STATEMENT OF QUALIFICATIONS FOR WATER AND SEWER CONCESSION

PREPARED FOR

City of Allentown, Pennsylvania

AMERICAN WATER

August 8, 2012

AMERICAN WATER

Mark Strauss
Sr. Vice President – Corp. Business Development
1025 Laurel Oak Road
Voorhees, NJ 08043
mark.strauss@amwater.com
www.amwater.com
P 856-309-4530
F 856-309-4525

August 8, 2012

Mr. Jason Brockman
Senior Managing Consultant
Public Financial Management, Inc.
One Keystone Plaza
Suite 300
North Front & Market Streets
Harrisburg, PA 17101-2044

RE: Submittal of Qualifications to the City of Allentown

Dear Mr. Brockman:

We understand the motivation of Mayor Pawlowski to keep the City of Allentown on solid footing, and we applaud his action and leadership to consider alternative solutions such as leasing the city's water and wastewater assets to address the city's financial issues. We know that the city's unfunded pension liability is the driver and that any partnership must come with certain assurances that labor, rates, and customer service goals, among others, are met.

We believe you will find our qualifications to be of a high standard and that our team approach is straightforward with minimal execution risk. The team is simply and solely American Water. There are many private equity funds that can generate the upfront payment. Some of these even have a water entity in their portfolios. But none can match the heritage of American Water. Keeping in mind that this is a 50-year lease, once the upfront check is received by the City, it will live with the operational entity for many years to come. Further, your union employees will literally live this experience. In our approach you receive both the financial support as well as an experienced operator who has a very good relationship with its customer base and with the SEIU. We are a stable company with a robust business model that should offer peace of mind to your workforce. Our large footprint in Pennsylvania will also serve the city well.

Further, we are very aware of the timeline that has been announced and that a transaction needs to be completed in time for the city's next budget cycle. The team approach we

AMERICAN WATER

propose, based on our experience with concession transactions, should help expedite what might otherwise be a complicated and prolonged process.

Our strength is ready to be shared through partnering with Allentown so that the City can enjoy prosperity and a secure future. We will do our best to address any questions you might have and look forward to your decision later this month.

Sincerely,

Mark Strauss
Senior Vice President
Business Development and Strategy

Cc: Mr. Scott Shearer – Managing Director, Public Financial Management
Ms. Kathleen Carney – VP of Business Development, American Water

Table of Contents

Proposer Information **1**
I. Description of Prospective Proposer 1
II. Roles of Team Members and Key Personnel 1
III. Operator 11
IV. Contact Person 11
V. Controlling Interest 11
VI. Expected Advisors 12
VII. Comparable Projects 12
VIII. Team Member References 15
IX. References 15

Technical Capability **17**
I. Operations and Maintenance Expertise 17
II. Customer Service 29
III. Safety and Security 33
IV. Capital Improvements 38

Financial Capability **40**
I. Capacity to Make Upfront Payment, Maintain the Concession Assets 40
II. Ability to Raise Financing 41

Proposer Information

I. Description of Prospective Proposer

American Water Works Company, Inc. (American Water) is the respondent to Allentown's Request for Qualifications. American Water is the largest publicly traded water and wastewater utility in the United States and provides approximately 15 million people with drinking water, wastewater and other water-related services in over 30 states and 2 Canadian provinces through its regulated subsidiaries, market-based operations, and other services to public- and private-sector clients. Our current plan is to be the only financier of the project.

American Water employs more than 7,000 employees. Of the more than 3,600 union employees represented by 19 different collective bargaining units within American Water, 8.6 percent are represented by the Service Employees International Union (SEIU) and are located primarily in Pennsylvania and New Jersey. These valued employees are intrinsic to our success and solid reputation and are the heartbeat of American Water.

The second team member will be American Water Enterprises, a wholly owned subsidiary of American Water, which offers operations and maintenance services to approximately 90 clients throughout North America through its Contract Services Group.

Since both team members are affiliated entities within a single corporate hierarchy, there is an established legal and governance structure. We understand that changes to the composition of a team after the qualification process is complete are subject to review by and consent of Allentown.

II. Roles of Team Members and Key Personnel

Team Members

The construct of our proposed team is streamlined and straightforward.

American Water will serve as the project leader and financing arm, utilizing the strength of its balance sheet to provide debt and equity financing to fully support the concession. We have provided details of American Water's financial strength in "Section 3. Financial Capability."

A Special Purpose Entity (SPE) would be created by American Water to serve as the investment and service vehicle through which the proposed 50-year partnership would be administered and through which all financing would flow. Allentown would lease its water and wastewater system assets to the SPE in return for the SPE's payment of an upfront fee and other mutually negotiated financial commitments and operational responsibilities for the water and wastewater systems. To operate Allentown's utilities, the SPE would, in turn,

engage American Water Enterprises to supply the water and wastewater operations and capital improvements scope of work.

Such an arrangement achieves two important goals for Allentown:

1. Its structural simplicity provides the city with assurance that its timeline will be met.
2. Its minimized structure keeps transaction costs lower for both parties. There are few water-only companies today, if any, with the in-house financial capacity American Water brings to Allentown coupled with the long history of successful operations.

It is difficult to say at this point what aspects of the capital improvement program to be performed over the course of the agreement would be best met by sub-contractors due to the need for highly specialized services, local affiliations, or cost effectiveness. As such we wish to reserve the right to augment our capabilities with firms we find to be necessary. It is our practice to work, whenever possible, with local subcontractors, including women-owned and minority-owned business entities. Because of our size and scale, we have long-standing relationships with most national and regional, and many local, engineering and construction firms who participate on scores of American Water capital projects every year.

Technical Capacity. American Water has a history of over 125 years of successful provision of water-related services, recognition as a leader in the water industry and, as the largest investor-owned water provider, is about four times the size of our nearest competitor. It has provided guarantees for projects valued in the hundreds of millions of dollars.

American Water Enterprises has provided contract operations to a wide variety of public sector entities since 1992, some with contract terms of up to 50 years. It has led engineering and construction teams in some of the largest design-build-operate (DBO) contracts that have been undertaken in the U.S.

Taken together, the team offers Allentown overwhelming assurance that all technical obligations required by any concession agreement will be met.

Financial Capacity. American Water is responsible for the planning and funding of capital improvements needed to maintain the water and wastewater infrastructure that its residential, commercial and industrial consumers depend upon. To accomplish this, American Water has used cash generated from operations, borrowings under our revolving credit facility and commercial paper programs and issuances of long-term debt and equity securities to prudently finance at satisfactory interest rates approximately $4 billion of capital investment projects over the past five years. The company plans to fund between $800 million and $1 billion more in capital improvements each year for the next five. American Water has clear financial capacity to meet all commitments associated with Allentown's proposed project.

Key Personnel

The level of technical resources detailed in this section comprise of some of the best engineers and operators in the country from both the field and corporate levels. In fact, American Water operators have won more Director's Awards of Recognition from the Partnership for Safe Water for water quality than any other water company in the country—approximately one third of the total.

Our leading scientist, Dr. Mark LeChevallier, is the recipient of the 2012 Abel Wolman Award of Excellence from the American Water Works Association (AWWA). This award is one of AWWA's highest honors and is presented annually to one individual whose career in the water works industry exemplifies vision, creativity, and excellent professional performance.

The individuals listed below represent key employees of American Water and its advisors for this transaction. They, or employees of equal competence, will hold principal responsibility for undertaking and completing all due diligence, negotiations, financing, management, and operations activities relating to Allentown's water and wastewater systems.

▪ ***Kathleen E. Carney, Vice President of Corporate Business Development.*** Ms. Carney serves as team leader and corporate contact for the Allentown response and has over 30 years of business and leadership experience that span three industries and several of *Fortune's* Top 50 companies. Ten of those years have been with American Water in the capacities of business development and marketing, directing business efforts that match client needs with the company's capabilities.

She studied economics at Lafayette College and received her bachelor of arts in marketing from North Central College in Illinois and a master of business administration from Illinois Benedictine University, with further leadership and managerial training completed at Oxford University, England.

▪ ***James E. Cowley, P.E., Director- Special Projects, Contract Services Group.*** Mr. Cowley has over 29 years of experience working on a wide range of projects that encompass the water cycle from source of supply, through treatment, to the delivery of potable water to the customer's tap. It is anticipated that, Mr. Cowley, or an employee of equal standing, will be designated as the project manager.

His current responsibilities as director of special projects includes inventorying existing key processes and systems; developing operational and technology implementation strategies; practices that balance efficiency, risk, and service levels; establishing operational metrics that promote rapid implementation; and continual improvement and operational resiliency. He has been operationally responsible for managing multiple water supply and treatment

facilities ranging in size up to 165mgd. His most recent assignment has been to lead a team for the operational commissioning of New York City's Croton Water Filtration Plant.

He holds a bachelor of science in civil engineering from the New Jersey Institute of Technology and is a licensed professional engineer in New Jersey. He is assigned to the Contract Services Group's New Jersey headquarters.

▪ ***Robert F. Schnitzler, Jr. Manager of Production, Pennsylvania.*** Mr. Schnitzler directs the personnel, capital resources and business processes that are engaged in the production of drinking water and treatment of wastewater for Pennsylvania American Water across Central and Southeast Pennsylvania. He is responsible for 19 water treatment plants and a wastewater plant serving 176,000 customers and a population of approximately 500,000. Mr. Schnitzler has managed the construction and startup of numerous water treatment plants, pump stations, pressure regulating stations, storage tanks and ground water sources. He has more than 28 years of experience in the water and wastewater industry.

Mr. Schnitzler earned a bachelor of science degree in environmental resource management from The Pennsylvania State University in University Park. He is a certified water treatment plant operator in the Commonwealth of Pennsylvania and a member of the American Water Works Association.

▪ ***Gregory Cobourn, Regional Vice President of Contract Services Operations.*** Mr. Cobourn has held several senior positions in the water resources industry, from facility manager to director of project development to vice president of operating services. As head of operating services, Mr. Cobourn is responsible for all contract operations, establishing corporate performance standards, reporting the progress of operations to the board of directors, budgeting, facilitating monthly operational meetings, assisting managers by providing technical and management support, negotiating contracts, and providing client service.

In the project development role, Mr. Cobourn was ultimately responsible for all opportunities within American Water contract services group. The project development department includes mechanical, civil, chemical engineers, operations specialists, and financial analysts who develop technical and financial solutions for new business opportunities. As facility manager, he managed several large wastewater treatment facilities, lift stations, land application programs, and pretreatment programs. He was responsible for employee supervision, operations and maintenance activities, and client relations.

He earned a bachelor of science degree in environmental systems technology from Southern Illinois University. He holds an Illinois Class II Sewage Treatment License, a Missouri Class A Sewage Treatment License, an Indiana Class IV Wastewater Treatment License, an Indiana

Class D Industrial Wastewater Treatment License, and a Kentucky Class IV Wastewater Treatment License

▪ ***Peter Keenan, P.E., Director, Water/Wastewater Engineering Design Services.*** Mr. Keenan is the director of American Water's corporate engineering design team. In this role, he oversees a multi-disciplinary team of engineers and technicians in the design of water and wastewater treatment and conveyance facilities across the U.S. He has over 20 years of experience in the design, evaluation, and operation of water and wastewater treatment facilities, including numerous facilities utilizing the same treatment technologies in use at the Allentown's plants.

Mr. Keenan has experience with many advanced water treatment process technologies, including high rate processes such as plate settlers, superpulsators, dissolved air floatation, and ballasted flocculation, as well as membrane, ion exchange, and advanced oxidation technologies. He also has extensive experience with wastewater treatment technologies, including both suspended and attached growth biological processes, biological nutrient removal, and tertiary treatment. Mr. Keenan's experience has been put to use in the preparation of hydraulic and process models and the management of full-scale testing at water and wastewater treatment facilities to identify factors limiting treatment plant capacity and performance. In addition, he has overseen several energy optimization studies for both water and wastewater systems, and has helped devise and implement practical solutions for minimizing the impact of wet weather flows on treatment performance.

Mr. Keenan received his bachelor's degree in civil engineering from Villanova University and a master of science in environmental engineering from the University of Massachusetts at Amherst. He is a licensed professional engineer in the state of Pennsylvania.

▪ ***John Gallagher, P.E., Director, Water/Wastewater Construction Services.*** Mr. Gallagher has over 28 years' experience in engineering and construction management of large and complex water resources projects. Mr. Gallagher is responsible for the overall management of American Water's major construction program as well as directing project managers and field inspection personnel assigned to major construction projects. He has an in-depth knowledge of water/wastewater construction agreements, program and project management, contract administration, project delivery systems and site management. Mr. Gallagher has directly managed projects ranging up to $60 million in value..

Prior to this position, Mr. Gallagher was responsible for administering the American Water annual materials contract-purchasing program involving the procurement of $35 million of water distribution related materials, such as pipe, valves, hydrants, meters, and service connections. Additionally, he developed a national fleet program including the acquisition, distribution and maintenance for all American Water vehicles. He also developed contract

agreements and has made presentations to national audiences regarding the use of alternative design/build and construction management contract approaches.

He received a bachelor's degree in civil engineering from the University of Delaware, a master's in business administration from Syracuse University, and a master of science in civil engineering from Drexel University. Mr. Gallagher is a registered professional engineer in Pennsylvania and a member of the American Society of Civil Engineers and the Design Build Institute of America.

▪ ***James Chelius, P.E., Director, Water/Wastewater Asset/Capital Planning.*** Mr. Chelius provides direction, governance, support and training to corporate and regional staff for implementing asset planning programs. He directs American Water's comprehensive planning program that delivers quality engineering planning studies designed to assess supply, treatment and distribution system needs and that identify infrastructure improvement projects which provide the foundation of the company's capital investment program. He also is responsible for the development of the company's asset investment strategy which provides direction on prioritizing annual capital investment. He leads several initiatives in the development of asset management practices, with the overall objectives of optimizing asset lifecycle and investment, improving the availability and quality of information on American Water's assets, and implementing strategies and tools for analyzing and optimizing asset performance.

Prior to his current role, Mr. Chelius managed project teams tasked with implementing asset management and projects using geographical information system technology designed to improve efficiency and effectiveness of the asset lifecycle process. He also held the position of senior planning engineer with American Water where he was responsible for conducting and managing numerous engineering projects and studies associated with American Water's Comprehensive Planning Study program, which provides thorough analyses of the present and future capital facility needs of American's operating utilities.

He received a bachelor of science degree in basic sciences, with a concentration in metallurgy, and a master of science in water resources engineering from Villanova University.

▪ ***Michael E. McDonald, P.E., Senior Water/Wastewater Planning Engineer.*** Mr. McDonald addresses the spectrum of water supply, demand, operational and efficiency issues impacting water and wastewater utilities. His current role involves engineering evaluations of entire water systems, including process improvements, supply evaluation and recommendations, demand projections, storage and distribution analyses with the aid of hydraulic modeling, and energy/operations efficiency evaluations. He has 20 years of construction management and detailed design experience in extensive capital improvements including pump stations, water treatment plants, pipelines and wastewater conveyance systems.

He has completed evaluations of several of American Water's systems and identified process and energy optimization savings, as well as recommendations for capital investments to meet future regulations and projected demands. A recent evaluation included an energy use audit and process optimization involving three water treatment plants serving the same system. The assessment addressed savings with energy and demand usage as well as operational savings.

He received a bachelor of science in geology from the University of Massachusetts at Amherst and holds a master of science degree in civil engineering from Stanford University. He is a registered professional engineer in Massachusetts.

▪ ***Dr. Mark W. LeChevallier, Director, Innovation & Environmental Stewardship.*** Dr. LeChevallier directs a staff of 18 in both research and environmental compliance programs. Research areas have included bacterial regrowth, disinfection of biofilms, corrosion, bacterial nutrients, AOC measurement techniques, biological treatment, mycobacterium, microbial recovery and identification, modeling and impact of pressure transients on water quality, and detection, treatment and survival of *Giardia* and *Cryptosporidium*.

As director of environmental compliance programs, he has been responsible for the development of environmental management plans for more than 1,000 operating centers, environmental audits to ensure compliance, development of a national cross connection control program for American Water, and implementation of environmental stewardship and greenhouse gas control programs. He has authored or coauthored over 100 research papers, most in peer-reviewed journals. Several of his papers have received awards from the American Water Works Association for outstanding contributions to the science of water treatment.

Dr. LeChevallier received his bachelor of science and master's degrees in microbiology from Oregon State University in 1978 and 1980. He worked as a research associate at Montana State University where he received his doctorate in microbiology in 1985.

▪ ***Dr. Orren Schneider, Senior Environmental Engineer, Innovation and Technology.*** Dr. Schneider is involved with research leading to optimization of water treatment and distribution system operations. Dr. Schneider has been a technical manager with expertise in evaluation and design of advanced coagulation, clarification, filtration, disinfection, and membrane technologies for water treatment. He has extensive experience with pilot plants specializing in collection and analysis of data for scale-up to full-scale operations. He has shown proven abilities in development of new water treatment facilities, water quality evaluation, and treatment optimization.

Dr. Schneider is a technical resource for American Water and is routinely called upon to provide guidance and ideas for troubleshooting of existing treatment processes and for business development opportunities. He has conducted many applied research studies and is

well integrated with research community having initiated and led research projects and pursuits. Dr. Schneider has been either principal investigator or co-investigator on approximately $2 million worth of funded research projects. He has made numerous presentations on a wide variety of topics related to drinking water treatment and has published many papers as author or co-author.

Dr. Schneider is a referee for a number of peer-reviewed publications: The Journal of the American Water Works Association, Ozone Science and Engineering, the Journal of Water Supply: Research and Technology (Aqua), and Science of the Total Environment

- ***Dr. Yanjin Liu, P.E., Environmental Engineer.*** Prior to joining American Water, Yanjin worked as a plant engineering supervisor at Washington Suburban Sanitary Commission. He is a certified wastewater operator and superintendent.

Dr. Liu earned a bachelor's degree in structural engineering and a master's degree in hydraulic Engineering at Dalian University of Technology in China. He earned his doctorate in Environmental Engineering at North Carolina State University.

- ***Meg Neafsey, Vice President, Customer Service.*** Ms. Neafsey leads American Water's integrated customer service center, which has locations in Alton, Illinois, and Pensacola, Florida. The center provides call handling, billing, and collections activities, as well as assistance and management of local and company-wide projects for subsidiaries. Under her leadership, American Water has improved customer satisfaction scores, consistently surpassed industry standards for service level, and led the development of an online customer self-service tool.

Before accepting her current role, she was an enterprise architect for American Water's ITS team. She has more than 25 years of experience in the water industry, most recently as director of customer relationship management for the call center at the former Elizabethtown Water systems, now part of New Jersey American Water Company.

She holds a bachelor's degree in management science from Kean College and a master's in business administration from Georgian Court College.

- ***Jordan Mersky, American Water Northeast Division, Deputy General Counsel.*** Mr. Mersky is the principal transaction counsel for American Water's Northeast Division and also handles most of the contract and property work. Mr. Mersky also works as transactional counsel for American Water, recently leading the teams responsible for the sale of American Water's Arizona and New Mexico subsidiaries and its exchange of various operating assets with Aqua America.

Mr. Mersky has 16 years experience in transactional law. Prior to joining American Water, he was general counsel for UM Holdings, a private investment company. He began his career as

part of the mergers and acquisitions team at the New York office of Shearman and Sterling, an international law firm.

He graduated summa cum laude from American University's Washington College of Law and has a degree in political science from the University of Chicago

- ***William D. Rogers, American Water Vice President and Treasurer.*** Mr. Rogers leads the company's long-term and short-term financing, corporate planning, and investment analysis activities. He also oversees employee benefit plan trust asset investments and Enterprise Risk Management efforts. He leads the financial evaluation and analysis of new business opportunities.

Mr. Rogers has more than 20 years of financial experience. Prior to American Water, he was the chief financial officer for NV Energy, an investor-owned utility in Las Vegas serving 1.5 million electric and gas customers, with annual revenues of $3.3 billion. He had previously served as vice president of finance, risk and tax, as well as corporate treasurer. Prior to joining NV Energy, Rogers was a managing director of capital markets for both Merrill Lynch and JPMorgan Chase in New York. Before beginning his finance career, Rogers served as a captain in the Army Corps of Engineers for five years.

Mr. Rogers holds an MBA in accounting and finance from Duke University. He is also a distinguished graduate of the U.S. Military Academy with a bachelor's degree in engineering and economics.

- ***Michael Hoffman, Senior Manager, Corporate Finance.*** Mr. Hoffman is responsible for the financial evaluation and analysis of new business opportunities. Prior jobs at American Water included rates and regulatory responsibilities, revenue budgeting and long-term financing activities across operating companies.

Mr. Hoffman has more than 15 years of financial experience. Prior to American Water, he worked in Goldman Sachs' investment banking division performing structured finance, mergers and acquisitions, real estate evaluations and other strategic activities. Mr. Hoffman also worked for Charterhouse Group International, a leading private equity fund, and for Interliant, a Charterhouse portfolio company focused on providing internet hosting infrastructure and services.

Mr. Hoffman graduated summa cum laude from the University of Illinois with a bachelor's degree in accounting. Mr. Hoffman passed the CPA exam immediately after graduating college and also passed the Series 63 exam while working at Goldman Sachs.

- ***William L. Komianos, Senior Director of Operational Risk Management.*** Mr. Komianos is responsible for security, health and safety, and event management, directing a staff of 65 professionals across American Water and has more than 30 years experience in these areas.

Prior to joining American Water, he served as vice president of health, safety and environmental compliance for Hamon-Research Cottrell and Air and Water Technologies. Prior to that, he held positions as manager of health, safety and security for Johnson & Johnson Consumer Products and as a director for the northeast region of Clayton Environmental Consultants.

Mr. Komianos is chair of the Water Sector Coordinating Council, which focuses on protecting water systems from threats, and served as co-chair of the Critical Infrastructure Partnership's Advisory Council Metrics Workgroup and the Water Sector Strategic Planning Working Group. He is past chair of the National Association of Water Companies' Safety and Security Committee. He is also a member of the American Industrial Hygiene Association, the American Society of Safety Engineers and American Water Works Association.

Mr. Komianos holds a bachelor's degree in environmental health from Colorado State University. He is a Certified Industrial Hygienist and a Certified Safety Professional.

▪ ***Brian McCord, PG, Director Environmental Health and Safety.*** Mr. McCord is responsible for the development and implementation of the environmental management and health and safety systems at water treatment and wastewater facilities for American Water. His job includes supervising three environmental, health, and safety managers with reporting responsibilities to dedicated field services and facility personnel. Mr. McCord has over 20 years experience in the geologic, water resource, health and safety, and environmental fields as a senior manager or division director.

He holds a bachelor of science in geology from San Diego State University and a master of science in geology from California State University, Northridge.

▪ ***Andrew L. Swope, Partner, K&L Gates.*** Mr. Swope's practice concentrates on complex commercial matters, including both litigation and transactions, with an emphasis in construction, public private partnerships and energy law. His experience includes drafting and negotiating of design-build contracts, construction contracts, engineering contracts, equipment supply agreements, fuel supply agreements, operation and maintenance agreements, power purchase agreements, lease agreements and other commercial contracts.

Litigation experience includes representation of owners, general contractors and subcontractors in arbitration proceedings, lien proceedings, civil litigation in a variety of courts and administrative proceedings. Mr. Swope also has developed substantial experience representing owners and contractors in the context of bankruptcy proceedings and addressing the unique issues that are faced by owners and contractors whose projects are impacted by a bankruptcy or other financial difficulties.

III. Operator

Operations and maintenance will be provided through American Water Enterprises. It enters into public-private partnerships, concessions, leases and other contractual relationships for the provision of a variety of DBO and operation and maintenance services at water and wastewater facilities. Clients include the United States military, municipalities and regional authorities, as well as a variety of private-sector entities. American Water Enterprises holds approximately 90 contracts for these services across the United States and Canada, varying in size and scope. Included in these are nine 50-year contracts with the Department of Defense for the operation and maintenance of the water and wastewater systems on military bases.

American Water has integrated its wealth of experience, skills, systems, and financial strengths into best industry practices that assure reliable, effective water services across all subsidiaries, clients, and customers, including those of American Water Enterprises. This ability to draw on corporate experience and resources is an underlying strength in our delivery of successful public-private partnerships.

American Water Enterprises also brings to each public-private partnership it enters into a robust corporate technology group that is involved in the testing and implementation of many cutting-edge industry innovations that help reduce or control production costs and/or meet or exceed stringent water-quality standards. This group also works closely with the Environmental Protection Agency.

IV. Contact Person

The contact person for American Water is:

Kathleen E. Carney
Vice President of Corporate Business Development
American Water
1025 Laurel Oak Road
Voorhees, NJ 08043
856-309-4530 (office)
856-912-4268 (cell)
kathleen.carney@amwater.com

V. Controlling Interest

There are no individuals or companies who hold a major or controlling interest in American Water. The company is publicly traded on the New York Stock Exchange under the ticker symbol “AWK.”

As noted above, American Water Enterprises, which will execute on the operations and maintenance scope of work, is wholly owned by American Water.

As presently envisioned, the SPE will also be a wholly owned American Water entity.

VI. Expected Advisors

American Water will utilize K&L Gates as the legal advisor for the project. The company is located at K&L Gates Center, 210 Sixth Avenue, Pittsburgh, PA 15222-2613. The phone number is 412.355.6500; the fax number is 412.355.6501. The company website can be accessed at www.klgates.com. Principal contact is Andrew Swope, Partner.

K&L Gates has helped municipal and private sector clients form and manage some of the largest and most complex public-private partnerships using a multidisciplinary approach to legal issues across the range of legal practices available within the firm and with sensitivity to the cultural differences between public and private decision-making. The firm has extensive experience with structuring, documenting and/or implementing numerous joint public-private transactions, including concession agreements, development agreements, disposition and development agreements, operating agreements, reimbursement agreements, restrictive covenants, and conditions of approval with municipalities and redevelopment agencies.

