainy season, while the winter corresponds to the dry season. The demand in the coastal region is increased by tourism, with the greatest demand occurring during the Brazilian summer holiday months.

Water Resources

We can abstract water only to the extent permitted by DAEE pursuant to water right granted by it. Depending on the geographic location of the river basin or if the river crosses more than one state (federal domain), the approval of ANA a federal agency under the Ministry of the Environment is required. We currently abstract substantially all of our water supply from rivers and reservoirs, with a small portion being abstracted from groundwater. Our reservoirs are filled by impounding water from rivers and streams, by diverting the flow from nearby rivers, or by a combination of both methods. For more information on water usage regulation, see “—Environmental Matters—Water Usage”.

In order to supply water to the São Paulo metropolitan region, we rely on 20 reservoirs of non treated water and 254 reservoirs of treated water, which are located in the areas under the influence of the eight water producing systems comprising the interconnected water system of the São Paulo metropolitan region. The total capacity of the water sources available for treatment in this area is 75.5 m³/s, not including an additional 6.5 m³/s resulting from the emergency construction work conducted by us in 2014 and 2015. Total current installed capacity is 75.8 m³/s and can be distributed to the São Paulo metropolitan region. Average verified production for the interconnected water system of the São Paulo metropolitan region was 52.0 m³/s during 2015. The Cantareira, Guarapiranga and Alto Tietê systems produce 79.0% of the water we distributed in the São Paulo metropolitan region in 2015.

In 2015, the Cantareira system accounted for 27.1% of the water that we supplied to the São Paulo metropolitan region (including the municipalities to which we supplied water on a wholesale basis), which represented 67.3% of our gross operating revenues (excluding revenues relating to the construction of concession infrastructure) for the year. For more information, see “Item 3.D. Risk Factors—Risks Relating to Our Business—We are exposed to risks associated with the provision of water and sewage services”.

For further information on droughts see “Item 3.D Risk Factors—Risks Relating to Our Business—The measures we took to mitigate the effects of the drought resulted in a significant decrease in the volume of water billed and revenues from services we provide, which had a material adverse effect on our company and that may worsen if the drought escalates in severity” and “—The Current Water Crisis”.

Current river basin committees are authorized to charge both for water usage and the dumping of sewage into water bodies. We participate in the decentralized and integrated management of water resources established by the National Policy on Water Resources. We are represented by 158 employees on the 21 State River Basin Committees and the four Federal Committees that act in the state of São Paulo and in the National and State Councils on Water Resources.

The following table sets forth the water production systems from which we produce water for the São Paulo metropolitan region:

Production Rate⁽¹⁾		
2015	2014	2013

(in cubic meters per second)

Water production system:

Cantareira

14.1

23.7