Of relevance to Allentown, K&L Gates was deeply involved in proposed concession/lease transactions involving the Pennsylvania Turnpike, the City of Harrisburg and the City of Pittsburgh. The firm has familiarity with the legal requirements imposed by the Pennsylvania Constitution, the Acts of the General Assembly, and regulatory issues associated with the authorization for and execution of such transactions.

VII. Comparable Projects

The projects listed below offer experience comparable to that sought by Allentown in the areas of concessions, operational size and scope, technical aspects, and/or contract length. Additional comments in blue italic, describing relevance, accompany the examples.

The following two projects are examples of long-term concession agreements, the first of which involves an upfront payment and calls for significant investment in system capital improvements while the second provides an annual fee to the city.

Elizabeth, New Jersey, Water and Wastewater Systems Concession. For this project, American Water and the City of Elizabeth received the 2012 Outstanding Partnership Award from the U.S. Conference of Mayors for achieving significant improvements to the city's water and wastewater systems. Elizabeth entered into a 40-year concession agreement with a subsidiary of American Water for the operations, maintenance and management of the water system, which serves a population of 125,000 in 1998. Four years later, a separate 20-year contract for the wastewater system was signed with American Water.

Under the water agreement, American Water made $50 million in concession payments to the city between 1998 and 2000, stabilizing property taxes and decreasing system debt. It also guaranteed at least $58 million, spread over 40 years, for improvements to water infrastructure. American Water initiated a comprehensive maintenance program, invested in system-wide meter replacements using automated meter reading touch-pad capability, developed an emergency management plan and a system operation and maintenance manual, and assumed all billing and collection functions for both water and wastewater service. The partnership guaranteed stable water rates for the city with a 1.4 percent average annual base rate increase over the life of the contract.

> *"Beyond the financial benefits to the city, this public-private partnership has allowed the administration to focus its attention on other priorities in our ongoing commitment to Elizabeth's future."*
>
> ***Elizabeth, New Jersey, Mayor J. Christian Bollwage***

For the wastewater system, American Water will ultimately invest $3 million to rehabilitate the brick collection system.

Edison, New Jersey, Water System Concession. In 1997, American Water entered into a 20-year concession agreement with the Township of Edison for the operation, maintenance and management of the township's 70-year-old water distribution system, which serves an estimated population of 100,000 people. There was an initial concession payment of more than $5 million, with subsequent annual payments to total $9.6 million. In the first three years of the agreement, American Water cleaned and lined 117,000 feet of the distribution system, looped dead-end mains and replaced some older four-inch mains--all of which not only reduced complaints but increased the system's fire fighting capability. System improvements made by American Water have reduced water losses significantly.

The following are two examples of 50-year contracts that have been awarded to American Water under the U.S. Department of Defense's military privatization program. Both involve sizeable capital improvement projects and execution of contract operations. The company holds nine such contracts for military base operations.

Fort Rucker, Alabama. American Water is responsible for operation and maintenance of an activated sludge wastewater treatment plant and an extended aeration treatment plant, a sewer collection system and a potable water supply at this Army base. Other responsibilities include system capital investment, regulatory and environmental compliance, planning, and asset recapitalization.

Fort Sill, Oklahoma. American Water is responsible for the operations and maintenance of a three-stage wastewater treatment plant, collection system, and potable water distribution system. Other responsibilities include system capital investment, regulatory and environmental compliance, planning, and asset recapitalization. American Water employed

innovative ways to optimize the facility, and the resulting efficiencies resulted in operational savings. Immediate impacts include the reduction of chemical usage, which cut by half the amount of dried tons of sludge disposed of annually.

The following two facilities, both operated under long-term contracts and both renewed, are similar in size and feature comparable technologies to those found at the Allentown wastewater facility. Both examples include the project management of significant capital improvements and successful intervention with environmental regulatory agencies on each client's behalf. Further technical information about the projects is included under the "Technical Capabilities" section.

Lincoln, Illinois, Wastewater Treatment Plant. This 33 million gallons a day (mgd) wastewater facility has been operated by American Water's Contract Services Group since November 1990. The city has renewed the contract twice; the current term will end in April, 2015. During the term of the contract, the plant was significantly expanded in 2004, including new headworks, extra aeration bays, an added final clarifier, a RAS station, conversion of two trickling filters into aerobic digesters, conversion of two anaerobic digesters into sludge holding, and the addition of a belt filter press. American Water's operating subsidiary undertook the expansion as a design-build project. The collection system consists of 100 miles of main ranging in size from 8 inches to 96 inches, 11 lift stations, and two combined sewer outfalls.

St. Charles, Missouri, Wastewater Treatment Plants. American Water is currently providing project management for major capital improvements at this project's two wastewater facilities. At the Mississippi River plant, a major expansion to increase plant capacity by 28 percent was begun in 2011, with the $23 million project scheduled for completion in September, 2013. The Missouri River plant is also undergoing an $18 million expansion that will bring its design flow to 24mgd. Both plants will see the installation of sophisticated new equipment for UV disinfection as a result of more rigorous standards from the EPA and Missouri Department of Natural Resources for the removal wastewater bacteria.

The following two water facilities are relevant in demonstrating American Water's financial capacity to guarantee large construction projects and represent treatment plants of similar size and process technology to Allentown's plant, where American Water's optimization expertise resulted in significant operating savings. Both demonstrate American Water's ability to utilize new technologies to reduce costs.

Seattle, Washington, Tolt Water Treatment Plant. American Water was the project guarantor for this $107 million, 120mgd DBO project. The design utilized a high-rate filtration which offered a smaller facility footprint with a filtration rate twice that was previously approved by the Washington State Department of Health. The design resulted in lower costs

for concrete structures, fewer and smaller filters, and less valves and controls. The smaller plant footprint resulted in reduced impact on nearby wetlands. The overall contract saved Seattle approximately $70 million over projected project costs.

Waterbury, Connecticut, Harry P. Danaher Water Treatment Plant. American Water undertook the responsibility for operating and maintaining this water treatment facility in 2003; the contract was renewed in 2008 for an additional five years. The plant is located in Thomaston about 15 miles north of Waterbury. It is a conventional water treatment facility with coagulation, flocculation, sedimentation, filtration, and chemical addition and has the capacity to deliver 38mgd of water per day. It serves a population of approximately 115, 000 in Waterbury as well as four other smaller municipalities in the surrounding area.

Since the date the Contract Services Group had won the initial contract, it has achieved a number of improvements at the plant that effectively reduced operating expenses. As a result of a treatment optimization study at startup, plant operators were able to achieve a greater than 50 percent reduction in the use of alum during winter months. A trial of a new coagulation polymer shows promise of consistent year-round reductions in that range. AWE also implemented the use of Geotube® dewatering technology for plant residuals in place of the drying basins. The new technology significantly increased percentage of solids, reducing the costs associated with hauling and disposal.

VIII. Team Member References

Since the team is composed only of American Water entities, the references below will provide relevant qualifications and capabilities demonstrated by American Water in carrying out the relevant projects.

IX. References

Elizabeth, New Jersey Water and Wastewater System. Mayor J. Christian Bollwage, Elizabeth City Hall, 50 Winfield Scott Plaza, Elizabeth, NJ 07201. Tel: 908.820.4170. mayor@elizabethnj.org. Also John Papetti, Public Works Director, same address. Tel: 908.820.4106.

Edison, New Jersey, Water Distributions System. Mayor Antonia Ricigliano, Municipal Complex, 100 Municipal Boulevard, Edison, New Jersey. Tel: 732.248.7298. Mayorricigliano@edisonnj.org. Also Maureen Ruane, Business Administrator, same address. Tel: 732.248.7298, Email: mruane@edisonnj.org.

Lincoln, Illinois, Wastewater Treatment and Collection System. Orville Busby, Alderman and Sewer Committee Chairman, 220 Peoria Street, Lincoln, Illinois 62656. Tel: 217.732.7935. Email: Not available.

Quincy, Illinois, Wastewater Treatment and Collection System. John Spring, Mayor, 730 Maine Street, Quincy, Illinois 62305. Phone: 217.228.4500. Email: jspring@quincyil.gov.

St. Charles, Missouri, Wastewater Treatment Plant. Mayor Sally Faith, City Hall, 200 North Second Street, Saint Charles, Missouri 63301. Tel: 636.949.3268. Email: Sally.Faith@stcharlescitymo.gov

Waterbury, Connecticut, Harry P. Danaher Water Treatment Plant. Donald Carver, Superintendent of Water, Bureau of Water, 31 East Aurora Street, Waterbury, Connecticut 06708. Tel: 203.574.8250. Email: dcarver@waterburyct.org.

Phoenix, Arizona, Lake Pleasant Water Treatment Plant. Cynthia Prejs, Contract Manager, Water Services Department, 200 West Washington St–9th Floor, Phoenix, Arizona 85003-1611. Tel: 602.534.1795 Email: cindy.prejs@phoenix.gov

Seattle, Washington, Tolt River Water Treatment Plant. Dave Hilmoe, Director, Drinking Water Division, Seattle Municipal Tower, 700 West 5th Avenue, Seattle, Washington 98104. Tel: 206.684.7414. Email: Dave.Hilmoe@Seattle.gov

Technical Capability

I. Operations and Maintenance Expertise

American Water has operated and maintained water infrastructure for more than 125 years. During the decades since its founding, American Water has remained one of the acknowledged leaders in the water industry, successfully adapting to changing industry demands, developing new technologies, and meeting increasingly rigorous compliance regulations. Our environmental compliance for 2011 was greater than 99 percent for both water and wastewater operations.

The company's leadership role in the water industry was recognized by *Global Water Intelligence* magazine, which bestowed its "Water Company of the Year" award on American Water in 2009. The award recognizes overall excellence in the global water industry—the projects, the technologies and the people who have made a difference.

Today, the largest business segment is comprised of American Water subsidiaries that own the infrastructure assets they operate and are regulated by state public utility commissions. These subsidiaries provide water and wastewater services in approximately 1,600 communities in 16 states in the United States. Infrastructure assets include approximately 80 surface water treatment plants, 500 groundwater treatment plants, 1,000 wells, 100 wastewater treatment facilities, 1,100 treated water storage facilities, 1,200 pumping stations, 90 dams and 46,000 miles of mains and collection pipes.

> *"Pennsylvania American Water has been a trusted partner and corporate citizen to my constituents. The regionalization of water assets in Washington County has brought long-term reliability and quality service to many of our citizens. We continue to partner with Pennsylvania American Water to consolidate distressed systems, which has produced more efficient management of our water systems and continued infrastructure investment."*
>
> ***Pennsylvania State Senator Tim Solobay***

American Water has a substantial presence in Pennsylvania. Pennsylvania is the company's largest subsidiary by customer count and the largest regulated water and wastewater supplier in the state. Its more than 1,000 employees serve 2.2 million persons in nearly 400 communities. Our 38 treatment plants and 110 wells in Pennsylvania provide consumers each day with an average of 202 million gallons of drinking water.

In addition, American Water also offers market-based operations that provide high-quality water and wastewater operations and maintenance services through long-term contracts and concessions to clients who might wish to have these assets operated by the private sector. The company has been involved in contract operations for municipal governments for more

than 65 years and now provides these services through American Water Enterprises to clients that include federal, regional and municipal governmental entities and private-sector clients.

Many of the systems we operate, whether for ourselves or others, are similar in size to, or larger than, the Allentown water and wastewater facilities. The company has the expertise, the record of environmental compliance, the commitment to invest in required capital improvements, necessary resources, and experienced managerial and operating personnel to provide safe and reliable water and wastewater utility services to Allentown.

> *"Throughout my 20 plus years with Green Tree Borough, Pennsylvania American Water has continually reinvested in our municipality's water infrastructure and worked closely with us to coordinate these projects along with our other community improvements. They have always been extremely responsive to our requests, as well as a great, dedicated community partner."*
>
> ***Green Tree, Pennsylvania Borough Manager Dave Montz***

A. Substantial Water and Sewer Operations Experience

The range of management responsibilities American Water accepts in public-private partnerships range from packaged treatment plants for small residential developments to plants rated at more than 100mgd.

Water

In terms of water facilities, American Water's technical and practical experience for public sector clients includes the operation, maintenance and management of a number of surface water, multi-well or combination ground water/surface water systems. These include Seattle's Tolt Water Treatment Plant, rated at 120mgd; the Lake Pleasant facility in Phoenix, Arizona, rated at 80mgd; Waterbury's Harry P. Danaher Water Treatment Plant, rated at 38mgd, and the 25mgd Tampa Bay Water Authority seawater desalination plant.

In addition to water treatment, additional contractual responsibilities include the operation and maintenance of transmission mains, distribution systems, high- and low-lift pump stations, ground reservoirs, water towers and tanks, and the installation, repair and reading of water meters.

Sewer

For wastewater, American Water's experience includes simple facultative ponds to complex membrane bio-reactors in every climate zone across the United States. Facilities that American Water has operated include a variety of aeration techniques, including coarse bubble and fine bubble diffused aeration, pure oxygen, and simple extended aeration. Contract facilities are equipped with biological nutrient removal of both nitrogen and phosphorus to the most stringent effluent limits.

In terms of biosolids, American Water operates a wide variety of sludge management technologies for thickening, digestion and dewatering, from simple to complex, gravity to dissolved air flotation thickeners, aerobic and anaerobic digesters, sludge presses, centrifuges, simple drying beds and complex thermal drying pelletizers. Some contracts involve systems with multiple plants. It is also responsible for the operation and maintenance of wastewater collection systems, combined storm-sewer systems and storm drain systems; pump stations; sewer manholes; and effluent outfalls.

Operations Awards

We take partnerships seriously evidenced by the number of public-private partnerships we have entered into that have been recognized for their success. In the boxes below, we have listed some of the project awards American Water has won for its public-private partnerships.

AMERICAN WATER EPA AWARDS

In June 2012, **American Water received 18 Directors Awards of Recognition from the Partnership for Safe Water**. Fifteen plants received awards for maintaining Phase III certification for ten years, two plants received awards for maintaining Phase III certification for five years, and one plant was presented with its first Directors Award for Phase III certification.

The Partnership is a voluntary initiative developed by the U.S. Environmental Protection Agency (EPA) and other water organizations to recognize water suppliers that consistently achieve water treatment standards that surpass EPA regulatory requirements.

With a total of 66 surface water treatment plants recognized across the country, American Water has had more plants receive Phase III certification than any other water utility in the country. Approximately 30 percent of all water treatment plants nationwide to receive Phase III certification are American Water plants.

AMERICAN WATER PROJECT AWARDS

2012 Outstanding Partnership Award, U.S. Conference of Mayors, Elizabeth, NJ, Concession agreement

2010 Project of the Year, American Public Works Association, Fillmore, California, zero-discharge wastewater recycling facility DBO.

Global Water Awards 2009, Water Company of the Year, **Global Water Intelligence magazine,** Corporate Award

2009 Excellence in Public-Private Partnerships Outstanding Achievement Award, U.S. Conference of Mayors, Lake Pleasant Water Treatment Plant, Phoenix, DBO.

2009 Associated General Contractors of America, Special Recognition, Lake Pleasant Water Treatment Plant.

2008 Public-Private Partnership Award, National Council for Public-Private Partnerships, Tampa Bay Water desalination plant DBO

2008 Excellence in Public-Private Partnership Award, U.S. Conference of Mayors, Buffalo, New York, water system operation

Global Water Awards 2008, "Water Project of the Year", Global Water Intelligence, Tampa Bay Water desalination plant.

Global Water Awards 2008, Highly Commended, Global Water Intelligence, Lake Pleasant Water Treatment Plant

2005 Design-Build Industry Association-Southeast Project of the Year, Camp Creek Wastewater Treatment Plant, Fulton County, Georgia, DBO

2002 Grand Award, American Academy of Environmental Engineers, Tolt Treatment Plant, Seattle.

Substantial Experience - Project Descriptions

Lincoln, Illinois, Wastewater Treatment Plant.

This 33mgd wastewater facility has been operated by American Water's Contract Services Group since November 1990. The city has renewed the contract twice; the current term will end in April 2015. Initially the contract involved only the operation of the wastewater facility. Later scope changes included adding the responsibility for the maintenance of the city's collection system. A later amendment has American Water providing a licensed professional the city's engineer.

A project manager, eight full-time operators and one part-time operator handle the wastewater treatment plant and 100 miles of collection system mains, 11 lift stations, and two combined sewer outfalls. Mains range in size from 8- to 96-inches. The majority of the lab services are performed in-house. Exceptions are specialized testing for mercury, bio-monitoring, and metals performed by an outside lab. There is an annual responsibility of $85,000 in maintenance and repair costs.

American Water's operating subsidiary undertook a major expansion of the plant as a design-build project in 2004, including new headworks, extra aeration bays, an added final clarifier, a RAS station, conversion of two trickling filters into aerobic digesters, conversion of two anaerobic digesters into sludge holding, and the addition of a belt filter press. Later, it also designed and constructed the equipment necessary for the conversion of the plant from gas chlorine to liquid hypochlorite.

American Water also assisted the city with a study of the effluent receiving stream and successfully negotiated with the Illinois Environmental Protection Agency (IEPA) to maintain the city's NPDES permit limits, after the IEPA had indicated that the facility would become subject to stricter permit requirements. It recommended improvements to the plant's electrical system which resulted in savings of $85,000.

The facility received "Plant Of The Year" nominations from the IEPA in 1997 and 1999; the Burke Safety Award, through the Water Environment Federation in 2002; and the American Water Works Safety Award for 2009.

Quincy, Illinois, Wastewater Treatment Plant

This 34mgd facility has been operated by a Contract Services Group entity since June 2002. The contract was renewed for five years in 2005, with a scope change for sludge handling. The contract was renewed a second time in March 2010 for another five-year term. Full-time staffing includes a facility manager, assistant manager/pre-treatment coordinator, industrial technician, two maintenance technicians, and five operator who are municipal employees.

The contract includes responsibility for all operational and maintenance for the wastewater treatment plant and six combined sewer outfalls, nine lift stations and a two-stage lagoon system and the Industrial Pre-Treatment Program that includes 31 significant industrial users. Prior to entering into the agreement for its wastewater facility, the city faced significant challenges in meeting its NPDES permit for discharge. The city was required to test the discharge five days weekly per the permit. Within two weeks of beginning our operations, the plant was operating in compliance, resulting in its being nominated in 2005 as "Plant of the Year" by the IEPA. Because of the improved performance, the new NPDES permit in 2007 reduced the testing limits to three days per week.

St. Charles, Missouri – Missouri and Mississippi River Wastewater Treatment Plants

This project, operated by American Water's Contract Services Group, consists of two plants serving a population of 91,000. The contract has been renewed a number of times: in January, 1989 for five years; January, 1994 for five years; amended in November, 1997 to extend the contract to 2004; and amended in 2005 to extend the contract to 2013.

Scope amendments include responsibility for project management of the installation of a 720,000-gallon sludge storage tank at the Mississippi facility. As noted in Section 1, American Water is currently managing the construction of a combined $40 million in capital improvements at the two plants.

The project has earned a number of awards: the WEF Burke Safety Award in 1995 and 2007; two nominations by the EPA for the National Pretreatment Excellence Award; plant operators

received the Missouri Water and Wastewater Conference Operator of the Year Award in 1995, 1996 and 2008; EPA awarded its Certificate of Merit for Beneficial Reuse of Biosolids; and the Missouri River plant was selected as Missouri Water Environment Association Plant of the Year in 2007.

Waterbury, Connecticut - Harry P. Danaher Water Treatment Plant

American Water undertook the responsibility for operating and maintaining this water treatment facility in 2003; the contract was renewed in 2008 for an additional five years. The plant has the capacity to deliver 38mgd and serves a population of approximately 115,000 in Waterbury as well as four other smaller nearby municipalities. It is a conventional water treatment facility with coagulation, flocculation, sedimentation, filtration and chemical addition. American Water completed a full scale implementation of the Infor EAM Enterprise Edition CMMS software (formerly DataStream 7i) and has used the CMMS program to provide work orders and track the repair history of water treatment equipment, pumps, motors and valves of all types, generators, on-line analyzers, flow metering equipment, and a variety of chemical feed systems.

Work orders are generated daily, with a monthly reporting of completion status provided to the city. The CMMS is also used for tracking

spare parts and inventory. Microsoft Dynamics 9, Great Plains is used across a Citrix platform to generate and track purchase orders and accounts payable. Scanned images of invoices are tracked in the ImageNow 6 Sunflower software program, which offers workflow management capabilities.

Since American Water won the initial contract it has achieved a number of improvements at the plant which have resulted in reduced operating expenses. As a result of a treatment optimization study at startup, plant operators were able reduce by more than 50 percent the use of alum during winter months. A new coagulation polymer shows promise of consistent year-round reductions in that range.

Reduction in alum use has also helped control energy costs at the plant since the lower dosages allows plant filters to operate longer before they must be taken off-line and backwashed.

New Jersey American Water - Canal Road Water Treatment Plant

An advanced surface water treatment plant operated by New Jersey American Water, it is located the Raritan and Millstone rivers. Water is directed through a series of wedge-wire screens, and then flows by gravity through two 60-inch diameter water raw water mains, housed in two 10-foot diameter tunnels, under the Raritan and Millstone rivers to Franklin Township to the Raw Water Pump Station.

The plant employs pre-ozonation to remove taste and odors, color, iron and manganese. Hydrogen peroxide can be added at this stage of treatment, the addition of which in conjunction with ozone is known as an advanced oxidation practice and is available as a treatment option when needed. There are two rapid mix basins in which acid/caustic is added in the first stage for pH adjustment and coagulant added in the second. Two parallel flocculation trains have a capacity of 0.86 million gallons with a detention time of approximately 40 minutes at 80mgd.

This is followed by four parallel sedimentation trains. Two of the trains are the original conventional sedimentation basins that were part of the original construction of the plant.

The second two clarification trains consist of high rate lamella plate settler units, which were added during a recent capacity expansion project. On line turbidimeters and particle counters continuously monitor both basins. Intermediate ozonation is utilized as the primary

method of disinfection, followed by eight dual-media gravity box filters.

After filtration and sodium hypochlorite addition, the water flows to the 5-million-gallon filtered water reservoir, where chemicals are added for pH adjustment and corrosion control. Chloramines are also added to minimize disinfection by-product (DBP) formation in the distribution system, although the need is primarily because the water from Canal Road

blends with supplies from the Raritan-Millstone WTP, which is a less advanced and requires chloramines to limit DBP formation.

A ground mounted dual array photo-voltaic system was installed at the plant consisting of 2,871 solar PV modules. The $3.5 million project won a $1.9 million grant from the New Jersey Clean Energy Fund. Following the initial installation, the solar array was been expanded by nearly one-fifth. About 15 percent of the plant's peak electrical needs are supplied by the solar panels, which generate 0.75 megawatts of power.

Seattle, WA - Tolt Water Treatment Plant

This 120mgd treatment facility consists of a chemical storage and feed system, flocculation basins, deep bed anthracite filters, a buried clearwell, washwater clarification and solids drying basins, and an on-site landfill for disposal of dried solids. The plant includes ozonation facilities which, together with filtration, will achieve the goal established by Seattle Public Utilities. These facilities are divided into two parallel treatment trains to maintain plant flexibility and backup capabilities.

Raw water flows to ozone diffusion and contacting basins, followed by flash mixing facilities for chemical addition and hydraulic flocculation basins. Flocculated water flows to the adjacent filter block, where it is passed through six mono-media deep bed anthracite filters. Filtered water is piped to the buried clearwell, which provides volume to balance variations in plant production and chlorine contact time for emergency disinfection. Entering the clearwell, the filtered water receives additional chemicals for pH adjustment, corrosion control, and secondary disinfection. Water flows by gravity through the entire facility. The facility is one of two supplying Seattle with water although the Tolt plant is the only filtration facility in the Seattle system.

Phoenix, Arizona—Lake Pleasant Water Treatment Plant.

As one of the nation's fastest-growing metropolitan areas in the U. S., the City of Phoenix had an urgent need to address future water supply, particularly in the City's expanding northern portion. Late in the last decade, the City began planning for a new water treatment plant and in 2003 contracted with American Water to execute the largest water DBO in North America. Design started in the summer 2003 and construction began the following year. Performance trials were completed prior to the plant's delivery to the City. The plant was commissioned in June 2007.

It has treatment capacity of 80mgd, which can be expanded to 320mgd, enabling the city to keep pace with population growth and development. The Lake Pleasant Water Treatment Plant operates with the latest in modern water treatment technology and automation. The plant has an intake structure and pumping station located on the Waddell Canal. A 90-inch diameter pipeline delivers raw water 2.3 miles from the canal to the 225-acre treatment plant site, where indigenous materials and native flora were used to make the facility blend with the surrounding desert.

Treatment is a multi-barrier process that includes ballasted flocculation, ozonation, filtration and secondary treatment through granular activated carbon contactors, UV disinfection, chemical dosing, and solids processing. The plant produces water with extremely low levels of trihalomethane pollutants. American Water will operate and maintain the facility for 15 years, with an option for an additional five years.

Tampa Bay Water Authority – Seawater Desalination Plant.

American Water operates this seawater reverse osmosis (RO) desalination plant, the largest such facility in the United States. The scope included the required remedial design, permitting and construction to correct facility deficiencies from a prior contractor

Three 350hp vertical turbine pumps rated at 18,000 gallons per minute supply seawater from the adjacent Tampa Electric Company generating facility to the plant's pre-treatment band-screen which removes larger debris from the raw water. Another similar pump provides cooling water when needed. Chlorine dioxide is injected to reduce biological and algal growth, followed by coagulation and flocculation utilizing ferric chloride. There are 32 up-flow style single stage sand filters that remove particles conditioned by the initial pre-treatment. Filtered water is pumped to pressuring vessels containing five micron pre-coat cartridge filter elements which are automatically backwashed based on head loss.

From the pre-coat filters, water is pumped into the seven first-pass RO trains, each with 168 pressure vessels per train containing thin filter seawater RO membranes. A second pass RO train is available mainly to reduce chloride levels. Carbon dioxide is dosed for bicarbonate alkalinity formation, hydrated lime is injected to increase alkalinity and calcium hardness of the water, sodium hypochlorite is added for disinfection and sulfuric acid is used to adjust final water pH.

B. Advanced Knowledge Of Maintenance, Repair, Construction

Maintenance

American Water understands that an effective maintenance program is a well-balanced combination of industry-proven techniques undertaken by skilled people on a scheduled basis. American Water closely monitors the condition of the facilities it operates. Through a computerized maintenance management system and the use of specialized diagnostic equipment, it can schedule maintenance and repair activities before major problems arise. Asset management programs track individual system components, assessing their condition and prioritizing capital improvements. Even highly skilled employees continue to receive regular training in maintenance techniques, monitoring equipment and tools.

Preventive/Predictive Maintenance. American Water's approach to maintenance activities is based on manufacturer's recommendations and industry-accepted best operating practices, both incorporated into the plant operations manual American Water develops for each project. The overall objective is to ensure that consistent standards of maintenance are applied and management systems are introduced which ensure clear procedures, reliability, and quality of maintenance, while taking into account the differing conditions and equipment existing at each plant.

A combination of maintenance strategies is used with a focus on predictive and preventive maintenance programs. Predictive maintenance is applied to major equipment whose failure would upset treatment processes, affect reliability and require costly repairs. A preventive maintenance approach is used for all equipment where preventive tasks will extend mean-time-before-failure. Corrective or repair maintenance is reserved for non-critical, off-the-shelf-type equipment. It is the proper blending of the various maintenance approaches that yields the most efficient use of resources, improves equipment/process reliability and ensures the greatest return on capital cost. Major pieces of equipment have continued to function well beyond their normal and expected useful life cycle.

An emphasis on predictive tasks is an obvious key to the success of the preventive maintenance program. Monitoring requirements are established for each piece of equipment, and regular performance measurements compare it to known baselines to assess variance. By properly implementing a predictive maintenance program and selecting appropriate predictive technologies, significant savings in maintenance costs can be realized through:

- Equipment downtime reduction
- Reduced preventive maintenance costs
- Reduced energy consumption
- Reduced unscheduled or emergency repairs

Specialized Maintenance Tools and Practices. In carrying out its maintenance program, American Water utilizes a wide variety of specialized maintenance tools and practices, some of which are described below.

Infrared Thermography: Many maintenance problems are associated with localized areas of increased temperature. Hand-held thermography instruments are utilized to detect infrared (I/R) radiation emitted from an object which is directly proportional to its temperature. I/R thermography provides non-contact and condition-based information that can be used in a number of areas. In the electrical system, hot spots indicate areas with loose or corroded connections, damaged insulation, or overloaded conditions. The treatment plant utilizes a great deal of electrical equipment and switchgear so the use of thermography is very important in reducing the risk of critical failures. For mechanical systems, heat may indicate areas of increased friction caused by poor lubrication, misaligned bearings or faulty drive systems that can be detected by thermography.

Vibration Analysis: Vibration analysis is a sensitive and accurate indicator of equipment health. Each piece of equipment has a signature vibration frequency, and variations, when detected, are analyzed to determine the problem source, typically imbalance, misalignment or defective bearings. While vibration analyses can be conducted by personnel, continuous on-line instrumentation incorporated into the control logic for the device can be used to shutdown critical large rotating equipment before serious damage occurs.

Pump Precision Alignment and Inspection: Alignment provides an accurate and effective method of analyzing the amount of misalignment in coupled rotating equipment. Misalignment leads to excessive vibration, which can lead to further problems such as excessive heat and increased electrical costs. Portable computer-aided laser optical alignment systems employ a low emission laser, target and a hand-held analyzer to assess parallel and angular displacements and provide the necessary corrections.

Wear Particle Analysis: Samples of lubricating oils extracted from identified equipment are studied to determine the effectiveness of the lubrication and whether excessive wear is evident. Effectiveness is determined by characterization of the wear particles in the samples. By utilizing this condition-based approach, the necessary preventive maintenance can be reliably scheduled in advance of any failures that might affect the life of the equipment.

Motor Testing and Inspection: Motor testing is utilized to identify deteriorating insulation, problems with motor windings or wiring connections, and excessive dirt or other contaminants.

Transformer, Motor Starter and Switch Gear Inspections: Just as important as the motors themselves, transformers, motor starters and electrical switchgear are valuable assets that need to be inspected to identify any deterioration, loose connections, wearing mechanical parts, signs of heat or corrosion and excessive buildup of dust and grime.

Wire-to-Water Efficiencies: Measuring the ratio of energy output in the form of pressure and flow compared to the electrical energy input provides performance data for a pump and motor operating under actual field conditions. This is a valuable tool for monitoring pump condition and wear and ultimately predicting pump wear over time and related maintenance.

Computerized Maintenance and Management Systems. As part of its maintenance programs, American Water regularly employs computerized maintenance management systems (CMMS) at its facilities to assist operators in the implementation and analysis of the various maintenance management efforts. Recently, American Water chose Infor EAM Enterprise Edition (formerly Datastream7i) as the CMMS platform of choice for its regulated facilities and has started implementing it across the company. American Water's Contract Services Group has standardized on JobCal and, with a few exceptions, are utilizing this as the CMMS software of choice.

Because many facilities we operate for others already have established CMMS programs;, American Water also has had experience with a number of other such programs and has made these programs an integral part of its operations at those locations.

Other Information Systems. American Water utilizes a variety of information systems—for laboratory information, operations, maintenance, fleet management, financial and general administrative purposes. Information technology (IT) professionals play a vital role in ensuring the smooth and efficient operation of American Water facilities and are responsible for implementing standardized computer networks and systems, and providing ongoing advice, support and procurement for all computer equipment and supplies. They provide guidance in the installation of appropriate management information systems.

Engineering

American Water's Engineering Center of Expertise offers a 40-person team providing planning and engineering services to all American Water subsidiaries. The center supports each state-subsidiaries' engineering groups with dedicated resources for planning, project management, civil, environmental, electrical and mechanical disciplines. In Pennsylvania, recent collaborations include the Hays Mine Water Treatment Plant expansion near Pittsburgh, the New Castle Comprehensive Planning Study, the Ellwood Treatment Facility siting evaluation and the West Shore Treatment Facilities Chemical Improvement project.

The division handled a wide variety of system evaluations, selected treatment processes, established critical criteria for water and wastewater treatment systems in order to improve operations, considered how worker safety should be incorporated into the design of facilities, and prioritized pending capital improvements.

The experienced engineering staff is skilled in assessing each project's unique challenges, selecting treatment processes or design approaches tailored to the project, and managing

design and construction subcontractors in completing the work. American Water's history of process design experience, performed in-house or in conjunction with outside engineering firms, as well as its engineering excellence and project management skills is essential to the effective execution of any water or wastewater capital program.

Our engineers play an important role in the DBO partnerships we engage in. American Water's engineers bring an operator's perspective to all potential designs, carefully assessing any proposed design that may be proposed to ensure it is cost efficient, robust, and reliable in real-world operating conditions. American Water engineers also provide process recommendations during the design of the various elements of a capital improvement program to control project costs. Construction costs, operating costs, and life cycle costs are evaluated and value engineering studies are performed during design to challenge design criteria and help control project costs.

This extensive experience positions us favorably to partner with municipalities to upgrade and manage their infrastructure projects. While American Water does not undertake any construction directly on its major capital improvement projects, it has worked cooperatively with most national and regional constructors in the United States, either on its own projects, or on public sector capital improvement projects.

C. Assessment of Remedial Maintenance Action

We provided our general approach to remedial maintenance in the section above. Not discussed in prioritizing maintenance tasks in that section was our use of asset management programs. Although similar in nature to a CMMS, an asset management program works in tandem with the CMMS. It provides an overview of the entire system and is useful in the development of long-term remedial plans for infrastructure deficiencies. American Water routinely prepares asset management plans for its water and wastewater facilities, systematically characterizing equipment and systems and updating condition assessments. This assures that assets are being maintained appropriately and replaced strategically. In addition, planning for such issues as service level requirements, environmental objectives, and infrastructure expansion assists in the development of the long-term capital improvement program.

D. Maintenance of Water and Sewer Concession Assets

In the sections above we have provided information about our capability to operate and maintain the physical plant and distribution and collection systems, supplying our project experience with a wide variety of water and wastewater systems. In Allentown, we will implement the same technologies and methodologies and will assign skilled managers to assure that the city's assets continue to operate at a high level.

Water and Sewer Fee Management, Operations, Administration

In most of our contracts, we manage the full cycle of the water and sewer process—from treatment to billing and collection to administration and back-office systems to educating and engaging with the public. As an example, in Buffalo, New York, we significantly transformed the city's back-office customer services system and administrative tasks, making them modern and efficient. This achievement was recognized by the U.S. Conference of Mayors in 2008, which awarded the project is Excellence in Public-Private Partnership Award for water system operations.

We offer payment on-line or mail-in and establish walk-in locations for bill payment. In bill statements, we often include educational pieces for the citizens we serve, such as cold-weather tips, water conservation tips, and more. We have an in-house professional staff that specializes in media relations. Pennsylvania-based staff would oversee project-related media relations in Allentown.

Marketing and Public Relations

If selected to operate the systems, American Water will work with the city to develop a communications program to educate residents about the proposed transaction. As we have elsewhere, American Water, in conjunction with a regional communications partner, will help Allentown develop an educational program to ensure residents receive accurate information, which includes correcting misinformation and countering any negative messages about the city's plans to implement a concession agreement.

American Water has decades of experience in identifying issues, educating customers, and providing information that addresses the needs or concerns of the public. Key messages to a variety of audiences will detail the benefits that accrue to the public when the public and private sectors work together to find solutions to specific issues. American Water will work with the city to develop a series of communication channels that will enable information to be shared with the city, all regulatory agencies, and the general public throughout the life of the contract.

II. Customer Service

In June, American Water's Customer Service Center (CSC) was awarded the 2012 Call Center Excellence Award for Best in Class Call Center (over 200 staff), from the International Quality and Productivity Center (IQPC). The IQPC's Call Center Excellence Awards recognize the most innovative call center solutions and individuals over the past year. With awards given in eight categories, the winners are selected by a panel of call center experts who look for superior thinking, creativity, and execution across all call center functions. The global award recognizes companies that provide outstanding customer service while controlling costs and

managing complex operations. The award also honors call centers that set a vision of excellence and work collaboratively within their organizations to achieve their goals.

American Water manages all aspects of billing and customer services for over four million customers. With a support staff of over 700 employees, the company operates two large centralized customer service centers located in Alton, Illinois, and Pensacola, Florida which offer 24/7, 365 service. Aspects provided include:

- Processing meter reads
- Water and wastewater billing, collections
- Customer call handling
- Field service scheduling
- Emergencies
- Delinquency processing, and reporting.

In other cases, American Water has provided stand-alone customer service within the municipality. In some cases, the client wishes to retain overall responsibility for billing and collection and requires American Water to provide only some aspect of those services, such as meter reading and repair. American Water Enterprises has provided local billing and customer services to public entities as part of its operation and maintenance contracts for over 20 years.

Overall, American Water is experienced and routinely handles all of the key areas of water utility billings, collections, and customer service, such as:

- Flat rate utility billings
- Meter reading, meter replacements, and meter repairs
- Transmitting meter reading data to municipal billing systems or in-house billing software
- Printing, processing, and mailing utility bills
- Payment collection in various forms including mailed, lockbox, walk-in, payment agent, drop box and electronic payments
- Daily, monthly and annual reporting on billing data
- Providing information, developing processes, and managing effective billing and customer service processes

While the city's goals as elaborated in the Request for Proposals may ultimately differ, the following summary enumerates typical goals for delivering excellent, cost-effective performance. We have experience and success in the following areas:

Timely and Accurate Billings. Primary focus is on accuracy, as quality minimizes billing complaints and avoids customer calls.

First-Call Service Resolution. The timely response to customer queries improves satisfaction, reduces avoidable calls, and improves staff productivity.

Outstanding Collection Performance. Collections typically exceed 96 percent of billings, with proven processes to manage delinquent customers.
Comprehensive Reporting and Internal Control. This will met any financial requirements of the City.

Convenient Customer Service. Billing, service and emergency questions get answered by customer service experts who are available around the clock. Customers may also pay their bills by mail, direct debit, online or at local payment stations–a range of options that are simple and convenient. When customers need immediate help, Pennsylvania American Water teams dispatch service requests sent directly to computer laptops in employee trucks, for more efficient customer service.

Customer Satisfaction. American Water conducts quarterly customer satisfaction surveys through an impartial third-party firm. The surveys measure overall customer satisfaction and satisfaction among customers who have had a recent contact with the company's customer service center and/or field operations employees. Our overall company customer satisfaction scores from the second quarter of 2012 equate to approximately 94 percent in satisfied categories while service quality equaled 89 percent in satisfied categories. These high ratings are consistent with surveys conducted over the last three years.

Community Service. Our community involvement is multifaceted, drawing on the unique talents of our employees as well as the resources of our business. Through community giving, partnerships and volunteering, we demonstrate our commitment to programs that address community-specific needs. One example is American Water's H2O – Help to Others Program, which for nearly 20 years has assisted low-income customers in Pennsylvania. Customers who qualify can receive a grant of up to $500, a discount on their service fees and water-saving devices and education on how to use water wisely. Another is our support of local organizations who share our vision–community organizations such as local watershed groups, river clean-ups, and community charitable associations such as the United Way. American Water also offers a firefighter grant program to help support equipment and training costs borne by these departments. Since the program's inception in 2009, fire departments in Pennsylvania have received nearly $100,000 in contributions.

Established in 2005, our annual Environmental Grant Program offers funds for innovative, community-based environmental projects that improve, restore or protect the watersheds, surface water and/or groundwater supplies in our local communities. In 2011, American Water awarded $35,000 to seven Pennsylvania community organizations.

Beyond the company's efforts, our local employees volunteer their time to support important community events such as, in Pennsylvania, United Way's "Day of Caring", Mechanicsburg's Earth Day event, Habitat for Humanity, and the West Shore Chamber of Business and Industry events.

Transition Plan

American Water has prepared and implemented a great variety of transition plans that successfully incorporated the full range of utility functions, including customer services functions. While it is impossible to offer any plans for Allentown's system without the opportunity to complete due diligence, we can offer some general guidelines that have been used in previous transitions.

Transition Team. One of the first things undertaken during a transition is developing lines of communications with municipal employees and officials, as well as any groups with special interests identified. Since communications and coordination are critical for the safe and reliable operation of the system, American Water will assist in developing a series of communication channels that will enable information to be shared with the City, all regulatory agencies, and the general public throughout the life of the contract.

With respect to operations, immediately after being selected to undertake operations, American Water assembles a transition team that guides the transfer of operational management. The transition team is co-led by the project manager and an assigned transition manager. American Water has found that this co-lead approach during the transition phase allows each manager to focus his or her efforts on specific areas of responsibility. Such an arrangement allows existing staff to concentrate on its critical mission of providing high-quality service to water and wastewater customers. Other typical members of the team include operations experts, IT personnel, human resources specialists, customer service managers, and administrative staff.

Data Acquisition Transition. American water personnel typically arrive to begin inventorying, cataloging, and archiving the historical data pertaining to the system approximately 60 to 90 days before assuming operational responsibility. This review includes legal documents involving consent agreements, service agreements, current and historical system maps, service records, meter records, customer complaint logs, laboratory records, operations logs, reports, well logs, regulatory filings and information. All data will have been located and cataloged 30 days before assuming operations.

Billing and Collections Transition. Generally, the approach is to archive historic data, capture current accounts receivables, and begin integrating the billing and accounting into the formats to be used for meter reading, billing, account collection, and customer service. By 30 days prior to taking over financial responsibility for the system, American Water will have completed any necessary recruitment for customer service positions, meter routes will have been established, and billing programs prepared. Programs will be debugged and fine tuned during the 30 days prior to contract start, and all meters identified, located, and accounted for.

Maintenance Transition. American Water undertakes an initial facilities survey to establish the condition of all equipment. We perform a thorough review of all systems that require maintenance, identifying the routine maintenance required, and describing those maintenance cycles. This team utilizes best available technology to help them in their evaluation, such as thermographic imaging, vibration testing, and oil analysis. Those items found to be in need of repair, or are otherwise not functioning properly, will be identified and prioritized for repair or replacement. We will share our observations of system functionality with local officials prior to the start of the contract term.

III. Safety and Security

A. Knowledge of Safety and Security Techniques & Methodologies

Health and Safety

Protecting the health and safety of employees is American Water's top priority. We begin all meetings with a safety reminder. Our CEO's message to our organization: "Getting the job done will never take priority over getting the job done safely. Speed does not come before safety at American Water. Not ever." Health and safety performance targets are established at the corporate level and for each subsidiary. In addition to these targets, management and employees also have specific safety goals that are reviewed as part of their annual performance appraisal.

Health and safety professionals with deep and broad safety knowledge provide advice, guidance and training, audits, and corrective action management on both the corporate and subsidiary levels. Several of the professional staff have certifications from nationally recognized entities such as the Board of Certified Safety Professionals and the American Board of Industrial Hygiene. These qualified professionals work closely with operations personnel in assuring appropriate health and safety processes and procedures are in place at all American Water operations.

Following these corporate policies, an active Health and Safety Management Program is developed and reviewed annually. Every facility has a comprehensive site-specific safety and emergency response plan also reviewed, at a minimum, annually, to assure it is current and reflects any operational changes that may occur. The health and safety policies define the roles, responsibilities and expectations of all workplace parties, including sub-contractors and visitors. Confined space entry, chemical handling and work at heights exemplify the activities for which each facility must develop specific solutions that protect the health of our employees, the integrity of the facilities we maintain, and the safety of communities we serve.

American Water personnel are trained in emergency management and incident reporting which categorizes and identifies events and procedures for notification, reporting and implementing actions. Incidents that require immediate response and mobilization are quickly responded to by a highly trained staff of operational and environment, health and safety personnel. Local emergency responders are identified and clearly posted at each facility and are contacted as the incident requires.

Each facility develops plans and standard operating procedures that mitigate the inherent risks involved in our industry. Many of these plans involve community emergency responder input from agencies such as the local fire departments and emergency planning offices. When necessary the facility will develop and implement EPA Risk Management Plans for sites with chlorine gas or other chemicals, Spill Prevention Control and Countermeasure Plan for sites with petroleum storage above threshold levels and must adhere to all local, State and Federal Environmental Protection and Community Right-to-Know laws and regulations. Our health and safety program requires that all facilities must report and comply with U.S. Occupational Safety and Health Act and Canadian Ministry of Labor safety and health regulations.

A Safety, Health, and Environmental Quality Team is dedicated to making sure every employee, contractor, or any other person involved with the company has access to a safe work place and follows safety rules. Basic rules which employees abide by include:

- Work is not conducted without a pre-job risk assessment appropriate to the level of risk
- Persons are trained and competent in the work they conduct
- The right tools and equipment are provided to do work safely
- Personal protective equipment will be worn as defined by risk assessment and local site requirements
- Employees have an obligation to stop work that they consider unsafe and immediately report their concerns
- Use of drugs and alcohol in the workplace is prohibited
- All work practices and procedures will be in compliance with all relevant regulations and company policies

American Water also has a qualified group of security professionals who support its operations. Responsibilities of this group include conducting security vulnerability assessments, identification of security issues, investigations and implementation of security controls. As a recognized critical infrastructure operator, American Water maintains close contact with federal and state security organizations such as the Department of Homeland Security (DHS) and the EPA Water Security Division. Several members of the American Water's Operational Risk Management staff have been granted secret clearance through

DHS, which facilitates the flow of communication regarding emerging threats that could impact the water sector.

Emergency Plans. American Water has prepared an emergency plan guideline for employees containing a general outline for establishing an emergency plan for water and wastewater facilities. This guideline contains policies and procedures governing the response to a variety of emergencies. It is meant to be a general approach to conducting comprehensive vulnerability analyses of infrastructure and operations, to developing and testing an emergency plan that is integrated with other community emergency plans, and which includes provision for regular revision and communication of information to customers and the community at large. Although this document provides a solid foundation for the development of policies and procedures, modifications to fit site-specific requirements of individual facilities are required.

The document provides employees with the basis for establishing the information that will serve as the essential foundation of any emergency response plan—emergency staffing, notification procedures, emergency equipment and supplies, specific responses to various types of emergencies, and restoring operations when they have been curtailed.

The following are typical examples of measures taken at American Water facilities for specific emergencies:

CHEMICAL SPILLS. Chemical spills may occur either within the containment areas or elsewhere within a facility. Containment areas are configured and protected with the appropriate chemical resistant coatings to contain the contents of the storage tanks. The chemical will either be returned to the storage tank or collected within a local sump for disposal off-site. In the event of a leak outside the containment areas, the chemicals are diluted with water to prevent injury to employees or damage equipment. The diluted chemicals are collected and discharged either to the headworks if it will not impact the process or to recovery basins for treatment and disposal.

PERSONNEL EMERGENCY. Operators generally have access to telephones throughout facilities for voice communication, both internal and external to the facility. In addition to the telephones, the operators are also provided with mobile telephones, which can be utilized when traveling throughout the facilities they service. In the event of a personnel emergency, operators communicate with local police, first aid squads, and hospitals. Senior American Water managers are notified of all such situations, and ensure the needs of the staff are immediately provided as required.

FIRE. In the event of a fire, the staff will contact the Fire Department and, if possible, take the appropriate actions to contain/minimize the fire such as turning off the electrical power supply, using portable fire extinguishers, or closing fire separations. After contacting the local

fire department, the staff would contact American Water's regional office, providing details as to extent of fire, location, estimated damage, and impact on operation, impact on structure, impact on staff, need for additional resources.

PIPE, VALVE, OR PUMP FAILURE. In the event of a pipe or valve failure, the failed component will be isolated, removed and replaced. In the event of a pump failure, backup pumps will be utilized until the damaged unit is repaired. Appropriate repairs are undertaken either by the operations staff or subcontractors and equipment suppliers.

PROCESS FAILURE. A process failure is a deviation from the required performance criteria. Operators immediately stop the processing and take the required actions to attain performance standards. This may entail the isolation of the process unit, sampling of the process stream, analysis of the sample, adjustment of the chemical application rate, retesting and continued processing of the waste water.

POWER OUTAGES. American Water would craft a plan in collaboration with the City of Allentown so that back-up plans are appropriately developed and executed.

Safety Management. To ensure compliance with various environment, health, and safety regulations which govern our facilities, a scheduling program is implemented for each facility.

Staff Training and Development. American Water understands the close relationship between quality in operations and a well-trained staff. The company is diligent in ensuring that each employee receives extensive on-the-job operations and safety training so as to be able to perform the work required of them in a safe and efficient manner. To achieve this goal, a combination of classroom education and field training programs are typically provided.

Part of the safety training program includes behavioral-focused training tailored to the specific hazards at each facility. The program is used to train employees to instinctively recognize hazards, manage risks, care for themselves and fellow employees, and continuously seek to improve safety. The program includes best operating practices, government-required standards and site-specific safety requirements. The program covers the following topics, at a minimum:

- Hazard communication (Right-to-Know Training)
- Chemical inventory, storage, and handling procedures
- Lock-out/tag-out
- Fire prevention and fire extinguisher usage
- Confined spaces

AMERICAN WATER'S HEALTH AND SAFETY METRICS

- Monthly inspection results
- Safety training information
- Safety Committee Meeting information
- Number and topics of toolbox/tailgate safety sessions
- Number of corrective action requests generated
- Number of corrective requests completed on time
- Incident rates
- Total recordable incidents
- Lost-time incidents
- First aid cases
- Automobile incidents
- Near-misses

- Personal protective equipment
- Machine and tool safety
- Vehicle safety
- Hot work (welding, cutting and brazing)
- Ladder safety
- Laboratory safety
- Safety observations
- Safety audits
- Blood-borne pathogens
- Universal precautions for first aid and CPR
- Hearing conservation
- Contingency/emergency action plans
- Vulnerability assessments and security

B. Experience in Emergency Response Support

The company's ability to respond quickly and effectively to emergency situations was demonstrated when an F-5 tornado struck Joplin, Missouri on May 22, 2011. The force of the storm ripped at least 4,000 homes from their water service lines, immediately creating a huge number of system leaks.

Our response was accelerated because of regularly tested emergency operations plans and long-standing relationships with local emergency planning and response agencies. Additionally, we were able to quickly mobilize other entities within other service territories, which gave us the resources we needed when many local Joplin suppliers and contractors were not available. We were also able to deploy an additional 60 water service experts from corporate resources to restore full pressure in the entire system in just two days. A required boil order was lifted in just 5.5 days–an achievement that was recognized at the American Water Works Association's national convention.

Another example, in September, 2011, can be found in the company's response to flooding in Pennsylvania when, following on the heels of Hurricane Irene, Tropical Storm Lee dumped approximately 13 inches of rain in the Hershey area causing the Swatara Creek to rapidly overflow its banks and create major issues for residents, businesses, fire and emergency services, and utility companies.

Floodwaters shut down two of Pennsylvania American Water's three raw water pumps serving the water treatment plant and cut access to the intake building. In order to keep the third pump operating, Pennsylvania American Water connected with South Hanover Township emergency response personnel, who helped secure a state police helicopter. The helicopter airlifted firemen and employees to the pump station's roof where employees spent the night monitoring water levels and maintaining pumping operations.

Because nearby utilities were also experiencing problems, including plant shutdowns and boil water advisories, the emergency created a great deal of confusion, rumors and fear among water customers. In response, Pennsylvania American Water's communications team continually monitored its Facebook (www.facebook.com/pennsylvaniaamwater) and Twitter (www.twitter.com/paamwater) pages, as well as postings on the Facebook sites of *The Sun*, a local newspaper, and Derry Township Police Department. The team used social media to address numerous inquiries about boil water advisories, conservation measures and respond to false rumors that the water system was being shut down.

Despite the many challenges presented by Lee's historic flooding, the water quality supplied by Pennsylvania American Water was never compromised, no boil water advisories were necessary, and water service continued uninterrupted to customers throughout its service area. The credit for this accomplishment–in the face of incredible weather and flooding conditions–goes to the dozens of employees and managers who literally worked around the clock to monitor, stabilize and protect Pennsylvania American Water's East Shore system.

IV. Capital Improvements

American Water has an established track record of successfully managing large capital investment projects. Investment in treatment plants and underground pipes is important to keep utility operations safe and dependable. In order to continually provide reliable service to our communities, regular investment must be made to upgrade, replace and add new pipes, treatment and pumping facilities and other necessary water and wastewater infrastructure.

As we noted above, over the last several years and for the foreseeable future, company-funded capital investments for regulated subsidiaries are estimated to range between $800 million and $1 billion per year. Nearly half of this will be used for infrastructure renewal programs used to renew ageing assets replacing existing infrastructure such as mains, meters, and supply and treatment facilities as needed. Almost one quarter will go to projects to enhance system reliability, quality of service, and risk reduction while another quarter will go to meeting water quality standards and other regulatory requirements and capacity expansion projects.

In Pennsylvania alone, American Water has invested over $1 billion in the past five years on needed system improvements that allow us to continue to provide high quality water and wastewater service–from extending water mains to replacing meters and hydrants to upgrading plant equipment. In 2011, Pennsylvania American Water was awarded the Client of Distinction Award from the American Council of Engineering Companies of Pennsylvania (ACEC/PA) in relation to its capital work. The award recognized Pennsylvania American Water for its fair business practices, for focus on fostering a team-building atmosphere,

commitment to quality that goes above and beyond regulatory requirements, and commitment to completing projects on time and on budget.

In the "Engineering" section above, we discussed how capital planning is jointly performed by corporate engineering and operating subsidiaries staff who establish system capacity needs, regulatory impacts, service adequacy and reliability and determine project costs, alternatives and risks. Comprehensive, periodic assessment of our water and wastewater assets, as described above, gives American Water an objective view of needs and potential capital project solutions.

In the case of those systems it operates for public sector clients, American Water's capital improvement responsibilities are typically more limited since it does not own the infrastructure, although in the case of long-term concession agreements capital improvement activities are akin to those undertaken in American Water's regulated systems. In many contracts, the operating contract requires American Water to develop a rolling five-year capital improvement plan, with the recommendations presented annually to the local governing officials for implementation.

Examples of American Water Capital Construction in Pennsylvania. Pennsylvania American Water started construction last year on extensive upgrades to its G.C. Smith Water Treatment Plant located in Hershey. The approximately $7.7 million project includes expanding the plant's capacity to meet customer demand, replacing outdated control systems, adding safety features and installing new water treatment equipment to ensure that the facility continues to comply with all water quality standards.

CUMBERLAND AND YORK COUNTIES–In 2006, a new 12mgd water treatment plant was constructed, which serves customers on the West Shore. This new plant replaced two water treatment facilities, one of which dated back to the early 1900s. We also expanded the clearwell capacity of the Silver Spring Water Treatment Plant, which also serves the West Shore, to increase storage of treated water.

ALLEGHENY AND WASHINGTON COUNTIES–Pennsylvania American Water broke ground in June 2010 on the $101 million upgrade of its Pittsburgh area water treatment facilities, including the Hays Mine Water Treatment Plant, Becks Run Pumping Station, Arlington Avenue Booster Station and E.H. Aldrich Treatment Complex. The improvements included the construction of new chemical storage and feed facilities at the Hays Mine and E.H. Aldrich plants; a new 60mgd Becks Run Raw Water Pump Station and intake, two new finished water clearwell tanks with a combined capacity of 4.9 million gallons, and a new 60mgd finished water pump station at the Hays Mine plant; and the installation of two 2,000 kilowatt (kW) generators at the Becks Run Pump Station and two 2,500kW generators at the new Hays Mine pump station.

Financial Capability

I. Capacity to Make Upfront Payment, Maintain the Concession Assets

A. Financial Capacity

American Water is the largest publicly traded water and wastewater utility company in the U.S. In 2011, the company generated $2.7 billion in total operating revenue, a 4.4 percent increase over 2010 revenues of $2.6 billion. Operating income in 2011 totaled $803 million, compared to $728 million in 2010. The company's financial performance for the year resulted in income from continuing operations of $305 million—a 20 percent increase over the prior year. Our 2011 revenue represents approximately four times the operating revenue of the next largest publicly traded company in this U.S. sector.

For the year ended December 31, 2011, our regulated businesses, American Water's largest operating segment, generated $2.37 billion in operating revenue, representing 89.4 percent of the company's consolidated operating revenue compared to $2.28 billion in operating revenues in 2010 representing 90.4 percent of our consolidated operating revenue. Additionally, for the year ended December 31, 2011, our market-based operations generated $328 million in operating revenue, compared to $294.7 million in 2010.

In the two quarterly reports filed with the Security and Exchange Commission since the 2011 annual filing, the company reported continued increases in revenues, net income and earnings per share for both quarters, as compared to comparable periods the year before. Net cash provided by operating activities for the six months ended June 30, 2012, was $316.9 million, compared to $262.4 million for the second quarter in 2011, which was primarily driven by the increase in operating revenues and changes in working capital.

In the most recent Form 10-Q submitted on August 2, for the three months ended June 30, the company reported income from continuing operations of $116.7 million or diluted earnings per share of $0.66, compared with $74.8 million, or $0.42 per share for the comparable period in 2011. For the quarter, the company's revenues increased 11.5 percent, or $76.7 million, over the comparable quarter in 2011 to $745.6 million. Operating expenses for the three months ended June 30, 2012, totaled $475.0 million, an increase of $7.5 million, or 1.6 percent, compared to the same period in 2011.

In the appendix we have supplied digital copies of the last three years of American Water's audited financial statements. Because of their voluminous nature, we have included them on a USB thumb drive rather than as printed copies. All of the company's required financial reporting, including our Form 10-Ks containing the audited financials, can also be accessed through the American Water Investor Relations webpage available at http://ir.amwater.com.

We believe these filings, and the continual improving performance they represent, clearly demonstrate American Water's financial capability to enter into a long-term concession agreement with Allentown, to assume all operational costs of running the systems regardless of the term of that contract, and to provide the necessary financing to maintain and upgrade the concession assets.

Credit Rating

On July 18, Standard & Poor's Ratings Services reaffirmed its "BBB+" corporate credit rating and "A2" short-term commercial paper rating for American Water and American Water Capital Corp., the subsidiary through which American Water accesses the debt markets. Subsidiaries Pennsylvania-American Water and New Jersey American Water were also included in the reaffirmed ratings.

Standard and Poor's also revised its ratings outlook to "positive" from its previous "stable" rating for both American Water and American Water Capital Corp. Standard & Poor's stated its ratings for American Water and its subsidiaries reflect an "excellent" business risk profile and expectations that financial (rating) measures will remain around current levels. A favorable competitive position, a diverse and supportive regulatory environment, and stable service territories were also listed by Standard and Poor's as supporting American Water's excellent business risk profile.

On November 19, 2010, Moody's Investors Service, affirmed its "Baa2" corporate credit rating and "P2" short-term rating on American Water and American Water Capital Corp. Their rating outlook for both American Water and AWCC is "stable."

Our internal team of finance, legal, and engineering professionals have extensive experience in meeting the financing needs of all American Water activities. These professionals research, structure, and execute agreements involving the full range of financial transactions for the company–concessions, lease financing, acquisitions, private activity bonds, tax-exempt financing, and various state revolving funds.

II. Ability to Raise Financing

In Allentown, the upfront payment required to fund the agreement will require the commitment of substantial funds to the SPE that will enter into the concession with the City. These funds will be used to provide the concession fee to the City and for other purposes as may be negotiated as part of the concession contract. For a concession valued in the range that Allentown is considering, American Water has the requisite financing capacity to meet all obligations that may be agreed to by the parties during negotiations.

In addition to our ability to access the capital markets on reasonable terms (shown below with our recent debt issuance history), we have sufficient capacity in our revolving credit

facility to fund this transaction. This revolving credit facility is for $840 million until September 15, 2012 and $685 million thereafter and is with a variety of banking institutions. American Water would, subsequent to the initial funding, determine how and when it would be best to repay the credit lines, possibly raising some of the funds through either long-term debt or an equity offering or some combination thereof. It is possible, therefore, for American Water to complete this transaction without the need to access capital markets to meet our obligations. This presents minimal market risk to Allentown and allows the proposed project timeline to be met without exposing it to future market variables.

American Water regularly evaluates cash requirements for current operations, commitments, development activities and capital expenditures. Our business is focused on investing in and operating water and wastewater infrastructure. This business is very capital intensive and requires significant capital resources. A portion of these capital resources is provided by internally generated cash flows from operations. When necessary, we obtain additional funds from external sources in the debt and equity capital markets and through bank borrowings.

In its reaffirmation of American Water' corporate credit rating noted above, Standard and Poor's update noted several points relevant to the Allentown concession. In regard to American Water's liquidity, the rating agency stated American Water's liquidity sources during the next 12 months, including cash, funds from operations, and credit facility availability, should exceed uses by more than 1.2 times giving it financial resilience to unforeseen events with limited need for refinancing due to its flexibility to lower capital spending or sell assets, its sound bank relationships, its solid standing in credit markets, and its generally prudent risk management.

Capacity For Debt/Equity in the Current Capital Market

American Water primarily accesses the debt capital markets, including the commercial paper market, through American Water Capital Corp., a wholly owned subsidiary of American Water. American Water always seeks to find the lowest cost of debt and, where possible, we also issue debt in the form of tax exempt securities to lower our overall cost of debt.

Recent American Water Debt Issuances and Credit Ratings

Year of Issue	Amount	Issuer	Interest Rate	Date Due	S&P Rating	Moodys Rating
2009	$75M	AWCC	8.25%	2038	Not Rated	Not Rated
	$25.5M	AWCC	8.27%	2039	Not Rated	Not Rated
	$24.5M	AWCC	7.21%	2019	Not Rated	Not Rated
	$60M	AWCC	6%	2039	Not Rated	Not Rated
	$18.25M	AWCC	6%	2018	Baa2	BBB+
	$17.95M	AWCC	6.1%	2019	Baa2	BBB+
	$16.7M	AWCC	6.75%	2031	Baa2	BBB+
	45.4M	AWCC	6.25%	2039	Baa2	BBB+
	24.9M	AWCC	6.25%	2032	Baa2	BBB+
	23.3M	AWCC	6.25%	2032	Baa2	BBB+

Recent American Water Debt Issuances and Credit Ratings						
Year of Issue	Amount	Issuer	Interest Rate	Date Due	S&P Rating	Moodys Rating
	26M	AWCC	5.625%	2039	Baa2	BBB+
	28.5M	PAWC	5.25%	2039	Baa2	BBB+
	80M	NJAWC	6.2%	2039	A2	A
	134.2M	NJAWC	5.7%	2039	A2	A
	10.5M	NJAWC	5%	2039	A2	A
	75M	NJAWC	6.35%	2039	Not Rated	Not Rated
	25M	NJAWC	5.48%	2019	Not Rated	Not Rated
	80M (Remarketing)	PAWC			A2	A
	13M (Remarketing)	PAWC			A2	A
2010	25M	AWCC	5.25%	2040	Baa2	BBB+
	26M	AWCC	5.375%	2040	Baa2	BBB+
	15.3M	NJAWC	4.45%	2023	A2	A
	110M	NJAWC	5.60%	2034	A2	A
	24.7M	NJAWC	5.10%	2023	A2	A
	10.6M	AWCC	5.25%	2028	Baa2	BBB+
	35M	AWCC	5.25%	2040	Baa2	BBB+
	25M	AWCC	4.85%	2040	Baa2	BBB+
	35M	NJAWC	4.875%	2029	A2	A
	40M	NJAWC	4.70%	2025	A2	A
	30M	AWCC	6.00%	2040	Baa2	BBB+

Appendix

Audited Financial Reports - 2009-2011

American Water Works Company, Inc.

Audited Consolidated Financial Statement

Excerpted from SEC Form 10-K Annual Report
Filed on 02/28/2012

Filed Period 12/31/2011

AMERICAN WATER

Annual Report Available At : http://ir.amwater.com/phoenix.zhtml?c=215126&p=irol-sec

AUDITED CONSOLIDATED FINANCIAL STATEMENTS – 2011

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2011 and 2010

Consolidated Statements of Operations and Comprehensive Income (Loss) for the years ended December 31, 2011, 2010 and 2009

Consolidated Statements of Cash Flows for the years ended December 31, 2011, 2010 and 2009

Consolidated Statements of Changes in Common Stockholders' Equity for the years ended December 31, 2011, 2010 and 2009

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
American Water Works Company, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive income (loss), of cash flows, and of changes in common stockholders' equity, present fairly, in all material respects, the financial position of American Water Works Company, Inc. and Subsidiary Companies at December 31, 2011 and December 31, 2010, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 28, 2012

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Balance Sheets

(In thousands, except per share data)

	December 31,	
	2011	**2010**
ASSETS		
Property, plant and equipment		
Utility plant—at original cost, net of accumulated depreciation of $3,360,005 in 2011 and $3,134,094 in 2010	$ 10,872,042	$ 10,241,342
Nonutility property, net of accumulated depreciation of $164,417 in 2011 and $137,483 in 2010	149,056	140,298
Total property, plant and equipment	11,021,098	10,381,640
Current assets		
Cash and cash equivalents	14,207	13,112
Restricted funds	32,438	94,066
Utility customer accounts receivable	150,720	145,747
Allowance for uncollectible accounts	(15,319)	(17,474)
Unbilled utility revenues	134,938	132,876
Other receivables, net	60,413	71,589
Income taxes receivable	7,672	6,473
Materials and supplies	28,598	27,743
Assets of discontinued operations	929,858	937,705
Other	54,134	45,938
Total current assets	1,397,659	1,457,775
Regulatory and other long-term assets		
Regulatory assets	1,079,661	976,174
Restricted funds	25,503	26,718
Goodwill	1,195,069	1,195,585
Other	57,401	48,354
Total regulatory and other long-term assets	2,357,634	2,246,831
TOTAL ASSETS	$ 14,776,391	$ 14,086,246

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Balance Sheets—(Continued)
(In thousands, except per share data)

	December 31,	
	2011	2010
CAPITALIZATION AND LIABILITIES		
Capitalization		
Common stock ($.01 par value, 500,000 shares authorized, 175,664 shares outstanding in 2011 and 174,996 in 2010)	$ 1,757	$ 1,750
Paid-in capital	6,180,558	6,156,675
Accumulated deficit	(1,848,801)	(1,959,235)
Accumulated other comprehensive loss	(97,677)	(71,446)
Treasury stock	0	(19)
Common stockholders' equity	4,235,837	4,127,725
Preferred stock without mandatory redemption requirements	4,547	4,547
Total stockholders' equity	4,240,384	4,132,272
Long-term debt		
Long-term debt	5,339,947	5,394,135
Redeemable preferred stock at redemption value	21,137	22,135
Total capitalization	9,601,468	9,548,542
Current liabilities		
Short-term debt	515,050	228,905
Current portion of long-term debt	28,858	36,092
Accounts payable	243,709	188,343
Taxes accrued	36,606	36,939
Interest accrued	59,067	60,465
Liabilities of discontinued operations	382,218	373,960
Other	223,597	182,060
Total current liabilities	1,489,105	1,106,764
Regulatory and other long-term liabilities		
Advances for construction	386,970	397,164
Deferred income taxes	1,288,797	1,110,250
Deferred investment tax credits	29,427	30,969
Regulatory liabilities	325,829	296,121
Accrued pension expense	411,998	413,513
Accrued postretirement benefit expense	237,086	215,217
Other	38,963	42,150
Total regulatory and other long-term liabilities	2,719,070	2,505,384
Contributions in aid of construction	966,748	925,556
Commitments and contingencies (See Note 16)	—	—
TOTAL CAPITALIZATION AND LIABILITIES	$ 14,776,391	$ 14,086,246

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Operations and Comprehensive Income (Loss)

(In thousands, except per share data)

	Years Ended December 31,		
	2011	2010	2009
Operating revenues	$ 2,666,236	$ 2,555,035	$ 2,290,446
Operating expenses			
Operation and maintenance	1,301,794	1,290,941	1,182,376
Depreciation and amortization	351,821	330,264	309,874
General taxes	210,478	205,597	186,620
(Gain) loss on asset dispositions and purchases	(993)	111	(295)
Impairment charge	0	0	428,036
Total operating expenses, net	1,863,100	1,826,913	2,106,611
Operating income	803,136	728,122	183,835
Other income (expenses)			
Interest, net	(312,415)	(313,765)	(296,623)
Allowance for other funds used during construction	13,131	9,644	8,342
Allowance for borrowed funds used during construction	5,923	5,225	5,529
Amortization of debt expense	(5,055)	(4,516)	(6,609)
Other, net	(1,040)	4,714	(680)
Total other income (expenses)	(299,456)	(298,698)	(290,041)
Income (loss) from continuing operations before income taxes	503,680	429,424	(106,206)
Provision for income taxes	198,751	174,352	113,792
Income (loss) from continuing operations	304,929	255,072	(219,998)
Income (loss) from discontinued operations, net of tax	4,684	12,755	(13,085)
Net income (loss)	$ 309,613	$ 267,827	$ (233,083)
Other comprehensive income, net of tax:			
Change in employee benefit plan funded status, net of tax of $(19,498), $(7,567) and $6,381, respectively	(30,497)	(11,836)	9,981
Pension plan amortized to periodic benefit cost:			
Prior service cost, net of tax of $112, $50 and $29, respectively	175	79	46
Actuarial loss, net of tax of $2,879, $2,793 and $3,832, respectively	4,504	4,368	5,994
Foreign currency translation adjustment	(413)	620	1,553
Other comprehensive income	(26,231)	(6,769)	17,574
Comprehensive income (loss)	$ 283,382	$ 261,058	$ (215,509)
Basic earnings per common share: (a)			
Income (loss) from continuing operations	$ 1.74	$ 1.46	$ (1.31)
Income (loss) from discontinued operations, net of tax	$ 0.03	$ 0.07	$ (0.08)
Net income (loss)	$ 1.76	$ 1.53	$ (1.39)
Diluted earnings per common share: (a)			
Income (loss) from continuing operations	$ 1.73	$ 1.46	$ (1.31)
Income (loss) from discontinued operations, net of tax	$ 0.03	$ 0.07	$ (0.08)
Net income (loss)	$ 1.75	$ 1.53	$ (1.39)
Average common shares outstanding during the period:			
Basic	175,484	174,833	168,164
Diluted	176,531	175,124	168,164
Dividends per common share	$ 1.13	$ 0.86	$ 0.82

(a) Amounts may not sum due to rounding.

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Cash Flows

(In thousands, except per share data)

	Years Ended December 31,		
	2011	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income (loss)	$ 309,613	$ 267,827	$ (233,083)
Adjustments			
Depreciation and amortization	351,821	330,264	309,874
Impairment charge	0	0	428,036
Provision for deferred income taxes	195,494	152,760	134,232
Amortization of deferred investment tax credits	(1,542)	(1,561)	(1,413)
Provision for losses on utility accounts receivable	16,178	17,973	20,999
Allowance for other funds used during construction	(13,131)	(9,644)	(8,342)
(Gain) loss on asset dispositions and purchases	(993)	111	(295)
Pension and non-pension post retirement benefits	71,439	89,342	105,133
Stock-based compensation expense	10,008	10,334	7,602
Other, net	44,521	9,033	21,000
Changes in assets and liabilities			
Receivables and unbilled utility revenues	(17,433)	(33,044)	(18,751)
Taxes receivable, including income taxes	(1,199)	17,920	(17,920)
Other current assets	(14,917)	5,149	(6,737)
Pension and non-pension post retirement benefit contributions	(186,730)	(137,257)	(127,446)
Accounts payable	37,824	6,487	52
Taxes accrued, including income taxes	4,274	39,577	(13,321)
Interest accrued	(1,417)	746	6,499
Other current liabilities	4,547	8,916	(9,963)
Net cash provided by operating activities	808,357	774,933	596,156
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures	(924,858)	(765,636)	(785,265)
Acquisitions	(7,220)	(1,642)	(18,144)
Proceeds from sale of assets and securities	9,972	239	1,237
Removal costs from property, plant and equipment retirements, net	(53,134)	(43,695)	(29,900)
Net funds released	62,843	63,991	129,711
Other	0	0	(1,250)
Net cash used in investing activities	(912,397)	(746,743)	(703,611)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from long-term debt	12,510	268,559	542,926
Repayment of long-term debt	(70,045)	(272,700)	(178,131)
Proceeds from issuance of common stock (net of 2009 expenses of $7,824)	0	0	242,301
Net borrowings (repayments) under short-term debt agreements	303,024	93,029	(352,005)
Proceeds from issuances of employee stock plans and DRIP	13,866	6,711	2,089
Advances and contributions for construction, net of refunds of $21,061 in 2011, $35,830 in 2010 and $27,481 in 2009	22,298	7,042	21,211
Change in cash overdraft position	(16,862)	17,173	(7,508)
Debt issuance costs	(552)	(6,619)	(13,165)
Redemption of preferred stocks	(1,888)	(228)	(218)
Dividends paid	(157,855)	(150,301)	(137,331)
Other	639	0	0
Net cash provided by (used in) financing activities	105,135	(37,334)	120,169
Net increase (decrease) in cash and cash equivalents	1,095	(9,144)	12,714
Cash and cash equivalents at beginning of period	13,112	22,256	9,542
Cash and cash equivalents at end of period	$ 14,207	$ 13,112	$ 22,256
Cash paid during the year for:			
Interest, net of capitalized amount	$ 331,944	$ 329,417	$ 303,958
Income taxes, net of refunds of $812 in 2011, $37,790 in 2010 and $2,754 in 2009	$ 14,269	$ (30,108)	$ 11,205
Non-cash investing activity			
Capital expenditures acquired on account but unpaid as of year end	$ 104,816	$ 112,313	$ 59,219
Non-cash financing activity			
Advances and contributions	$ 23,504	$ 27,566	$ 77,094
Long-term debt	$ 0	$ 122,775	$ 179,931

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Changes in Stockholders' Equity

(In thousands, except per share data)

	Common Stock				Accumulated Other	Treasury Stock		Preferred Stock of Subsidiary Companies Without Mandatory	Total
	Shares	Par Value	Paid-in Capital	Accumulated Deficit	Comprehensive Loss	Shares	At Cost	Redemption Requirements	Stockholders' Equity
Balance at December 31, 2008	160,000	$1,600	$5,888,253	$(1,705,594)	$ (82,251)	0	$ (7)	$ 4,557	$ 4,106,558
Net loss	—	—	—	(233,083)	—	—	—	—	(233,083)
Common stock offering, net of expenses of $7,824	14,500	145	242,156	—	—	—	—	—	242,301
Employee stock purchase plan	128	1	2,453	—	—	1	23	—	2,477
Stock-based compensation activity	2	—	7,215	(279)	—	(1)	(16)	—	6,920
Other comprehensive income, net of tax of $10,242	—	—	—	—	17,574	—	—	—	17,574
Dividends	—	—	—	(137,331)	—	—	—	—	(137,331)
Balance at December 31, 2009	174,630	$1,746	$6,140,077	$(2,076,287)	$ (64,677)	0	$ 0	$ 4,557	$ 4,005,416
Net income	—	—	—	267,827	—	—	—	—	267,827
Direct stock reinvestment and purchase plan, net of expense of $96	63	1	1,328	—	—	—	—	—	1,329
Employee stock purchase plan	112	1	2,502	—	—	7	127	—	2,630
Stock-based compensation activity	191	2	12,768	(474)	—	(8)	(146)	—	12,150
Subsidiary preferred stock redemption	—	—	—	—	—	—	—	(10)	(10)
Other comprehensive loss, net of tax of ($4,724)	—	—	—	—	(6,769)	—	—	—	(6,769)
Dividends	—	—	—	(150,301)	—	—	—	—	(150,301)
Balance at December 31, 2010	174,996	$1,750	$6,156,675	$(1,959,235)	$ (71,446)	(1)	$ (19)	$ 4,547	$ 4,132,272
Net income	—	—	—	309,613	—	—	—	—	309,613
Direct stock reinvestment and purchase plan, net of expense of $19	64	1	1,807	—	—	—	—	—	1,808
Employee stock purchase plan	121	1	3,533	—	—	—	—	—	3,534
Stock-based compensation activity	483	5	18,543	(921)	—	1	19	—	17,646
Other comprehensive income (loss), net of tax of $(16,507)	—	—	—	—	(26,231)	—	—	—	(26,231)
Dividends	—	—	—	(198,258)	—	—	—	—	(198,258)
Balance at December 31, 2011	175,664	$1,757	$6,180,558	$(1,848,801)	$ (97,677)	0	$ 0	$ 4,547	$ 4,240,384

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Notes to Consolidated Financial Statements
(In thousands, except per share data)

Note 1: Organization and Operation

American Water Works Company, Inc. ("AWW") and its subsidiaries (collectively referred to herein as the "Company") is the holding company for regulated and market-based subsidiaries throughout the United States of America and two Canadian provinces. The regulated subsidiaries included in continuing operations provide water and wastewater services as public utilities. These regulated subsidiaries are operationally segregated into 16 U.S. states in which the Company operates regulated utilities. The market-based subsidiaries include various lines of business including Homeowner Services, which provides water and sewer line protection plans for homeowners, and the Contract Operations group, which conducts operation and maintenance of water and wastewater facilities for the U.S. Military, municipalities and the food and beverage industry.

Note 2: Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of AWW and its subsidiaries. Intercompany balances and transactions between subsidiaries have been eliminated. The Company uses the equity method to report its investments in two joint venture investments in each of which the Company holds a 50% voting interest and cannot exercise control over the operations and policies of the investments. Under the equity method, the Company records its interests as an investment and its percentage share of earnings as earnings or losses of investee.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The Company considers benefit plan assumptions; the carrying values of goodwill and other long-lived assets, including regulatory assets; revenue recognition; and accounting for income taxes to be its critical accounting estimates. The Company's significant estimates that are particularly sensitive to change in the near term are amounts reported for pension and other postemployment benefits, contingency-related obligations and goodwill.

Regulation

The Company's regulated utilities are subject to economic regulation by the public utility commissions and the local governments of the states in which they operate (the "Regulators"). These Regulators have allowed recovery of costs and credits which the Company has recorded as regulatory assets and liabilities. Accounting for future recovery of costs and credits as regulatory assets and liabilities is in accordance with authoritative guidance applicable to those companies whose rates are established by or are subject to approval by an independent third-party regulator. Regulated utilities defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate making process in a period different from the period in which they would have been reflected in operations by a market-based company. These deferred regulatory assets and liabilities are then reflected in the statement of operations in the period in which the costs and credits are reflected in the rates charged for service. (See Note 7)

Property, Plant and Equipment

Property, plant and equipment consist primarily of utility plant. Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. The costs incurred to acquire and internally develop computer software for internal use are capitalized as a unit of property. The carrying value of these costs amounted to $49,241 and $60,408 at December 31, 2011 and 2010, respectively. The cost of repairs; maintenance, including planned major maintenance activities; and minor replacements of property is charged to maintenance expense as incurred.

When units of property are replaced, retired or abandoned, the recorded value thereof is credited to the asset account and charged to accumulated depreciation. To the extent the Company recovers cost of removal or other retirement costs through rates after the retirement costs are incurred, a regulatory asset is recorded. In some cases, the Company recovers retirement costs through rates during the life of the associated asset and before the costs are incurred. These amounts result in a regulatory liability being reported based on the amounts previously recovered through customer rates, until the costs to retire those assets are incurred.

The cost of property, plant and equipment is depreciated using the straight-line average remaining life method.

Nonutility property consists primarily of buildings and equipment utilized by the Company for internal operations. This property is stated at cost, net of accumulated depreciation calculated using the straight-line method over the estimated useful lives of the assets, ranging from three to 50 years.

Cash and Cash Equivalents

Substantially all cash is invested in interest-bearing accounts. All highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

The Company had book overdrafts for certain of its disbursement accounts of $34,002 and $50,881 at December 31, 2011 and 2010, respectively. A book overdraft represents transactions that have not cleared the bank accounts at the end of the period. The Company transfers cash on an as-needed basis to fund these items as they clear the bank. The balance of the book overdraft is reported as short-term debt and the change in the book overdraft balance is reported as cash flows from financing activities.

Restricted Funds

Restricted funds primarily represent proceeds from financings for the construction and capital improvement of facilities and deposits for future services under operation and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within 12 months subsequent to year end are classified as current.

Utility Customer Accounts Receivable

Regulated utility customer accounts receivable represent amounts billed to water and wastewater customers on a cycle basis. Credit is extended based on the guidelines of the applicable Regulators and collateral is generally not required.

Allowance for Uncollectible Accounts

Allowances for uncollectible accounts are maintained for estimated probable losses resulting from the Company's inability to collect receivables from customers. Accounts that are outstanding longer than the payment terms are considered past due. A number of factors are considered in determining the allowance for uncollectible accounts, including the length of time receivables are past due and previous loss history. The Company writes off accounts when they become uncollectible. (See Note 5)

Other Receivables, Net

Other receivables, net consists of market-based trade accounts receivable and market-based unbilled revenues, net of a reserve for doubtful accounts, and non-utility customer receivables of the regulated subsidiaries. In determining the reserve for uncollectible market-based accounts, the Company considers the length of time the trade accounts receivable are past due and the customers' current ability to pay their obligations. Unbilled receivables are accrued when service has been provided but has not been billed to customers. (See Note 6)

Materials and Supplies

Materials and supplies are stated at the lower of cost or net realizable value. Cost is determined using the average cost method.

Goodwill

Goodwill is primarily associated with the acquisitions of AWW in 2003 and E'town Corporation in 2001 (the "Acquisitions") and has been assigned to reporting units based on the fair values at the date of the Acquisitions. The Regulated Businesses segment is a single reporting unit. In the Market-Based Operations segment, the business is organized into seven reporting units for its market-based services. Goodwill is reviewed annually, or more frequently if changes in circumstances indicate the carrying value may not be recoverable. Annual impairment reviews are performed in the fourth quarter of the calendar year, in conjunction with the timing of the completion of the Company's annual strategic business plan.

The Company considers the carrying value of goodwill to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to value goodwill to be appropriate. However, if experience differs from the assumptions and considerations used in its analysis, the resulting change could have a material adverse impact on the consolidated financial statements.

No impairment charge was recorded in the Company's continuing operations for the years ended December 31, 2011 and 2010, respectively. For the year ended December 31, 2009, the Company recorded goodwill impairment charges to continuing operations of $428,036. (See Note 8)

Long-Lived Assets

Long-lived assets include land, buildings, equipment and long-term investments. Long-lived assets, other than investments and land, are depreciated over their estimated useful lives, and are reviewed for impairment whenever changes in circumstances indicate the carrying value of the asset may not be recoverable. Such circumstances would include items such as a significant decrease in the market value of a long-lived asset, a significant adverse change in the manner the asset is being used or planned to be used or in its physical condition, or a history of operating or cash flow losses associated with the use of the asset. In addition, changes in the expected useful life of these long-lived assets may also be an impairment indicator. When such events or changes occur, the Company estimates the fair value of the asset from future cash flows expected to result from the use and, if applicable, the eventual disposition of the assets and compares that to the carrying value of the asset. If the carrying value is greater than the fair value, an impairment loss is recorded.

The Company considers the carrying value of long-lived assets to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to evaluate the carrying value of long-lived assets to be appropriate. However, if actual experience differs from the assumptions and considerations used in its estimates, the resulting change could have a material adverse impact on the consolidated financial statements.

The key variables to determine value include assumptions regarding sales volume, rates, operating costs, labor and other benefit costs, capital additions, assumed discount rates and other economic factors. These

variables require significant management judgment and include inherent uncertainties since they are forecasting future events. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

The long-lived assets of the regulated utility subsidiaries are grouped on a separate entity basis for impairment testing as they are integrated state-wide operations that do not have the option to curtail service and generally have uniform tariffs. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

The Company holds other investments including investments in privately held companies and investments in joint ventures accounted for using the equity method. The Company's investments in privately held companies and joint ventures are classified as other long-term assets.

The fair values of long-term investments are dependent on the financial performance and solvency of the entities in which the Company invests, as well as volatility inherent in the external markets. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

Advances and Contributions in Aid of Construction

Regulated utility subsidiaries may receive advances and contributions from customers, home builders and real estate developers to fund construction necessary to extend service to new areas. Advances for construction are refundable for limited periods of time as new customers begin to receive service or other contractual obligations are fulfilled. Included in other current liabilities at December 31, 2011 and 2010 in the accompanying Consolidated Balance Sheets are estimated refunds of $18,681 and $22,451, respectively. Those amounts represent expected refunds during the next 12-month period. Advances that are no longer refundable are reclassified to contributions in aid of construction. Contributions in aid of construction are permanent collections of plant assets or cash for a particular construction project. For ratemaking purposes, the amount of such contributions generally serves as a rate base reduction since the contributions represent non-investor supplied funds.

Generally, the Company depreciates utility plant funded by contributions and amortizes its contributions balance as a reduction to depreciation expense, producing a result which is functionally equivalent to reducing the original cost of the utility plant for the contributions. Certain of the Company's subsidiaries do not depreciate contributed property, based on regulatory guidelines. Amortization of contributions in aid of construction was $18,327, $17,423 and $16,371 for the years ended December 31, 2011, 2010 and 2009, respectively.

Recognition of Revenues

Revenues of the regulated utility subsidiaries are recognized as water and wastewater services are provided and include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

The Company has agreements with the United States Government to operate and maintain water and wastewater systems at various military bases pursuant to 50-year contracts ("military agreements"). These contracts also include construction components that are accounted for separately from the operations and management components. The military agreements are subject to periodic price redetermination adjustments and modifications for changes in circumstance. Additionally, the Company has agreements ranging in length from two to 40 years with various industries and municipalities to operate and maintain water and wastewater systems ("O&M agreements"). Revenue from operations and management services are recognized as services are provided. (See Note 16)

Construction Contracts

Revenues from construction projects are recognized over the contract term based on the estimated percentage of completion during the period compared to the total estimated services to be provided over the entire contract. Losses on contracts are recognized during the period in which the loss first becomes probable and estimable. Revenues recognized during the period in excess of billings on construction contracts are recorded as unbilled revenue. Billings in excess of revenues recognized on construction contracts are recorded as other current liabilities until the recognition criteria are met. Changes in contract performance and related estimated contract profitability may result in revisions to costs and revenues and are recognized in the period in which revisions are determined.

Income Taxes

AWW and its subsidiaries participate in a consolidated federal income tax return for U.S. tax purposes. Members of the consolidated group are charged with the amount of federal income tax expense determined as if they filed separate returns.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. The Company provides deferred income taxes on the difference between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates expected to be in effect when these temporary differences are projected to reverse. In addition, the regulated utility subsidiaries recognize regulatory assets and liabilities for the effect on revenues expected to be realized as the tax effects of temporary differences, previously flowed through to customers, reverse.

Investment tax credits have been deferred by the regulated utility subsidiaries and are being amortized to income over the average estimated service lives of the related assets.

The Company recognizes accrued interest and penalties related to tax positions as a component of income tax expense and accounts for sales tax collected from customers and remitted to taxing authorities on a net basis.

Allowance for Funds Used During Construction ("AFUDC")

AFUDC is a non-cash credit to income with a corresponding charge to utility plant that represents the cost of borrowed funds or a return on equity funds devoted to plant under construction. The regulated utility subsidiaries record AFUDC to the extent permitted by the Regulators.

Environmental Costs

The Company's water and wastewater operations are subject to federal, state, local and foreign requirements relating to environmental protection, and as such, the Company periodically becomes subject to environmental claims in the normal course of business. Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued, on an undiscounted basis, when it is probable that these costs will be incurred and can be reasonably estimated. Remediation costs accrued amounted to $5,500 and $6,630 at December 31, 2011 and 2010, respectively. At December 31, 2011, the entire accrual relates to a conservation agreement entered into by a subsidiary of the Company with the National Oceanic and Atmospheric Administration ("NOAA") requiring the Company to, among other provisions, implement certain measures to protect the steelhead trout and its habitat in the Carmel River watershed in the state of California. The Company paid and expensed $3,500 related to this agreement during 2009, and has agreed to pay $1,100 annually from 2010 to 2016. The Company pursues recovery of incurred costs through all appropriate means, including regulatory recovery through customer rates. The Company's regulatory assets at December 31, 2011 and 2010 include $9,187 and $10,642, respectively, related to the NOAA agreement, including an additional $3,500 granted in 2010 for recovery of the 2009 payment.

Derivative Financial Instruments

The Company uses derivative financial instruments for purposes of hedging exposures to fluctuations in interest rates. These derivative contracts are entered into for periods consistent with the related underlying exposures and do not constitute positions independent of those exposures. The Company does not enter into derivative contracts for speculative purposes and does not use leveraged instruments.

All derivatives are recognized on the balance sheet at fair value. On the date the derivative contract is entered into, the Company may designate the derivative as a hedge of the fair value of a recognized asset or liability (fair-value hedge) or a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash-flow hedge).

Changes in the fair value of a fair-value hedge, along with the gain or loss on the underlying hedged item, are recorded in current-period earnings. The effective portion of gains and losses on cash-flow hedges are recorded in other comprehensive income (loss), until earnings are affected by the variability of cash flows. Any ineffective portion of designated hedges is recognized in current-period earnings.

Cash flows from derivative contracts are included in net cash provided by operating activities.

New Accounting Standards

The following recently announced accounting standards have been adopted by the Company and have been included in the consolidated results of operations, financial position or footnotes of the accompanying Consolidated Financial Statements:

Revenue Arrangements with Multiple Deliverables

In October 2009, the Financial Accounting Standards Board ("FASB") issued authoritative guidance that amends existing guidance for identifying separate deliverables in a revenue-generating transaction where multiple deliverables exist, and provides guidance for allocating and recognizing revenue based on those separate deliverables. The guidance is expected to result in more multiple-deliverable arrangements being separable than under current guidance. This guidance is effective for the Company beginning on January 1, 2011 and is required to be applied prospectively to new or significantly modified revenue arrangements. The adoption of this guidance did not have a significant impact on the Company's results of operations, financial position or cash flows.

Business Combinations

In December 2010, the FASB clarified the requirements for reporting of pro forma revenue and earnings disclosures for business combinations. The accounting update specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments are effective for the Company for business combinations finalized after January 1, 2011. As this guidance clarifies and provides for additional disclosure requirements only, the adoption of this guidance has not had an impact on the Company's results of operations, financial position or cash flows.

Intangibles—Goodwill

In December 2010, the FASB issued authoritative guidance that modifies step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. The update requires that for those reporting units, an entity is required to perform step 2 of the goodwill impairment test if it is more likely than not that a goodwill

impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that impairment may exist. Existing authoritative guidance requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. This guidance is effective for the Company beginning on January 1, 2011. The adoption of this update did not have a significant impact on the Company's results of operations, financial position or cash flows.

The following recently issued accounting standards are not yet required to be adopted by the Company or included in the consolidated results of operations or financial position of the Company:

Fair Value Measurements

In May 2011, the FASB issued updated accounting guidance related to fair value measurements and disclosures that result in common fair value measurements and disclosures between U.S. GAAP and International Financial Reporting Standards. This new guidance amends current fair value measurement and disclosure guidance to increase transparency around valuation inputs and investment categorization. This guidance is effective for interim and annual periods beginning after December 15, 2011. The new guidance is to be adopted prospectively and early adoption is not permitted. The Company does not expect the adoption of this guidance to have a significant impact on the Company's results of operations, financial position or cash flows.

Comprehensive Income

In June 2011, the FASB issued guidance on the presentation of comprehensive income. The new guidance allows an entity to present components of net income and other comprehensive income in one continuous statement or in two separate, but consecutive statements. The new guidance eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. While the new guidance changes the presentation of comprehensive income, there are no changes to the components that are recognized in net income or other comprehensive income under current accounting guidance. In December 2011, the FASB deferred the requirement to present reclassification adjustments of other comprehensive income on the face of the income statement. The new guidance is effective for fiscal years and interim periods beginning after December 15, 2011. As the Company already presents the components of net income and other comprehensive income in one continuous statement, the adoption of the new guidance will not have an impact on its results of operations, financial position or cash flows.

Testing Goodwill for Impairment

In September 2011, the FASB updated the accounting guidance related to testing goodwill for impairment. This update permits an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test that is currently in place. Under the new guidance, an entity will not be required to calculate the fair value of a reporting unit unless the entity determines, based on the qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. This update is effective for annual and interim goodwill impairment tests performed in fiscal years beginning after December 15, 2011; however, early adoption is permitted. The Company is evaluating the specific provisions of the updated guidance, but does not expect the adoption of this guidance to have a significant impact on the Company's results of operations, financial position or cash flows.

Reclassifications

Certain reclassifications for discontinued operations (see Note 3) have been made to conform previously reported data to the current presentation.

Note 3: Acquisitions and Divestitures

Acquisitions

During 2011, the Company closed on nine acquisitions of regulated water and wastewater systems for an aggregate purchase price of $7,220. The purchase price for each acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired totaled $12,919, of which $12,814 was utility plant. Liabilities assumed totaled $4,945, including contributions in aid of construction of $3,847. The Company recorded gains on acquisitions during 2011 totaling $754.

In July of 2011, the Company entered into an agreement to purchase seven regulated water systems in New York for approximately $71,000, adding approximately fifty thousand customers to its regulated operations. This transaction is subject to customary closing conditions including regulatory approval in New York and is expected to close in the first half of 2012.

During 2010, the Company closed on six acquisitions of regulated water and wastewater systems for an aggregate purchase price of $1,642. The purchase price for each acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired consisted of plant and equipment of $3,064. Liabilities assumed totaled $1,422, including contributions in aid of construction of $1,109 and regulatory liabilities of $313.

During 2009, the Company closed on seven acquisitions (six regulated water and wastewater systems, and one in its Market-Based Operations segment) for an aggregate purchase price of $18,144. The purchase price for each acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired totaled $29,462, including plant and equipment of $17,843, current assets of $5,857, goodwill of $606, and long-lived assets of $5,156. Liabilities assumed totaled $11,318, including debt of $3,990, current liabilities of $5,732, long-term liabilities of $970, and contributions in aid of construction of $626.

Divestitures

As part of the Company's strategic review of its business investments, it has entered into agreements to sell assets or stock of certain subsidiaries.

In June 2011, the Company completed the sale of the assets of its Texas regulated subsidiary for proceeds of $6,245. A gain on the sale of the assets has been recognized for $142 ($87 after tax). In the first quarter of 2011, the Company recognized a pretax impairment charge of $561 for the goodwill associated with the Texas subsidiary.

In January of 2012, the Company received approximately $461,000 in proceeds as a result of completing the sale of its Arizona and New Mexico subsidiaries. The sale is subject to certain post-closing adjustments. In the first quarter of 2011, the Company evaluated the pending sale and recorded an impairment charge totaling $21,428 pretax and $21,099 after tax to reduce parent company goodwill associated with these subsidiaries to their net realizable value.

The Company has also entered into an agreement to sell the stock of its Ohio subsidiary. The sale price is currently estimated at approximately $89,000, plus assumed liabilities, for an estimated enterprise value of approximately $120,000. The sale is subject to certain closing adjustments. In February 2012, the Ohio public utility commission approved the sale. Closing of this sale is expected during the first half of 2012. In the second quarter of 2011, the Company updated its evaluation of the pending sale and recorded an impairment charge totaling $3,510 pretax and $3,456 after tax to reduce parent company goodwill associated with this subsidiary to its net realizable value.

In December 2011, the Company completed the sale of its Applied Water Management subsidiary, part of its Market-Based Operations segment. Proceeds from the sale totaled $2,923. The Company recorded a pre- and post-tax loss on sale of $3,126 and $2,032, respectively.

The Company plans to use the majority of the proceeds from the above sales to reduce debt financing.

Charges recorded in connection with the discontinued operations and disposals of businesses include estimates that are subject to subsequent adjustments.

Operating results and the financial position of the five subsidiaries named above are included in the accompanying financial statements as discontinued operations.

A summary of discontinued operations presented in the Consolidated Statements of Operations and Comprehensive Income follows:

	Years Ended December 31,		
	2011	2010	2009
Operating revenues	$ 173,447	$ 155,642	$ 150,257
Total operating expenses, net	147,012	135,673	160,483
Operating income (loss)	26,435	19,969	(10,226)
Other income (expense), net	(270)	43	4,767
Income (loss) from discontinued operations before income taxes	26,165	20,012	(5,459)
Provision for income taxes	21,481	7,257	7,626
Income (loss) from discontinued operations, net of tax	$ 4,684	$ 12,755	$ (13,085)

Operating expenses were lower in 2011 due to the cessation of depreciation for assets held for sale totaling $24,807 for the year ended December 31, 2011. Operating expenses in 2009 include an allocated impairment charge of $21,964.

Assets and liabilities of discontinued operations in the accompanying Consolidated Balance Sheets include the following:

	December 31, 2011	December 31, 2010
Assets:		
Total property, plant and equipment	$ 833,023	$ 819,977
Current assets	21,906	20,710
Regulatory assets	43,849	39,833
Goodwill	29,608	55,107
Other	1,472	2,078
Total assets of discontinued operations	$ 929,858	$ 937,705
Liabilities:		
Long-term debt	$ 11,697	$ 17,272
Current portion of long-term debt	12,839	8,668
Other current liabilities	29,530	39,505
Advances for construction	205,034	214,045
Regulatory liabilities	4,617	7,622
Other	15,540	(4,058)
Contributions in aid of construction	102,961	90,906
Total liabilities of discontinued operations	$ 382,218	$ 373,960

Table of Contents

Note 4: Utility Plant

The components of utility plant by category at December 31 are as follows:

	Range of Remaining Useful Lives	2011	2010
Water plant			
Land and other non-depreciable assets		$ 128,286	$ 125,648
Sources of supply	20 to 127 Years	565,301	527,552
Treatment and pumping facilities	3 to 101 Years	2,665,525	2,524,241
Transmission and distribution facilities	9 to 127 Years	6,632,828	6,333,032
Services, meters and fire hydrants	6 to 96 Years	2,539,696	2,402,038
General structures and equipment	3 to 112 Years	693,880	643,973
Wastewater plant	4 to 86 Years	546,002	519,219
Construction work in progress		460,529	299,733
		14,232,047	13,375,436
Less accumulated depreciation		3,360,005	3,134,094
		$ 10,872,042	$ 10,241,342

Utility plant depreciation expense of continuing operations amounted to $268,987 in 2011, $250,107 in 2010 and $237,741 in 2009. The Company's regulated utility subsidiaries record depreciation in conformity with amounts approved by state regulators after regulatory review of information the Company submits to support its estimates of the assets' remaining useful lives.

The provision for depreciation expressed as a percentage of the aggregate average depreciable asset balances was 2.68% in 2011, and 2.62% in 2010 and 2009, respectively.

Note 5: Allowance for Uncollectible Accounts

The following table summarizes the changes in the Company's allowances for uncollectible accounts:

	2011	2010	2009
Balance at January 1	$ (17,474)	$ (18,148)	$ (16,859)
Amounts charged to expense	(16,178)	(17,973)	(20,999)
Amounts written off	21,855	22,124	23,104
Recoveries of amounts written off	(3,522)	(3,477)	(3,394)
Balance at December 31	$ (15,319)	$ (17,474)	$ (18,148)

Note 6: Other Receivables, Net

Components of the Company's other receivables, net at December 31 are as follows:

	2011	2010
Market-based trade accounts receivable	$ 26,734	$ 36,357
Allowance for doubtful accounts—market-based trade accounts receivable	(3,067)	(3,015)
Market-based unbilled revenue	14,367	14,273
Other	22,379	23,974
	$ 60,413	$ 71,589

The following table summarizes the changes in the Company's market-based allowances for uncollectible accounts:

	2011	2010	2009
Balance at January 1	$ (3,015)	$ (3,520)	$ (4,622)
Amounts charged to (expense) income	(3,583)	(223)	796
Amounts written off	2,886	748	476
Recoveries of amounts written off	645	(20)	(170)
Balance at December 31	$ (3,067)	$ (3,015)	$ (3,520)

Note 7: Regulatory Assets and Liabilities

The regulatory assets represent costs that are expected to be fully recovered from customers in future rates. Except for income taxes, regulatory assets are excluded from the Company's rate base and generally do not earn a return. The components of regulatory assets at December 31 are as follows:

	2011	2010
Income taxes recoverable through rates	$ 252,570	$ 247,104
Debt and preferred stock expense	73,096	76,278
Deferred pension expense	256,858	207,633
Deferred other postretirement benefit expense	149,393	126,894
Deferred security costs	4,837	7,479
Deferred business services project expense	8,776	10,670
Deferred tank painting costs	29,500	26,924
Deferred rate case expense	14,553	9,322
Purchase premium recoverable through rates	60,635	60,647
Environmental remediation recoverable through rates	9,187	10,642
Coastal water project costs	24,419	27,084
San Clemente Dam project costs	22,890	18,723
Removal costs recoverable through rates	80,402	59,317
Other	92,545	87,457
	$ 1,079,661	$ 976,174

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the regulatory authorities of full normalization for rate making purposes. Full normalization requires no flow through of tax benefits to customers. The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets.

Debt expense is amortized over the lives of the respective issues. Call premiums on the redemption of long-term debt, as well as unamortized debt expense, are deferred and amortized to the extent they will be recovered through future service rates. Expenses of preferred stock issues without sinking fund provisions are amortized over 30 years from date of issue; expenses of issues with sinking fund provisions are charged to operations as shares are retired.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain subsidiaries. These costs will be recovered in future service rates as contributions are made to the pension plan. The Company

also has regulatory assets of $243,926 and $180,200 at December 31, 2011 and 2010, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

Postretirement benefit expense in excess of the amount recovered in rates through 1997 has been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service and will be recovered as authorized by the Company's regulatory authorities. The Company also has regulatory assets of $147,441 and $121,665 at December 31, 2011 and 2010, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

The costs of additional security measures that were implemented to protect facilities after the terrorist attacks on September 11, 2001 have been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service by certain subsidiaries. These costs are being recovered over periods ranging from five to ten years from the time of regulatory approval.

Business services project expenses consist of reengineering and start-up activities for consolidated customer and shared administrative service centers that began operations in 2001. These costs are recognized in the rates charged for water service by certain subsidiaries.

Tank painting costs are generally deferred and amortized to current operations on a straight-line basis over periods ranging from two to 15 years, as authorized by the regulatory authorities in their determination of rates charged for service.

The Company amortizes rate case expenditures over regulatory approved amortization periods, typically three years. Rate case proceeding expenditures probable of future recovery are deferred.

Purchase premium recoverable through rates is primarily the recovery of the acquisition premiums related to an asset acquisition by the Company's California subsidiary during 2002, and acquisitions in 2007 by the Company's New Jersey subsidiary. As authorized for recovery by the California and New Jersey Regulators, these costs are being amortized to operations through November 2048.

Environmental remediation recoverable through rates is the recovery of costs incurred by the Company's California subsidiary under a settlement agreement entered into with NOAA to improve habitat conditions in the Carmel River Watershed.

Coastal water project costs include preliminary costs associated with the studying, testing and design of alternatives to help solve water supply shortages in Monterey, California. Coastal water project costs incurred through December 31, 2009 have been reviewed and approved for recovery through a surcharge. Costs deferred during 2011 and 2010 totaled $2,528 and $7,677, respectively. The Company believes it is probable that the costs incurred since the last rate review will also be recoverable.

San Clemente Dam project costs include deferred costs for the Company's California subsidiary to investigate alternatives to strengthen or remove the San Clemente Dam due to potential earthquake or flood safety concerns. In November 2011, a Proposed Decision ("PD") was issued by the Administrative Law Judge ("ALJ") assigned to the matter. In the PD, the ALJ recommended that recovery of virtually all of the historical costs should be disallowed. The Company's California subsidiary has filed comments with the California Public Utility Commission ("CPUC") contending that the PD is unreasonable, unsupported by and contrary to the evidence, and contrary to law and policy. The PD is currently under review by the CPUC, which has delayed issuing a decision on several occasions and most recently has indicated that it will not vote on a decision until April 2012. The Company believes there are sound reasons for the CPUC to modify the PD to permit recovery of the historical costs. These costs are not yet in rates; however, the Company believes it is probable that the costs incurred will be recoverable.

Other regulatory assets include certain deferred employee benefit costs, deferred treatment facility costs, as well as various regulatory balancing accounts.

The components of regulatory liabilities at December 31 are as follows:

	2011	2010
Removal costs recovered through rates	$ 272,618	$ 260,947
Other	53,211	35,174
	$ 325,829	$ 296,121

Removal costs recovered through rates are retirement costs recovered during the life of the associated assets. In December 2008, the Company's subsidiary in New Jersey, at the direction of the New Jersey Regulator, began to amortize $48,000 of the total balance into operations via straight line amortization through November 2048.

Other regulatory liabilities include legal settlement proceeds, deferred gains, future customer refunds, and various regulatory balancing accounts. The Company's increased pension contributions in 2011 resulted in increased pension balancing accounts.

Note 8: Goodwill

The Company's annual impairment reviews are performed as of November 30 of each year, in conjunction with the completion of the Company's annual strategic business plan. At November 30, 2011, the Company's goodwill was $1,195,069. The Company also undertakes interim reviews when the Company determines that a triggering event that would more likely than not reduce the fair value of a reporting unit below its carrying value has occurred.

The Company uses a two-step impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). The step 1 calculation used to identify potential impairment compares the calculated fair value for each of the Company's reporting units to their respective net carrying values (book values), including goodwill, on the measurement date. If the fair value of any reporting unit is less than such reporting unit's carrying value, then step 2 is performed to measure the amount of the impairment loss (if any) for such reporting unit.

The step 2 calculation of the impairment test compares, by reporting unit, the implied fair value of the goodwill to the carrying value of goodwill. The implied fair value of goodwill is equal to the excess of the fair value of each reporting unit above the fair value of such reporting unit's identified assets and liabilities. If the carrying value of goodwill exceeds the implied fair value of goodwill for any reporting unit, an impairment loss is recognized in an amount equal to the excess (not to exceed the carrying value of goodwill) for that reporting unit.

The determination of the fair value of each reporting unit and the fair value of each reporting unit's assets and liabilities is performed as of the measurement date using observable market data before and after the measurement date (if that subsequent information is relevant to the fair value on the measurement date).

For the November 30, 2011 impairment test, the estimated fair value of each reporting unit for step 1 was based on a combination of the following valuation techniques:

- observable trading prices of comparable equity securities considered to be the Company's peers; and
- discounted cash flow models developed from the Company's internal forecasts.

The first valuation technique applies average peer multiples to each reporting unit's historic and forecasted cash flows. The peer multiples are calculated using the average trading prices of comparable equity securities, their published cash flows and forecasts of market prices and cash flows for those peers.

The second valuation technique forecasts each reporting unit's five-year cash flows using an estimated long-term growth rate and discounts these cash flows at their respective estimated weighted average cost of capital.

The Company has completed its November 30, 2011 annual impairment review. Based on this review, the Company's goodwill balance was not impaired. The Company's fair value calculated in its 2011 impairment test period was greater than the aggregate carrying value of its reporting units.

However, there can be no assurances that the Company will not be required to recognize an impairment of goodwill in the future due to market conditions or other factors related to the Company's performance. These market events could include a decline over a period of time of the Company's stock price, a decline over a period of time in valuation multiples of comparable water utilities, the lack of an increase in the Company's market price consistent with its peer companies, or decreases in control premiums. A decline in the forecasted results in the Company's business plan, such as changes in rate case results or capital investment budgets or changes in the Company's interest rates, could also result in an impairment charge.

The Company also made certain assumptions, which it believes to be appropriate, that support the fair value of its reporting units. The Company considered, in addition to the listed trading price of the Company's shares, the applicability of a control premium to the Company's shares and certain other factors the Company deemed appropriate. As a result, the Company concluded that the Company's fair value exceeds what the Company might otherwise have concluded had it relied on market price alone.

The difference between the Company's calculated market capitalization (which approximates carrying value) and the aggregate fair value of reporting units resulted from an estimated control premium. The estimated control premium represents the incremental premium a buyer is willing to pay to acquire a controlling, majority interest in the Company. In estimating the control premium, management principally considered the current market conditions and historical premiums paid in utility acquisitions observed in the marketplace.

No impairment charge was recorded to the Company's continuing operations for the years ended December 31, 2011 and 2010, respectively. For the year ended December 31, 2009, the Company recorded impairment charges for goodwill in the amount of $428,036.

The change in the Company's goodwill assets, as allocated between the reporting units is as follows:

	Regulated Unit		Market-Based Units		Consolidated		
	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Total Net
Balance at January 1, 2010	$ 3,399,848	$ (2,332,670)	$ 235,715	$ (107,619)	$ 3,635,563	$ (2,440,289)	$ 1,195,274
Reclassifications and other activity	36	0	275	0	311	0	311
Balance at December 31, 2010	$ 3,399,884	$ (2,332,670)	$ 235,990	$ (107,619)	$ 3,635,874	$ (2,440,289)	$ 1,195,585
Reclassifications and other activity	(516)	0	0	0	(516)	0	(516)
Balance at December 31, 2011	$ 3,399,368	$ (2,332,670)	$ 235,990	$ (107,619)	$ 3,635,358	$ (2,440,289)	$ 1,195,069

Note 9: Stockholders' Equity

Common Stock

In March 2010, the Company established American Water Stock Direct, a dividend reinvestment and direct stock purchase plan (the "DRIP"). Under the DRIP, stockholders may reinvest cash dividends and purchase

additional Company common stock, up to certain limits, through a transfer agent without commission fees. The Company's transfer agent may buy newly issued shares directly from the Company or shares held in the Company's treasury. The transfer agent may also buy shares in the public markets or in privately negotiated transactions. Purchases generally are made and credited to DRIP accounts once each week. As of December 31, 2011, there were 4,873 shares available for future issuance under the DRIP. The following table summarizes information regarding issuances under the DRIP for the years ended December 31, 2011 and 2010:

	2011	2010
Shares of common stock issued	64	63
Cash proceeds received	$ 1,827	$ 1,425

Cash dividend payments made during 2011 and 2010 were as follows:

	2011	2010
Dividends per share, three months ended:		
March 31	$ 0.22	$ 0.21
June 30	0.22	0.21
September 30	0.23	0.22
December 31	0.23	0.22
Total dividends paid, three months ended:		
March 31	$ 38,525	$ 36,679
June 30	38,580	36,689
September 30	40,358	38,457
December 31	40,392	38,476

On December 9, 2011, the Company declared a quarterly cash dividend payment of $0.23 per share payable on March 1, 2012 to all shareholders of record as of February 3, 2012. As of December 31, 2011, the Company had accrued dividends totaling $40,403 included in Other current liabilities in the accompanying Consolidated Balance Sheets.

Accumulated Other Comprehensive Loss

The following table presents accumulated other comprehensive loss:

	2011	2010
Employee benefit plans funded status adjustments	$ (101,457)	$ (75,639)
Foreign currency translation	3,780	4,193
Balance at December 31	$ (97,677)	$ (71,446)

Stock Based Compensation

The Company has granted stock option and restricted stock unit awards to non-employee directors, officers and other key employees of the Company pursuant to the terms of its 2007 Omnibus Equity Compensation Plan (the "Plan"). The total aggregate number of shares of common stock that may be issued under the Plan is 15,500. As of December 31, 2011, a total of 10,948 shares are available for grant under the Plan. Shares issued under the Plan may be authorized but unissued shares of Company stock or reacquired shares of Company stock, including shares purchased by the Company on the open market for purposes of the Plan.

The Company recognizes compensation expense for stock awards over the vesting period of the award. The following table presents stock-based compensation expense recorded in operation and maintenance expense in

the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss) for the years ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Stock options	$ 3,182	$ 4,116	$ 3,415
Restricted stock units	6,340	5,863	3,799
Employee stock purchase plan	486	355	388
Stock-based compensation in operation and maintenance expense	10,008	10,334	7,602
Income tax benefit	(3,903)	(4,030)	(2,965)
After-tax stock-based compensation expense	$ 6,105	$ 6,304	$ 4,637

There were no significant stock-based compensation costs capitalized during the years ended December 31, 2011, 2010 and 2009.

The cost of services received from employees in exchange for the issuance of stock options and restricted stock awards is measured based on the grant date fair value of the awards issued. The value of stock options and restricted stock unit awards at the date of the grant is amortized through expense over the three-year service period. All awards granted in 2011, 2010 and 2009 are classified as equity.

The Company receives a tax deduction based on the intrinsic value of the award at the exercise date for stock options and the distribution date for restricted stock units. For each award, throughout the requisite service period, the Company recognizes the tax benefit related to compensation costs, which have been included in deferred tax assets. The tax deductions in excess of the benefits recorded throughout the requisite service period are recorded to shareholders' equity or the income statement and are included in the financing section of the statement of cash flows.

The Company stratified its grant populations and used historic employee turnover rates to estimate employee forfeitures. The estimated rate is compared to the actual forfeitures at the end of the period and adjusted as necessary.

Stock Options

In the first quarters of 2011, 2010 and 2009, the Company granted non-qualified stock options to certain employees under the Plan. The stock options vest ratably over the three-year service period beginning on January 1 of the year of grant. These awards have no performance vesting conditions and the grant date fair value is amortized through expense over the requisite service period using the straight-line method.

On August 15, 2010, the Company's board of directors elected a new President and Chief Executive Officer ("CEO") of the Company. In connection with his election to these offices, the Company's new CEO was granted non-qualified stock options that cliff vest two years from the date of grant. Additionally, the CEO was granted non-qualified stock options that vest ratably over a three-year period beginning January 1, 2010. These awards have no performance vesting conditions.

Also on August 15, 2010, the Company's former President and Chief Executive Officer resigned as an officer and director of the Company. Pursuant to his resignation, the Company cancelled options to purchase 33 shares of Company stock, accelerated the vesting of 247 options, extended the termination dates of vested options and recognized $315 additional expense related to the modifications that is recorded in operation and maintenance expense in the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss) for the year ended December 31, 2010.

The following table presents the weighted average assumptions used in the pricing model for grants and the resulting weighted average grant date fair value of stock options granted in the years ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Dividend yield	3.25%	3.83%	3.86%
Expected volatility	29.32%	31.77%	31.67%
Risk-free interest rate	1.93%	2.14%	1.79%
Expected life (years)	4.35	4.29	4.36
Exercise price	$ 27.08	$ 22.01	$ 20.70
Grant date fair value per share	$ 5.14	$ 4.33	$ 3.96

The Company utilized the "simplified method" to determine the expected stock option life due to insufficient historical experience to estimate the exercise patterns of the stock options granted. The Company began granting stock options at the time of the IPO in April 2008. Expected volatility is based on a weighted average of historic volatilities of traded common stock of peer companies (regulated water companies) over the expected term of the stock options and historic volatilities of the Company's common stock during the period it has been publicly traded. The dividend yield is based on the Company's expected dividend payments and the stock price on the date of grant. The risk-free interest rate is the market yield on U.S. Treasury strips with maturities similar to the expected term of the stock options. The exercise price of the stock options is equal to the fair market value of the underlying stock on the date of option grant. Stock options granted vest over periods ranging from one to three years and expire seven years from the effective date of the grant. The fair value of each option is estimated on the date of grant using the Black-Scholes option-pricing model.

The value of stock options at the date of the grant is amortized through expense over the requisite service period using the straight-line method. As of December 31, 2011, $3,389 of total unrecognized compensation costs related to the nonvested stock options is expected to be recognized over the remaining weighted-average period of 1.6 years. The total grant date fair value of stock options vested during the years ended December 31, 2011, 2010 and 2009 was $4,578, $4,505 and $92, respectively.

The table below summarizes stock option activity for the year ended December 31, 2011:

	Shares	Weighted Average Exercise Price (per share)	Weighted Average Remaining Life (years)	Aggregate Intrinsic Value
Options outstanding at January 1, 2011	2,870	$ 21.38		
Granted	736	27.08		
Forfeited or expired	(71)	23.27		
Exercised	(423)	21.27		
Options outstanding at December 31, 2011	3,112	$ 22.70	4.3	$ 28,493
Exercisable at December 31, 2011	1,686	$ 21.34	3.5	$ 17,738

The following table summarizes additional information regarding stock options exercised during the years ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Intrinsic value	$ 3,026	$ 333	$ 0
Exercise proceeds	8,991	3,010	0
Income tax benefit (shortfall)	511	(89)	0

Restricted Stock Units

In the first quarters of 2011 and 2010 and August 2010, the Company granted restricted stock units to certain employees under the Plan. The restricted stock units vest ratably over the three-year performance period beginning January 1 of the year of grant (the "Performance Period"); however, distribution of the shares is contingent upon the achievement of internal performance measures and, separately, certain market thresholds over the Performance Period. In February 2009, the Company granted restricted stock units that vest ratably over the three year performance period beginning January 1, 2009 (the "2009 Performance Period"); however, distribution of the shares is contingent upon the achievement of certain market thresholds over the 2009 Performance Period.

During 2011, 2010 and 2009, the Company granted restricted stock units to certain non-employee directors under the Plan. The restricted stock units vested on the date of grant; however, distribution of the shares will be made within 30 days of the earlier of (a) 15 months after grant date or (b) the participant's separation from service. Because these restricted stock units vested on grant date, the total grant date fair value was recorded in operation and maintenance expense included in the expense table above on the grant date.

In August 2010, the Company accelerated the vesting of 12 restricted stock units granted in 2008 to the Company's former CEO. Additionally the Company cancelled 9 restricted stock units granted in 2009 and 2010; the remaining outstanding awards will be subject to the Company's achievement of internal performance measures and certain market thresholds over the applicable three-year performance periods as if he had remained in the employ of the Company during the entire performance periods. The net impact associated with these modifications was a reduction to operation and maintenance expense of $12 for the year ended December 31, 2010.

Restricted stock units generally vest over periods ranging from one to three years. Restricted stock units granted without market conditions are valued at the market value of the Company's common stock on the date of grant. Restricted stock units granted with market conditions are valued using a Monte Carlo model. Expected volatility is based on historical volatilities of traded common stock of the Company and comparative companies using daily stock prices over the past three years. The Company's volatility was calculated using a weighted average of eight companies for the 2011 and 2010 periods and nine companies for 2009, respectively, before the Company's stock was publicly traded. The expected term is three years and the risk-free interest rate is based on the three-year U.S. Treasury rate in effect as of the measurement date. The following table presents the weighted average assumptions used in the Monte Carlo simulation and the weighted average grant date fair values of restricted stock units granted during the years ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Expected volatility	29.50%	30.74%	32.00%
Risk-free interest rate	1.24%	1.50%	1.30%
Expected life (years)	3	3	3
Grant date fair value per share	$ 29.95	$ 23.23	$ 21.75

The value of restricted stock awards at the date of the grant is amortized through expense over the requisite service period using the straight-line method for restricted stock units with service and/or performance vesting. The grant date fair value of restricted stock awards that have (a) market and/or performance and service conditions and (b) vest ratably is amortized through expense over the requisite service period using the graded-vesting method. As of December 31, 2011, $3,172 of total unrecognized compensation cost related to the nonvested restricted stock units is expected to be recognized over the weighted-average remaining life of 1.3 years. The total grant date fair value of restricted stock units vested during the years ended December 31, 2011, 2010 and 2009 was $2,040, $2,204 and $438, respectively.

The table below summarizes restricted stock unit activity for the year ended December 31, 2011:

	Shares	Weighted Average Grant Date Fair Value (per share)
Nonvested total at January 1, 2011	479	$ 22.60
Granted	205	29.95
Vested	(89)	22.88
Forfeited	(18)	25.28
Nonvested total at December 31, 2011	577	$ 25.09

The following table summarizes additional information regarding restricted stock units distributed during the years ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Intrinsic value	$ 2,068	$ 1,241	$ 51
Income tax benefit (shortfall)	99	15	(2)

If dividends are declared with respect to shares of the Company's common stock before the restricted stock units are distributed, the Company credits a liability for the value of the dividends that would have been paid if the restricted stock units were shares of Company common stock. When the restricted stock units are distributed, the Company pays the employee a lump sum cash payment equal to the value of the dividend equivalents accrued. The Company accrued dividend equivalents totaling $921, $474 and $279 to retained earnings during the years ended December 31, 2011, 2010 and 2009, respectively.

Employee Stock Purchase Plan

The Company's Nonqualified Employee Stock Purchase Plan ("ESPP") was effective as of July 1, 2008. Under the ESPP, employees can use payroll deductions to acquire Company stock at the lesser of 90% of the fair market value of (a) the beginning or (b) the end of each three-month purchase period. As of December 31, 2011 there were 1,592 shares of common stock reserved for issuance under the ESPP. The Company's ESPP is considered compensatory. Compensation costs of $486, $355 and $388 were recognized for the years ended December 31, 2011, 2010 and 2009, respectively. During the years ended December 31, 2011, 2010 and 2009, the Company issued 121, 119 and 129 shares, respectively, under the ESPP.

Note 10: Preferred Stock Without Mandatory Redemption Requirements

Certain preferred stock agreements do not require annual sinking fund payments or redemption except at the option of the subsidiaries and are as follows:

	Balance at December 31,	
Dividend Yield	2011	2010
4.50%	$ 1,720	$ 1,720
5.00%	1,952	1,952
5.50%	486	486
5.75%	389	389
	$ 4,547	$ 4,547

Table of Contents

The Company reflects its subsidiaries' preferred stock without mandatory redemption requirements, which represents the Company's noncontrolling interest, in the total stockholders' equity section of the accompanying Consolidated Balance Sheets. The dividends on these preferred shares have not been reflected as income attributable to noncontrolling interest in the Consolidated Statements of Operations and Comprehensive Income (Loss) as the total amount of these dividends is not considered material. The dividends issued were $224 for 2011 and 2010, respectively, and $225 for 2009. The amounts have been included as a component of other income (expenses) in the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss).

Note 11: Long-Term Debt

The Company primarily incurs long-term debt to fund capital expenditures of the regulated subsidiaries. The components of long-term at December 31 are:

	Rate	Weighted Average Rate	Maturity Date	2011	2010
Long-term debt of American Water Capital Corp. ("AWCC")(a)					
Private activity bonds and government funded debt					
Fixed rate	4.85%-6.75%	5.72%	2018-2040	$ 322,610	$ 322,610
Senior notes					
Fixed rate	5.39%-10.00%	6.25%	2013-2040	3,089,409	3,117,696
Long-term debt of other subsidiaries					
Private activity bonds and government funded debt					
Fixed rate	0.00%-6.20%	5.07%	2012-2039	1,206,332	1,201,723
Mortgage bonds					
Fixed rate	5.48%-9.71%	7.40%	2012-2039	697,800	730,991
Mandatory redeemable preferred stock	4.60%-9.75%	8.43%	2013-2036	22,101	22,844
Notes payable and other(b)	9.49%-13.96%	12.12%	2013-2026	1,691	5,689
Long-term debt				5,339,943	5,401,553
Unamortized debt discount, net(c)				43,888	51,154
Fair value adjustment to interest rate hedge				6,111	(345)
Total long-term debt				$ 5,389,942	$ 5,452,362

(a) AWCC, which is a wholly-owned subsidiary of the Company, has a strong support agreement with its parent that, under certain circumstances, is the functional equivalent of a guarantee.
(b) Includes capital lease obligations of $1,264 and $5,076 at December 31, 2011 and 2010, respectively.
(c) Includes fair value adjustments previously recognized in acquisition purchase accounting.

All $697,800 of the subsidiaries' mortgage bonds and $1,150,003 of the $1,206,332 total subsidiaries' private activity bonds and government funded debt are collateralized by utility plant.

Long-term debt indentures contain a number of covenants that, among other things, limit, subject to certain exceptions, the Company from issuing debt secured by the Company's assets. Certain long term notes require the Company to maintain a ratio of consolidated total indebtedness to consolidated total capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2011 was 0.58 to 1.00. In addition, the Company has $1,701,322 of notes which include the right to redeem the notes in whole or in part from time to time subject to certain restrictions.

The future sinking fund payments and maturities are as follows:

Year	Amount
2012	$ 28,855
2013	112,594
2014	9,416
2015	49,568
2016	47,172
Thereafter	5,092,338

The following long-term debt was issued in 2011:

Company	Type	Interest Rate	Maturity	Amount
Other subsidiaries	Private activity bonds and government funded debt—fixed rate	0.00%-1.56%	2031	$ 12,510
Total issuances				$ 12,510

The following long-term debt was retired through optional redemption or payment at maturity during 2011:

Company	Type	Interest Rate	Maturity	Amount
American Water Capital Corp.	Senior notes—fixed rate	6.00%-8.25%	2011-2039	$ 28,287
Other subsidiaries	Private activity bonds and government funded debt—fixed rate	0.00%-5.90%	2011-2034	7,976
Other subsidiaries	Mortgage bonds—fixed rate	8.21%-9.71%	2011-2022	33,191
Other subsidiaries	Mandatory redeemable preferred stock	4.60%-9.18%	2013-2019	1,888
Other	Capital leases and other			4,078
Total retirements and redemptions				$ 75,420

Included in the capital lease redemptions above is a non-cash redemption of $3,487 associated with a cancelled sublease and a capital lease arrangement.

Interest, net includes interest income of approximately $10,942, $10,320 and $10,397 in 2011, 2010 and 2009, respectively.

One of the principal market risks to which the Company is exposed is changes in interest rates. In order to manage the exposure, the Company follows risk management policies and procedures, including the use of derivative contracts such as swaps. The Company uses a combination of fixed-rate and variable-rate debt to manage interest rate exposure. The Company does not enter into derivative contracts for speculative purposes and does not use leveraged instruments. The derivative contracts entered into are for periods consistent with the related underlying exposures. The Company is exposed to the risk that counterparties to derivative contracts will fail to meet their contractual obligations. The Company minimizes the counterparty credit risk on these transactions by dealing only with leading, credit-worthy financial institutions having long-term credit ratings of "A" or better.

On July 12, 2010, the Company entered into an interest rate swap to hedge $100,000 of its 6.085% fixed-rate debt maturing 2017. The Company will pay variable interest of six-month LIBOR plus 3.422%. The swap is

accounted for as a fair-value hedge, and matures with the fixed-rate debt in 2017. The Company uses a combination of fixed-rate and variable-rate debt to manage interest rate exposure.

At December 31, 2011 and 2010, the Company had a $100,000 notional amount variable interest rate swap fair-value hedge outstanding, respectively. The following table provides a summary of the derivative fair value balance recorded by the Company as of December 31, 2011 and 2010 and the line item in the Consolidated Balance Sheet in which such amount is recorded:

Balance sheet classification	December 31, 2011	December 31, 2010
Regulatory and other long-term assets		
Other	$ 5,824	$ 0
Regulatory and other long-term liabilities		
Other	0	898
Long-term debt		
Long-term debt	6,111	(345)

For derivative instruments that are designated and qualify as fair-value hedges, the gain or loss on the hedge instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current net income (loss). The Company includes the gain or loss on the derivative instrument and the offsetting loss or gain on the hedged item in interest expense as follows:

Income Statement Classification	December 31, 2011	December 31, 2010
Interest, net		
Gain (loss) on swap	$ 6,722	$ (898)
(Loss) gain on borrowing	(6,455)	345
Hedge ineffectiveness	267	(553)

Note 12: Short-Term Debt

The components of short-term debt at December 31 are as follows:

	2011	2010
Revolving credit lines	$ 0	$ 2,734
Commercial paper, net of $52 and $10 discount at 2011 and 2010, respectively	481,048	175,290
Book overdraft	34,002	50,881
Total short-term debt	$ 515,050	$ 228,905

AWCC had the following available capacity under its commercial paper program at December 31:

	2011	2010
Commercial paper program	$ 700,000	$ 700,000
Commercial paper program available capacity	218,900	524,700

AWCC has entered into an $840,000 senior unsecured credit facility syndicated among a group of 10 banks with JPMorgan Chase Bank, N.A. acting as administrative agent.

This revolving credit facility is principally used to support the commercial paper program at AWCC and to provide up to $150,000 in letters of credit. On September 15, 2008, a majority of the banks agreed to further extend $685,000 of commitments under this revolving credit facility to September 15, 2013. On December 18, 2008, The Bank of New York Mellon joined the credit facility syndicate with a commitment amount of $40,000 through September 15, 2012. If any lender defaults in its obligation to fund advances, the Company may request the other lenders to assume the default lender's commitment or replace such defaulting lender by designating an assignee willing to assume the commitment, however the remaining lenders have no obligation to assume a defaulting lender's commitment and we can provide no assurances that we will replace a defaulting lender.

At December 31, AWCC had the following sub-limits and available capacity under the credit facility.

	2011	2010
Letter of credit sublimit	$ 150,000	$ 150,000
Letter of credit available capacity	113,548	113,203

At December 31, 2011, the Company had $36,830 of outstanding letters of credit, $36,452 of which was issued under the revolving credit facility noted above.

The following table presents the short-term borrowing activity for AWCC for the years ended December 31, 2011 and 2010:

	2011	2010
Average borrowings	$ 362,615	$ 164,782
Maximum borrowings outstanding	494,900	263,500
Weighted average interest rates, computed on a daily basis	0.41%	0.42%
Weighted average interest rates, at December 31	0.56%	0.46%

Interest rates on advances under the credit facility are based on either prime or the London Interbank Offering Rate ("LIBOR") plus an applicable margin based upon credit ratings of the Company, as well as total outstanding amounts under the agreement at the time of the borrowing. The maximum LIBOR margin is 55 basis points.

The credit facility requires the Company to maintain a ratio of consolidated debt to consolidated capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2011 was 0.58 to 1.00.

None of the Company's borrowings are subject to default or prepayment as a result of a downgrading of securities, although such a downgrading could increase fees and interest charges under the Company's credit facilities.

As part of the normal course of business, the Company routinely enters contracts for the purchase and sale of water, energy, fuels and other services. These contracts either contain express provisions or otherwise permit the Company and its counterparties to demand adequate assurance of future performance when there are reasonable grounds for doing so. In accordance with the contracts and applicable contract law, if the Company is downgraded by a credit rating agency, especially if such downgrade is to a level below investment grade, it is possible that a counterparty would attempt to rely on such a downgrade as a basis for making a demand for adequate assurance of future performance. Depending on the Company's net position with a counterparty, the demand could be for the posting of collateral. In the absence of expressly agreed provisions that specify the collateral that must be provided, the obligation to supply the collateral requested will be a function of the facts and circumstances of the Company's situation at the time of the demand. If the Company can reasonably claim that it is willing and financially able to perform its obligations, it may be possible to successfully argue that no collateral should be posted or that only an amount equal to two or three months of future payments should be sufficient. The Company does not expect to post any collateral which will have a material adverse impact on the Company's results of operations, financial position or cash flows.

AWCC had entered into a one year $10,000 committed revolving line of credit with PNC Bank, N.A. Outstanding borrowings against this line totaled $0 and $2,734 at December 31, 2011 and 2010, respectively. This line of credit was terminated without renewal on December 31, 2011.

Note 13: General Taxes

Components of general tax expense from continuing operations for the years ended December 31 are as follows:

	2011	2010	2009
Gross receipts and franchise	$ 90,674	$ 86,063	$ 79,410
Property and capital stock	77,330	78,184	70,907
Payroll	31,705	31,089	27,834
Other general	10,769	10,261	8,469
	$ 210,478	$ 205,597	$ 186,620

Note 14: Income Taxes

Components of income tax expense from continuing operations for the years ended December 31 are as follows:

	2011	2010	2009
State income taxes			
Current	$ (7,440)	$ 24,653	$ (19,582)
Deferred			
Current	(171)	78	(1,661)
Non-current	44,576	11,024	38,908
	36,965	35,755	17,665
Federal income taxes			
Current	12,239	(1,500)	555
Deferred			
Current	(314)	69	(16,189)
Non-current	151,403	141,589	113,174
Amortization of deferred investment tax credits	(1,542)	(1,561)	(1,413)
	161,786	138,597	96,127
	$ 198,751	$ 174,352	$ 113,792

A reconciliation of income tax expense from continuing operations at the statutory federal income tax rate to actual income tax expense for the years ended December 31 is as follows:

	2011	2010	2009
Income tax at statutory rate	$ 176,288	$ 150,298	$ (37,172)
Increases (decreases) resulting from:			
State taxes, net of federal taxes	24,027	23,241	11,482
Change in valuation allowance	(160)	(533)	(6,578)
Flow through differences	2,895	2,807	2,760
Amortization of deferred investment tax credits	(1,542)	(1,561)	(1,413)
Subsidiary preferred dividends	668	675	680
Impairment charges	0	0	143,321
Other, net	(3,425)	(575)	712
Actual income tax expense	$ 198,751	$ 174,352	$ 113,792

The following table provides the components of the net deferred tax liability from continuing operations at December 31:

	2011	2010
Deferred tax assets:		
Advances and contributions	$ 475,280	$ 463,694
Deferred investment tax credits	11,202	11,789
Other postretirement benefits	101,258	92,620
Tax losses and credits	284,636	327,128
Pension benefits	132,972	141,530
Unamortized debt discount, net	23,872	22,889
Other	13,308	8,429
	1,042,528	1,068,079
Valuation allowance	(20,701)	(22,733)
	1,021,827	1,045,346
Deferred tax liabilities:		
Utility plant, principally due to depreciation differences	1,958,044	1,846,338
Income taxes recoverable through rates	94,331	93,495
Deferred security costs	1,982	3,065
Deferred business services project expenses	4,573	4,566
Deferred other postretirement benefits	58,238	48,155
Deferred pension benefits	97,899	78,972
Other	95,557	81,005
	2,310,624	2,155,596
	$ (1,288,797)	$ (1,110,250)

At December 31, 2011 and 2010, the Company recorded federal net operating loss ("NOL") carryforwards of $1,187,427 and $1,185,337, respectively. The Company believes the federal NOL carryforwards are more likely than not to be recovered and require no valuation allowance. The Company evaluated its ability to fully utilize the existing federal NOL carryforwards in light of the RWE divestiture in November 2009. Under Internal Revenue Code ("I.R.C.") Section 382, an ownership change occurs if there is a greater than fifty percent (50%) change in equity ownership of a company over a three-year period determined by reference to the ownership of persons holding five percent (5%) or more of that company's equity securities. If a company undergoes an ownership change as defined by I.R.C. Section 382, the company's ability to utilize its pre-change NOL carryforwards to offset post-change income may be limited.

The Company believes that the limitation imposed by I.R.C. Section 382 generally should not preclude use of its federal NOL carryforwards, assuming the Company has sufficient taxable income in future carryforward periods to utilize those NOL carryforwards. The Company's federal NOL carryforwards do not begin expiring until 2024.

At December 31, 2011 and 2010, the Company had state NOLs of $739,804 and $714,674, respectively, a portion of which are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The state NOL carryforwards will expire between 2012 and 2031.

At December 31, 2011 and 2010, the Company had Canadian NOL carryforwards of $6,198 and $5,398, respectively. The majority of these carryforwards are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The Canadian NOL carryforwards will expire between 2014 and 2030.

At December 31, 2011 and 2010, the Company had capital loss carryforwards for federal income tax purposes of $4,357 and $0, respectively. The Company has recognized a full valuation allowance for the capital loss carryforwards because the Company does not believe these losses are more likely than not to be recovered.

The Company files income tax returns in the United States federal jurisdiction and various state and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state or local or non-U.S income tax examinations by tax authorities for years before 2005.

In March 2010, the Company filed refund claims of $25,314. The refund claims are attributable to the carry back of Alternative Minimum Tax NOLs generated in 2008. These claims procedurally require approval by the Joint Committee of Taxation ("JCT"). The Company received the refund in April 2010. In August 2010, the IRS notified the Company that additional audit procedures were necessary to support the filing of the JCT report. The audit has not been concluded at December 31, 2011, and no adjustments have been proposed so far.

The Company has state income tax examinations in progress and does not expect material adjustments to result.

The Patient Protection and Affordable Care Act (the "PPACA") became law on March 23, 2010, and the Health Care and Education Reconciliation Act of 2010 became law on March 30, 2010, which makes various amendments to certain aspects of the PPACA (together, the "Acts"). The PPACA effectively changes the tax treatment of federal subsidies paid to sponsors of retiree health benefit plans that provide a benefit that is at least actuarially equivalent to the benefits under Medicare Part D. As a result of the Acts, these subsidy payments will effectively become taxable in tax years beginning after December 31, 2012.

Although this change does not take effect immediately, companies are required to recognize the full accounting impact in their financial statements in the period in which the legislation was enacted. As a result, the Company followed its original accounting for the underfunded status of the other postretirement benefits for the Medicare Part D adjustment and recorded a reduction in deferred tax assets and an increase in its regulatory assets amounting to $16,979.

The following table summarizes the changes in the Company's gross liability, excluding interest and penalties, for unrecognized tax benefits:

Balance at January 1, 2010	$	112,021
Increases in current period tax positions		7,434
Decreases due to lapse of statute of limitations		(1,141)
Balance at December 31, 2010		118,314
Increases in current period tax positions		46,961
Decreases in prior period measurement of tax positions		(6,697)
Balance at December 31, 2011	$	158,578

The liability balance as of December 31, 2011 and 2010 does not include interest and penalties of $214 and $80, respectively, which is recorded as a component of income tax expense. The majority of the increased tax position is attributable to temporary differences. The increase in 2011 current period tax positions relates primarily to the Company's change in tax accounting method filed in 2008 for repair and maintenance costs on its utility assets. The Company does not anticipate material changes to its unrecognized tax benefits within the next year. If the Company sustains all of its positions at December 31, 2011 and 2010, an unrecognized tax benefit of $6,644 and $6,644, respectively, excluding interest and penalties, would impact the Company's effective tax rate.

The following table summarizes the changes in the Company's valuation allowance:

Balance at January 1, 2009	$	28,862
Increases in current period tax positions		2,778
Decreases in current period tax positions		(5,698)
Decreases in prior period tax positions		(321)
Balance at December 31, 2009	$	25,621
Increases in current period tax positions		907
Decreases in current period tax positions		(2,740)
Balance at December 31, 2010	$	23,788
Increases in current period tax positions		1,525
Decreases in current period tax positions		(3,734)
Balance at December 31, 2011	$	21,579

Note 15: Employee Benefits

Pension and Other Postretirement Benefits

The Company maintains noncontributory defined benefit pension plans covering eligible non-union employees of its regulated utility and shared services operations. Benefits under the plans are based on the employee's years of service and compensation. The pension plans have been closed for most employees hired on or after January 1, 2006. Union employees hired on or after January 1, 2001 had their accrued benefit frozen and will be able to receive this benefit as a lump sum upon termination or retirement. Union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006 are provided with a 5.25% of base pay defined contribution plan.

The Company's funding policy is to contribute at least the minimum amount required by the Employee Retirement Income Security Act of 1974 and also an additional contribution if needed to avoid "at risk" status and benefit restrictions under the Pension Protection Act of 2006. The Company may also increase its contributions, if appropriate, to its tax and cash position and the plan's funded position. Pension plan assets are invested in a number of investments including equity and bond mutual funds, fixed income securities and guaranteed interest contracts with insurance companies.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain regulated subsidiaries pending future recovery in rates charged for utility services as contributions are made to the plans. (See Note 7)

The Company also has several unfunded noncontributory supplemental non-qualified pension plans that provide additional retirement benefits to certain employees.

The Company maintains postretirement benefit plans providing varying levels of medical and life insurance to eligible retirees. The retiree welfare plans are closed for union employees hired on or after January 1, 2006. The plans had previously closed for non-union employees hired on or after January 1, 2002.

The Company's policy is to fund postretirement benefit costs for rate-making purposes. Plan assets are invested in equity and bond mutual funds.

The obligations of the plans are dominated by obligations for active employees. Because the timing of expected benefit payments is so far in the future and the size of the plan assets are small relative to the Company's assets, the investment strategy is to allocate a large portion of assets to equities, which the Company believes will provide the highest return over the long-term period. The fixed income assets are invested in long duration debt securities in order to better match the duration of the plan liability.

The Company periodically conducts an asset liability modeling study to ensure the investment strategy is aligned with the profile of the obligations. The long-term goals are to maximize the plan funded status and minimize contributions and pension expense, while taking into account the potential volatility risks on each of these items.

None of the Company's securities are included in pension or other postretirement benefit plan assets.

The investment policy guidelines of the pension plan require that the fixed income portfolio has an overall weighted average credit rating of AA or better by Standard & Poor's and the minimum credit quality for fixed income securities must be BBB- or better. Up to 20% of the portfolio may be invested in collateralized mortgage obligations backed by the United States Government.

The fair values and asset allocations of pension plan assets at December 31, 2011, by asset category, follow:

Asset Category	Target Allocation 2012	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2011
Cash	—	$ 9,794	$ 9,794	—	—	—
Equity securities:						
U.S. large cap	36%	364,025	364,025	—	—	37%
U.S. small cap value	12%	119,996	116,748	$ 3,248	—	12%
International	22%	202,917	26	100,745	$ 102,146	21%
Fixed income securities:	30%					30%
U.S. Treasury and government bonds	—	61,278	61,278	—	—	—
Corporate bonds	—	48,564	2,487	46,077	—	—
Mortgage-backed securities	—	118,837	—	118,837	—	—
Guaranteed annuity contracts	—	55,657	—	9,229	46,428	—
Total	100%	$ 981,068	$ 554,358	$ 278,136	$ 148,574	100%

The following table presents a reconciliation of the beginning and ending balances of the fair value measurements using significant unobservable inputs (Level 3):

	Level 3
Balance, January 1, 2011	$ 141,403
Actual return on assets	(3,425)
Transfers in(out)	10,596
Balance, December 31, 2011	$ 148,574

Table of Contents

The fair values and asset allocations of pension plan assets at December 31, 2010, by asset category, follow:

Asset Category	Target Allocation 2011	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2010
Cash	—	$ 6,467	$ 6,467	—	—	—
Equity securities:						
U.S. large cap	36%	299,548	299,548	—	—	35%
U.S. small cap value	12%	113,356	113,356	—	—	13%
International	22%	190,330	682	$ 94,363	$ 95,285	22%
Fixed income securities:	30%					30%
U.S. Treasury and government bonds	—	63,469	63,469	—	—	—
Corporate Bonds	—	33,118	—	33,118	—	—
Mortgage-backed securities	—	99,478	—	99,478	—	—
Guaranteed annuity contracts	—	55,207	—	9,089	46,118	—
Total	100%	$ 860,973	$ 483,522	$ 236,048	$ 141,403	100%

The following table presents a reconciliation of the beginning and ending balances of the fair value measurements using significant unobservable inputs (Level 3):

	Level 3
Balance, January 1, 2010	$ 124,938
Actual return on assets	20,381
Transfers in (out)	(3,916)
Balance, December 31, 2010	$ 141,403

The Company's other postretirement benefit plans are partially funded and plan assets are invested in a manner consistent with the pension plan investment policy.

The fair values and asset allocations of postretirement benefit plan assets at December 31, 2011, by asset category, follow:

Asset Category	Target Allocation 2012	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2011
Cash	—	$ 10,196	$ 10,196	—	—	—
Equity securities:						
U.S. large cap	36%	136,625	136,625	—	—	36%
U.S. small cap value	12%	52,092	50,720	$ 1,372	—	14%
International	22%	78,294	45,537	32,757	—	20%
Fixed income securities:	30%					30%
U.S. Treasury securities	—	12,897	12,897	—	—	—
Corporate bonds	—	46,953	—	46,953	—	—
Mortgage-backed securities	—	45,613	—	45,613	—	—
Total	100%	$ 382,670	$ 255,975	$ 126,695	—	100%

The fair values and asset allocations of postretirement benefit plan assets at December 31, 2010, by asset category, follow:

Asset Category	Target Allocation 2011	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2010
Cash	—	$ 12,500	$ 12,500	—	—	—
Equity securities:						
U.S. large cap	36%	131,775	131,775	—	—	35%
U.S. small cap value	12%	53,898	53,898	—	—	14%
International	22%	77,935	77,935	—	—	21%
Fixed income securities:	30%					30%
U.S. Treasury securities	—	16,025	16,025	—	—	—
Corporate Bonds	—	34,746	—	$ 34,746	—	—
Mortgage-backed securities	—	47,524	—	47,524	—	—
Total	100%	$ 374,403	$ 292,133	$ 82,270	—	100%

Valuation Techniques Used to Determine Fair Value

Cash—Cash and investments with maturities of three months or less when purchased, including certain short-term fixed-income securities, are considered cash and are included in the recurring fair value measurements hierarchy as Level 1.

Equity securities—With respect to equity securities, the trustees obtain prices from pricing services, whose prices are obtained from direct feeds from market exchanges, which the Company is able to independently corroborate. Equity securities are valued based on quoted prices in active markets and categorized as Level 1.

Fixed-income securities—U.S. Treasury securities and government bonds have been categorized in Level 1 because they trade in highly-liquid and transparent markets that the Company can corroborate. The fair values of corporate bonds, mortgage backed securities and a certain guaranteed annuity contract are based on evaluated prices that reflect observable market information, such as actual trade information of similar securities and have

been categorized as Level 2 because the valuations are calculated using models which utilize actively traded market data that the Company can corroborate. Certain other guaranteed annuity contracts are invested in a commingled fund and categorized as Level 3 because the investments are not publicly quoted. The fund administrator values the fund using the net asset value per fund share, derived from the quoted prices in active markets of the underlying securities. Since these valuation inputs are not highly observable, the commingled funds have been categorized as Level 3.

In 2011, after a review of the underlying pension investments, the Company began classifying certain international equity securities as Level 2 and Level 3 and reclassified the prior years' presentations to conform to the 2011 presentation.

The following table provides a rollforward of the changes in the benefit obligation and plan assets for the most recent two years for all plans combined:

	Pension Benefits		Other Benefits	
	2011	2010	2011	2010
Change in benefit obligation				
Benefit obligation at January 1	$ 1,285,456	$ 1,128,162	$ 590,187	$ 548,139
Service cost	33,641	30,675	13,938	14,663
Interest cost	69,047	67,602	31,219	32,149
Plan participants' contributions	—	—	2,241	2,307
Amendments	0	3,762	0	(8,195)
Actuarial (gain) loss	55,743	93,399	4,826	23,764
Gross benefits paid	(41,933)	(38,144)	(23,824)	(23,989)
Federal subsidy	—	—	1,779	1,349
Benefit obligation at December 31	$ 1,401,954	$ 1,285,456	$ 620,366	$ 590,187
Change in Plan Assets				
Fair value of plan assets at January 1	$ 860,973	$ 695,520	$ 374,403	$ 312,042
Actual return on plan assets	2,529	105,078	2,619	45,305
Employer contributions	159,499	98,519	27,231	38,738
Plan participants' contributions	—	—	2,241	2,307
Benefits paid	(41,933)	(38,144)	(23,824)	(23,989)
Fair value of plan assets at December 31	$ 981,068	$ 860,973	$ 382,670	$ 374,403
Funded status at December 31	$ (420,886)	$ (424,483)	$ (237,696)	$ (215,784)
Amounts recognized in the balance sheet consist of:				
Current liability	$ (1,909)	$ (2,097)	$ (33)	$ (33)
Noncurrent liability	(418,977)	(422,386)	(237,663)	(215,751)
Net amount recognized	$ (420,886)	$ (424,483)	$ (237,696)	$ (215,784)
Asset (liability) of discontinued operations included in net amount recognized above	$ (6,979)	$ (8,873)	$ (577)	$ (534)

The following table provides the components of the Company's accumulated other comprehensive income and regulatory assets that have not been recognized as components of periodic benefit costs as of December 31:

	Pension Benefits		Other Benefits	
	2011	2010	2011	2010
Net actuarial loss (gain)	$ 409,129	$ 302,357	$ 164,305	$ 140,453
Prior service cost (credit)	5,858	6,580	(16,864)	(18,788)
Net amount recognized	$ 414,987	$ 308,937	$ 147,441	$ 121,665
Regulatory assets	$ 248,663	$ 184,937	$ 147,441	$ 121,665
Accumulated other comprehensive income	166,324	124,000	—	—
	$ 414,987	$ 308,937	$ 147,441	$ 121,665

Table of Contents

At December 31, 2011 and 2010, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with a projected obligation in excess of plan assets were as follows:

	Projected Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2011	2010
Projected benefit obligation	$ 1,402,000	$ 1,285,000
Fair value of plan assets	981,000	861,000

	Accumulated Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2011	2010
Accumulated benefit obligation	$ 1,257,000	$ 1,138,000
Fair value of plan assets	981,000	861,000

The accumulated postretirement benefit obligation exceeds plan assets for all of the Company's other postretirement benefit plans.

In August 2006, the Pension Protection Act ("PPA") was signed into law in the U.S. The PPA replaces the funding requirements for defined benefit pension plans by requiring that defined benefit plans contribute to 100% of the current liability funding target over seven years. Defined benefit plans with a funding status of less than 80% of the current liability are defined as being "at risk" and additional funding requirements and benefit restrictions may apply. The PPA was effective for the 2008 plan year with short-term phase-in provisions for both the funding target and at-risk determination. The Company's qualified defined benefit plan is currently funded above the at-risk threshold, and therefore the Company expects that the plans will not be subject to the "at risk" funding requirements of the PPA. The Company is proactively monitoring the plan's funded status and projected contributions under the new law to appropriately manage the potential impact on cash requirements.

Minimum funding requirements for the qualified defined benefit pension plan are determined by government regulations and not by accounting pronouncements. The Company plans to contribute amounts at least equal to the minimum required contributions in 2012 to the qualified pension plans. The Company plans to contribute its 2012 other postretirement benefit cost for rate-making purposes.

Information about the expected cash flows for the pension and postretirement benefit plans is as follows:

	Pension Benefits	Other Benefits
2012 expected employer contributions		
To plan trusts	$ 126,700	$ 29,983
To plan participants	1,909	33

The Company made 2012 contributions to fund pension benefits and other benefits of $32,931 and $7,496, respectively, through February 2012.

The following table reflects the net benefits expected to be paid from the plan assets or the Company's assets:

	Pension Benefits	Other Benefits	
	Expected Benefit Payments	Expected Benefit Payments	Expected Federal Subsidy Payments
2012	$ 47,139	$ 26,188	$ 1,814
2013	53,268	28,794	1,994
2014	59,412	31,641	2,161
2015	65,742	34,618	2,328
2016	72,373	37,581	2,515
2017—2021	458,798	228,379	15,770

Because the above amounts are net benefits, plan participants' contributions have been excluded from the expected benefits.

Accounting for pensions and other postretirement benefits requires an extensive use of assumptions about the discount rate, expected return on plan assets, the rate of future compensation increases received by the Company's employees, mortality, turnover and medical costs. Each assumption is reviewed annually. The assumptions are selected to represent the average expected experience over time and may differ in any one year from actual experience due to changes in capital markets and the overall economy. These differences will impact the amount of pension and other postretirement benefit expense that the Company recognizes.

The significant assumptions related to the Company's pension and other postretirement benefit plans are as follows:

	Pension Benefits			Other Benefits		
	2011	2010	2009	2011	2010	2009
Weighted-average assumptions used to determine December 31 benefit obligations						
Discount rate	5.02%	5.32%	5.93%	5.05%	5.27%	5.82%
Rate of compensation increase	3.25%	3.50%	4.00%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 7.5% in 2012 to 5% in 2019+	graded from 8% in 2011 to 5% in 2017+	graded from 8.5% in 2010 to 5% in 2017+
Weighted-average assumptions used to determine net periodic cost						
Discount rate	5.32%	5.93%	6.12%	5.27%	5.82%	6.09%
Expected return on plan assets	7.90%	7.90%	7.90%	7.60%	7.60%	7.60%
Rate of compensation increase	3.50%	4.00%	4.00%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 8% in 2011 to 5% in 2017+	graded from 8.5% in 2010 to 5% in 2017+	graded from 8% in 2009 to 5% in 2015+

N/A—Assumption is not applicable.

The discount rate assumption was determined for the pension and postretirement benefit plans independently. At year end 2011, the Company began using an approach that approximates the process of settlement of obligations tailored to the plans' expected cash flows by matching the plans' cash flows to the coupons and expected maturity values of individually selected bonds. The yield curve was developed for a universe containing the majority of U.S.-issued Aa-graded corporate bonds, all of which were non callable (or callable with make-whole provisions). Historically, for each plan, the discount rate was developed as the level equivalent rate that would produce the same present value as that using spot rates aligned with the projected benefit payments.

The expected long-term rate of return on plan assets is based on historical and projected rates of return for current and planned asset classes in the plans' investment portfolios. Assumed projected rates of return for each of the plans' projected asset classes were selected after analyzing historical experience and future expectations of the returns and volatility of the various asset classes. Based on the target asset allocation for each asset class, the overall expected rate of return for the portfolio was developed, adjusted for historical and expected experience of active portfolio management results compared to the benchmark returns and for the effect of expenses paid from plan assets. The Company's pension expense increases as the expected return on assets decreases.

Assumed health care cost trend rates have a significant effect on the amounts reported for the other postretirement benefit plans. The health care cost trend rate is based on historical rates and expected market conditions. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total of service and interest cost components	$ 7,145	$ 5,838
Effect on other postretirement benefit obligation	$ 83,456	$ 69,318

The following table provides the components of net periodic benefit costs for the years ended December 31:

	2011	2010	2009
Components of net periodic pension benefit cost			
Service cost	$ 33,641	$ 30,675	$ 28,426
Interest cost	69,047	67,602	62,919
Expected return on plan assets	(72,109)	(56,751)	(42,224)
Amortization of:			
Prior service cost (credit)	722	322	182
Actuarial (gain) loss	18,551	17,902	23,968
Net periodic pension benefit cost	$ 49,852	$ 59,750	$ 73,271
Other changes in plan assets and benefit obligations recognized in other comprehensive income, net of tax			
Amortization of prior service credit (cost)	$ (175)	$ (79)	$ (46)
Current year actuarial (gain) loss	30,497	11,836	(9,981)
Amortization of actuarial gain (loss)	(4,504)	(4,368)	(5,994)
Total recognized in other comprehensive income	$ 25,818	$ 7,389	$ (16,021)
Total recognized in net periodic benefit cost and comprehensive income	$ 75,670	$ 67,139	$ 57,250
Components of net periodic other postretirement benefit cost			
Service cost	$ 13,938	$ 14,663	$ 13,172
Interest cost	31,219	32,149	29,180
Expected return on plan assets	(28,779)	(24,372)	(18,638)
Amortization of:			
Transition obligation (asset)	0	173	173
Prior service cost (credit)	(1,924)	(1,180)	(1,180)
Actuarial (gain) loss	7,133	8,159	9,155
Net periodic other postretirement benefit cost	$ 21,587	$ 29,592	$ 31,862

The Company's policy is to recognize curtailments when the total expected future service of plan participants is reduced by greater than 10% due to an event that results in terminations and/or retirements.

The estimated amounts that will be amortized from accumulated other comprehensive income and regulatory assets into net periodic benefit cost in 2012 are as follows:

	Pension Benefits	Other Benefits
Actuarial (gain) loss	$ 29,923	$ 9,537
Prior service cost (credit)	722	(1,914)
Total	$ 30,645	$ 7,623

Savings Plans for Employees

The Company maintains 401(k) savings plans that allow employees to save for retirement on a tax-deferred basis. Employees can make contributions that are invested at their direction in one or more funds. The Company makes matching contributions based on a percentage of an employee's contribution, subject to certain limitations. Due to the Company's discontinuing new entrants into the defined benefit pension plan, on January 1, 2006 the Company began providing an additional 5.25% of base pay defined contribution benefit for union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006. The Company expensed contributions to the plans totaling $8,997 for 2011, $8,651 for 2010, and $8,082 for 2009, respectively. All of the Company's contributions are invested in one or more funds at the direction of the employee.

Note 16: Commitments and Contingencies

The Company is also routinely involved in legal actions incident to the normal conduct of its business. At December 31, 2011, the Company has accrued approximately $2,900 as probable costs and it is reasonably possible that additional losses could range up to $9,700 for these matters. For certain matters, the Company is unable to estimate possible losses. The Company believes that damages or settlements, if any, recovered by plaintiffs in such claims or actions will not have a material adverse effect on the Company's results of operations, financial position or cash flows.

The Company enters into agreements for the provision of services to water and wastewater facilities for the United States military, municipalities and other customers. The Company's military services agreements expire between 2051 and 2060 and have remaining performance commitments as measured by estimated remaining contract revenue of $2,037,000 at December 31, 2011. The military contracts are subject to customary termination provisions held by the U.S. Federal Government prior to the agreed upon contract expiration. The Company's Operations and Maintenance agreements with municipalities and other customers expire between 2012 and 2048 and have remaining performance commitments as measured by estimated remaining contract revenue of $1,076,000 at December 31, 2011. Some of the Company's long-term contracts to operate and maintain a municipality's, federal government's or other party's water or wastewater treatment and delivery facilities include responsibility for certain maintenance for some of those facilities, in exchange for an annual fee. Unless specifically required to perform certain maintenance activities, the maintenance costs are recognized when the maintenance is performed.

Commitments have been made in connection with certain construction programs. The estimated capital expenditures required under legal and binding contractual obligations amounted to $171,878 at December 31, 2011.

The Company's regulated subsidiaries maintain agreements with other water purveyors for the purchase of water to supplement their water supply. The Company's subsidiaries purchased water expense under these types of agreements amounted to approximately $104,384, $103,898 and $96,053 during the years ended December 31, 2011, 2010 and 2009, respectively. The estimated annual commitment related to the minimum quantities of water purchased is expected to approximate $48,916 in 2012, $47,576 in 2013, $47,452 in 2014, $47,404 in 2015, $43,439 in 2016 and $448,920 thereafter.

Table of Contents

Note 17: Earnings (Loss) per Common Share

Earnings per share is calculated using the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security. The Company has participating securities related to restricted stock units, granted under the Company's 2007 Omnibus Equity Compensation Plan, that earn dividend equivalents on an equal basis with common shares. In applying the two-class method, undistributed earnings are allocated to both common shares and participating securities. There were 21 participating securities that were not included in the basic net loss per common share calculation at December 31, 2009 because they were anti-dilutive. The following is a reconciliation of the Company's income (loss) from continuing operations, income (loss) from discontinued operations and net income (loss) and weighted average common shares outstanding for calculating basic net earnings (loss) per share:

	Years Ended December 31,		
	2011	2010	2009
Basic			
Income (loss) from continuing operations	$ 304,929	$ 255,072	$ (219,998)
Income (loss) from discontinued operations, net of tax	4,684	12,755	(13,085)
Net income (loss)	309,613	267,827	(233,083)
Less: Distributed earnings to common shareholders	158,708	150,724	137,597
Less: Distributed earnings to participating securities	68	51	0
Undistributed earnings	150,837	117,052	(370,680)
Undistributed earnings allocated to common shareholders	150,772	117,014	(370,680)
Undistributed earnings allocated to participating securities	65	38	0
Total income (loss) from continuing operations available to common shareholders, basic	$ 304,796	$ 254,983	$ (219,998)
Total income (loss) available to common shareholders, basic	$ 309,480	$ 267,738	$ (233,083)
Weighted average common shares outstanding, basic	175,484	174,833	168,164
Basic earnings (loss) per share: (a)			
Income (loss) from continuing operations	$ 1.74	$ 1.46	$ (1.31)
Income (loss) from discontinued operations, net of tax	$ 0.03	$ 0.07	$ (0.08)
Net income (loss)	$ 1.76	$ 1.53	$ (1.39)

(a) Amounts may not sum due to rounding.

Table of Contents

Diluted earnings (loss) per common share is based on the weighted average number of common shares outstanding adjusted for the dilutive effect of common stock equivalents related to the restricted stock units, stock options, and employee stock purchase plan. The dilutive effect of the common stock equivalents is calculated using the treasury stock method and expected proceeds on vesting of the restricted stock units, exercise of the stock options and purchases under the employee stock purchase plan. The following is a reconciliation of the Company's income (loss) from continuing operations, income (loss) from discontinued operations and net income (loss) and weighted average common shares outstanding for calculating diluted earnings (loss) per share:

	Years Ended December 31,		
	2011	2010	2009
Diluted			
Total income (loss) from continuing operations available to common shareholders, basic	$ 304,796	$ 254,983	$ (219,998)
Income (loss) from discontinued operations, net of tax	4,684	12,755	(13,085)
Total income (loss) available to common shareholders, basic	309,480	267,738	(233,083)
Undistributed earnings allocated to participating securities	65	38	0
Total income (loss) from continuing operations available to common shareholders, diluted	$ 304,861	$ 255,021	$ (219,998)
Total income (loss) available to common shareholders, diluted	$ 309,545	$ 267,776	$ (233,083)
Weighted average common shares outstanding, basic	175,484	174,833	168,164
Restricted stock units	556	264	0
Stock options	490	26	0
Employee stock purchase plan	1	1	0
Weighted average common shares outstanding, diluted	176,531	175,124	168,164
Diluted earnings per share: (a)			
Income (loss) from continuing operations	$ 1.73	$ 1.46	$ (1.31)
Income (loss) from discontinued operations, net of tax	$ 0.03	$ 0.07	$ (0.08)
Net income (loss)	$ 1.75	$ 1.53	$ (1.39)

(a) Amounts may not sum due to rounding.

The following potentially dilutive common stock equivalents were not included in the earnings (loss) per share calculations for the years ended December 31 because they were anti-dilutive:

	2011	2010	2009
Stock options	711	1,781	2,265
Stock options where certain performance conditions were not met	0	0	459
Restricted stock units	0	0	258
Restricted stock units where certain performance conditions were not met	22	69	144
Employee stock purchase plan	0	0	32

Note 18: Fair Values of Financial Instruments

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Current assets and current liabilities: The carrying amounts reported in the Consolidated Balance Sheets for current assets and current liabilities, including revolving credit debt, due to the short-term maturities and variable interest rates, approximate their fair values.

Preferred stock with mandatory redemption requirements and long-term debt: The fair values of preferred stock with mandatory redemption requirements and long-term debt are determined by a valuation model which is based on a conventional discounted cash flow methodology and utilizes assumptions of current market rates. As a majority of the Company's debts do not trade in active markets, the Company calculated a base yield curve using a risk-free rate (a U.S. Treasury securities yield curve) plus a credit spread that is based on the following two factors: an average of the Company's own publicly-traded debt securities and the current market rates for U.S. Utility BBB+ debt securities. The Company used these yield curve assumptions to derive a base yield and then adjusted the base yield for specific features of the debt securities of call features, coupon tax treatment and collateral.

The carrying amounts (including fair value adjustments previously recognized in acquisition purchase accounting) and fair values of the financial instruments are as follows:

As of December 31, 2011	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 22,036	$ 26,458
Long-term debt (excluding capital lease obligations)	5,366,642	6,230,547

As of December 31, 2010	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 22,794	$ 25,475
Long-term debt (excluding capital lease obligations)	5,424,492	5,841,448

Fair Value Measurements

To increase consistency and comparability in fair value measurements, FASB guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels as follows:

- Level 1—quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access as of the reporting date. Financial assets and liabilities utilizing Level 1 inputs include active exchange-traded equity securities, exchange-based derivatives, mutual funds and money market funds.
- Level 2—inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data. Financial assets and liabilities utilizing Level 2 inputs include fixed income securities, non-exchange-based derivatives, commingled investment funds not subject to purchase and sale restrictions and fair-value hedges.
- Level 3—unobservable inputs, such as internally-developed pricing models for the asset or liability due to little or no market activity for the asset or liability. Financial assets and liabilities utilizing Level 3 inputs include infrequently-traded non-exchange-based derivatives and commingled investment funds subject to purchase and sale restrictions.

Table of Contents

Recurring Fair Value Measurements

The following table presents assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of December 31, 2011 and 2010, respectively:

	At Fair Value as of December 31, 2011			
Recurring Fair Value Measures	Level 1	Level 2	Level 3	Total
Assets:				
Restricted funds	$ 57,941	—	—	$ 57,941
Rabbi trust investments	—	$ 518	—	518
Deposits	2,287	—	—	2,287
Mark-to-market derivative asset	—	5,824	—	5,824
Total assets	60,228	6,342	—	66,570
Liabilities:				
Deferred compensation obligation	—	9,036	—	9,036
Total liabilities	—	9,036	—	9,036
Total net assets (liabilities)	$ 60,228	$ (2,694)	—	$ 57,534

	At Fair Value as of December 31, 2010			
Recurring Fair Value Measures	Level 1	Level 2	Level 3	Total
Assets:				
Restricted funds	$ 120,784	—	—	$ 120,784
Rabbi trust investments	—	$ 1,552	—	1,552
Deposits	1,381	—	—	1,381
Total assets	122,165	1,552	—	$ 123,717
Liabilities:				
Deferred compensation obligation	—	9,180	—	9,180
Mark-to-market derivative liability	—	898	—	898
Total liabilities	—	10,078	—	10,078
Total net assets (liabilities)	$ 122,165	$ (8,526)	—	$ 113,639

Restricted funds—The Company's restricted funds primarily represent proceeds received from financings for the construction and capital improvement of facilities and from customers for future services under operations and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within twelve months subsequent to year end are classified as current.

Rabbi trust investments—The Company's rabbi trust investments consist primarily of fixed income investments from which supplemental executive retirement plan benefits are paid. The Company includes these assets in other long-term assets.

Deposits—Deposits includes escrow funds and certain other deposits held in trust. The Company includes cash deposits in other current assets.

Deferred compensation obligations—The Company's deferred compensation plans allow participants to defer certain cash compensation into notional investment accounts. The Company includes such plans in other long-term liabilities. The value of the Company's deferred compensation obligations is based on the market value of the participants' notional investment accounts. The notional investments are comprised primarily of mutual funds, which are based on observable market prices.

Mark-to-market derivative asset and liability-The Company utilizes fixed-to-floating interest-rate swaps, typically designated as fair-value hedges, to achieve a targeted level of variable-rate debt as a percentage of total debt. The Company uses a calculation of future cash inflows and estimated future outflows, which are discounted, to determine the current fair value. Additional inputs to the present value calculation include the contract terms, counterparty credit risk, interest rates and market volatility.

See Note 15 for the Company's fair value of qualified pension and postretirement welfare plans' assets.

Non-recurring Fair Value Measurements

As discussed in Note 8, the Company recognized continuing operations goodwill impairment charges of $0, $0, and $428,036 for the years ended December 31, 2011, 2010 and 2009, respectively. The Company's goodwill valuation model includes significant unobservable inputs and falls within Level 3 of the fair value hierarchy.

Note 19: Operating Leases

The Company has entered into operating leases involving certain facilities and equipment. Rental expenses of continuing operations under operating leases were $32,752 for 2011, $36,264 for 2010 and $34,862 for 2009. The operating leases for facilities will expire over the next 20 years and the operating leases for equipment will expire over the next five years. Certain operating leases have renewal options ranging from one to five years.

At December 31, 2011, the minimum annual future rental commitment under operating leases that have initial or remaining non-cancelable lease terms in excess of one year are $21,528 in 2012, $17,987 in 2013, $14,833 in 2014, $10,877 in 2015, $9,172 in 2016 and $101,472 thereafter.

The Company has a series of agreements with various public entities (the "Partners") to establish certain joint ventures, commonly referred to as "public-private partnerships." Under the public-private partnerships, the Company constructed utility plant, financed by the Company, and the Partners constructed utility plant (connected to the Company's property), financed by the Partners. The Company agreed to transfer and convey some of its real and personal property to the Partners in exchange for an equal principal amount of Industrial Development Bonds ("IDBs"), issued by the Partners under a state Industrial Development Bond and Commercial Development Act. The Company leased back the total facilities, including portions funded by both the Company and the Partners, under leases for a period of 40 years.

The leases related to the portion of the facilities funded by the Company have required payments from the Company to the Partners that approximate the payments required by the terms of the IDBs from the Partners to the Company (as the holder of the IDBs). As the ownership of the portion of the facilities constructed by the Company will revert back to the Company at the end of the lease, the Company has recorded these as capital leases. The lease obligation and the receivable for the principal amount of the IDBs are presented by the Company on a net basis. The carrying value of the facilities funded by the Company recognized as a capital lease asset was $159,211 and $159,707 at December 31, 2011 and 2010, respectively, which is presented within utility plant. The future payments under the lease obligations are equal to and offset by the payments receivable under the IDBs.

At December 31, 2011, the minimum annual future rental commitment under the operating leases for the portion of the facilities funded by the Partners that have initial or remaining non-cancelable lease terms in excess of one year included in the preceding minimum annual rental commitments are $3,629 in 2012, $3,668 in 2013, $3,727 in 2014 through 2016, and $82,620 thereafter.

Note 20: Related Party Transactions

One of the Company's Directors was employed by an electrical utility that supplies electricity and electrical services to the Company's subsidiaries in Ohio, Pennsylvania, and New Jersey. The Company purchased, from

various subsidiaries of this electrical utility, approximately $8,558 of such services in 2009. The Director retired from that electrical utility effective March 31, 2010. The Company purchased, from various subsidiaries of this electrical utility, approximately $3,225 of such services in the first quarter of 2010.

Note 21: Segment Information

The Company has two operating segments referred to as the Regulated Businesses and Market-Based Operations segments. The Company's chief operating decision maker regularly reviews the operating results of the Regulated Businesses and Market-Based Operations segments to assess segment performance and allocate resources. The evaluation of segment performance and the allocation of resources are based on several measures. The measure that is most consistent with that used by management is income from continuing operations before income tax.

The Regulated Businesses segment includes the Company's 17 utility subsidiaries in continuing operations that provide water and wastewater services to customers in 16 U.S. states. With the exception of one company, each of these public utility subsidiaries is subject to regulation by public utility commissions and local governments. In addition to providing similar products and services and being subject to the public utility regulatory environment, each of the regulated subsidiaries has similar economic characteristics, production processes, types and classes of customers and water distribution or wastewater collection processes. Each of these companies is also subject to both federal and state regulation regarding the quality of water distributed and the discharge of wastewater residuals.

The Market-Based Operations segment is comprised of market-based businesses that provide a broad range of market-based water and wastewater services and products including homeowner water and sewer line maintenance services, water and wastewater facility operations and maintenance services, granular carbon technologies and products for cleansing water and wastewater, wastewater residuals management services and water and wastewater facility engineering services.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see Note 2). The Regulated Businesses and Market-Based Operations segment information includes intercompany costs that are allocated by American Water Works Service Company, Inc. and intercompany interest that is charged by AWCC, which are eliminated to reconcile to the consolidated results of operations. Inter-segment revenues, which are primarily recorded at cost plus mark-up that approximates current market prices, include carbon regeneration services and leased office space, furniture and equipment provided by the Company's market-based subsidiaries to its regulated subsidiaries. Other includes corporate costs that are not allocated to the Company's subsidiaries, eliminations of inter-segment transactions, fair value adjustments and associated income and deductions related to the Acquisitions that have not been allocated to the segments for evaluation of segment performance and allocation of resource purposes. The adjustments related to the Acquisitions are reported in Other, as they are excluded from segment performance measures evaluated by management. The following table includes the Company's summarized segment information:

	As of or for the Year Ended December 31, 2011			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,368,891	$ 327,815	$ (30,470)	$ 2,666,236
Depreciation and amortization	321,540	6,822	23,459	351,821
Total operating expenses, net	1,609,276	290,854	(37,030)	1,863,100
Income (loss) from continuing operations before income taxes	535,445	39,250	(71,015)	503,680
Total assets	12,843,820	280,862	1,651,709	14,776,391
Assets of discontinued operations (included in total assets above)	904,391	0	25,467	929,858
Capital expenditures	920,210	4,648	0	924,858
Capital expenditures of discontinued operations (included in above)	21,052	86	0	21,138

	As of or for the Year Ended December 31, 2010			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,285,656	$ 294,723	$ (25,344)	$ 2,555,035
Depreciation and amortization	301,087	7,014	22,163	330,264
Total operating expenses, net	1,587,963	269,060	(30,110)	1,826,913
Income (loss) from continuing operations before income taxes	478,629	30,443	(79,648)	429,424
Total assets	12,290,798	240,718	1,554,730	14,086,246
Assets of discontinued operations (included in total assets above)	911,905	6,590	19,210	937,705
Capital expenditures	758,150	7,486	0	765,636
Capital expenditures of discontinued operations (included in above)	26,725	143	0	26,868

	As of or for the Year Ended December 31, 2009			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,076,563	$ 238,180	$ (24,297)	$ 2,290,446
Depreciation and amortization	286,390	5,306	18,178	309,874
Impairment charge	0	0	428,036	428,036
Total operating expenses, net	1,497,453	217,643	391,515	2,106,611
Income (loss) from continuing operations before income taxes	371,919	25,168	(503,293)	(106,206)
Total assets	11,673,685	246,201	1,539,482	13,459,368
Assets of discontinued operations (included in total assets above)	905,938	9,333	17,504	932,775
Capital expenditures	779,428	5,837	0	785,265
Capital expenditures of discontinued operations (included in above)	43,078	111	0	43,189

Note 22: Unaudited Quarterly Data

The following table sets forth certain supplemental unaudited consolidated quarterly financial data for each of the four quarters in the years ended December 31, 2011 and 2010, respectively. The operating results for any quarter are not indicative of results that may be expected for a full year or any future periods.

During the fourth quarter of 2011, the Company discovered errors in the Company's calculation of gain or loss on discontinued operations that originated in the first and second quarters of 2011. As a result, the Company recorded an after-tax charge totaling $24,555 to reduce the net asset values of those businesses, which included associated parent company goodwill, to their net realizable values. This charge was recognized within discontinued operations and net income and included in results for the full year ended December 31, 2011. The write-downs consisted of $21,099 recognized as of March 31, and $3,456 recognized as of June 30 as reflected in the table below. Management does not consider these write-downs to constitute a triggering event for the balance of the Company's goodwill of continuing operations. In addition, the adjustment had no impact on income from continuing operations or to the cash flows from operations or total cash flows.

Based on the materiality guidelines contained in SEC Staff Accounting Bulletin No. 99, "Materiality" and Topic 5.F of the Codification of Staff Accounting Bulletins, "Accounting Changes Not Retroactively Applied Due to Immateriality," the Company concluded that the adjustments to correct the errors were not material to its financial statements for the three months ended March 31, 2011 and June 30, 2011. Because the effect of the adjustments were not material to any previously issued financial statements, the Company determined not to

amend its previously filed Quarterly Reports on Form 10-Q for the quarters ended March 31, 2011 and June 30, 2011; instead, the Company will make corresponding adjustments to prior period financial statements, as appropriate, the next time those financial statements are filed.

2011	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(In thousands, except per share data)			
Operating revenues	$ 596,715	$ 668,873	$ 760,869	$ 639,779
Operating income	143,250	201,395	281,408	177,083
Income from continuing operations	40,699	74,817	128,495	60,918
Net income	26,233	81,110	137,422	64,848
Basic earnings per common share:				
Income from continuing operations	$ 0.23	$ 0.43	$ 0.73	$ 0.35
Net income	$ 0.15	$ 0.46	$ 0.78	$ 0.37
Diluted earnings per common share:				
Income from continuing operations	$ 0.23	$ 0.42	$ 0.73	$ 0.34
Net income	$ 0.15	$ 0.46	$ 0.78	$ 0.37

2010	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(In thousands, except per share data)			
Operating revenues	$ 554,205	$ 630,761	$ 744,296	$ 625,773
Operating income	123,831	188,367	266,480	149,444
Income from continuing operations	29,328	68,071	119,327	38,346
Net income	30,808	72,751	124,114	40,154
Basic earnings per common share:				
Income from continuing operations	$ 0.17	$ 0.39	$ 0.68	$ 0.22
Net income	$ 0.18	$ 0.42	$ 0.71	$ 0.23
Diluted earnings per common share:				
Income from continuing operations	$ 0.17	$ 0.39	$ 0.68	$ 0.22
Net income	$ 0.18	$ 0.42	$ 0.71	$ 0.23

Amounts may not sum due to rounding; per share amounts may not sum due to changes in shares outstanding during the year.

American Water Works Company, Inc.

Audited Consolidated Financial Statement

Excerpted from SEC Form 10-K Annual Report
Filed on 02/28/2011

Filed Period 12/31/2010

AMERICAN WATER

Annual Report Available At : http://ir.amwater.com/phoenix.zhtml?c=215126&p=irol-sec

CONSOLIDATED FINANCIAL STATEMENTS - 2010

Audited Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2010 and 2009

Consolidated Statements of Operations and Comprehensive Income (Loss) for the years ended December 31, 2010, 2009 and 2008

Consolidated Statements of Cash Flows for the years ended December 31, 2010, 2009 and 2008

Consolidated Statements of Changes in Common Stockholders' Equity for the years ended December 31, 2010, 2009, and 2008

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
American Water Works Company, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive income (loss), of cash flows, and of changes in common stockholders' equity, present fairly, in all material respects, the financial position of American Water Works Company, Inc. and Subsidiary Companies at December 31, 2010 and December 31, 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our audits (which were integrated audits in 2010 and 2009). We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 25, 2011

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Balance Sheets

(In thousands, except per share data)

	December 31, 2010	December 31, 2009
ASSETS		
Property, plant and equipment		
Utility plant—at original cost, net of accumulated depreciation of $3,402,466 in 2010 and $3,168,078 in 2009	$ 11,058,565	$ 10,523,844
Nonutility property, net of accumulated depreciation of $143,051 in 2010 and $117,245 in 2009	143,052	153,549
Total property, plant and equipment	11,201,617	10,677,393
Current assets		
Cash and cash equivalents	13,112	22,256
Restricted funds	94,066	41,020
Utility customer accounts receivable	152,878	149,417
Allowance for uncollectible accounts	(18,043)	(19,035)
Unbilled utility revenues	140,933	130,262
Other receivables, net	74,309	75,086
Income taxes receivable	0	17,920
Materials and supplies	28,867	29,521
Other	48,185	52,680
Total current assets	534,307	499,127
Regulatory and other long-term assets		
Regulatory assets	1,016,007	952,020
Restricted funds	26,718	20,212
Goodwill	1,250,692	1,250,381
Other	50,432	53,518
Total regulatory and other long-term assets	2,343,849	2,276,131
TOTAL ASSETS	$ 14,079,773	$ 13,452,651

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Balance Sheets—(Continued)
(In thousands, except per share data)

	December 31, 2010	December 31, 2009
CAPITALIZATION AND LIABILITIES		
Capitalization		
Common stock ($.01 par value, 500,000 shares authorized, 174,996 shares outstanding in 2010 and 174,630 in 2009)	$ 1,750	$ 1,746
Paid-in capital	6,156,675	6,140,077
Accumulated deficit	(1,959,235)	(2,076,287)
Accumulated other comprehensive loss	(71,446)	(64,677)
Treasury stock	(19)	0
Common stockholders' equity	4,127,725	4,000,859
Preferred stock without mandatory redemption requirements	4,547	4,557
Total stockholders' equity	4,132,272	4,005,416
Long-term debt		
Long-term debt	5,410,271	5,288,180
Redeemable preferred stock at redemption value	23,271	23,946
Total capitalization	9,565,814	9,317,542
Current liabilities		
Short-term debt	229,699	119,497
Current portion of long-term debt	44,760	54,068
Accounts payable	199,240	138,609
Taxes accrued, including income taxes of $906 in 2010 and $1,777 in 2009	46,710	45,552
Interest accrued	60,874	60,128
Other	193,223	189,538
Total current liabilities	774,506	607,392
Regulatory and other long-term liabilities		
Advances for construction	611,209	633,509
Deferred income taxes	1,093,055	851,677
Deferred investment tax credits	31,023	32,590
Regulatory liabilities	303,743	322,281
Accrued pension expense	422,386	431,010
Accrued postretirement benefit expense	215,751	236,045
Other	45,824	47,325
Total regulatory and other long-term liabilities	2,722,991	2,554,437
Contributions in aid of construction	1,016,462	973,280
Commitments and contingencies (See Note 16)	—	—
TOTAL CAPITALIZATION AND LIABILITIES	$ 14,079,773	$ 13,452,651

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENTS - 2010

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Operations and Comprehensive Income (Loss)

(In thousands, except per share data)

	Years Ended December 31,		
	2010	2009	2008
Operating revenues	$ 2,710,677	$ 2,440,703	$ 2,336,928
Operating expenses			
Operation and maintenance	1,389,212	1,283,417	1,262,283
Depreciation and amortization	354,650	335,178	312,776
General taxes	218,653	199,262	199,139
Loss (gain) on sales of assets	71	(763)	(374)
Impairment charge	0	450,000	750,000
Total operating expenses, net	1,962,586	2,267,094	2,523,824
Operating income (loss)	748,091	173,609	(186,896)
Other income (expenses)			
Interest, net	(315,043)	(296,545)	(285,155)
Allowance for other funds used during construction	10,003	11,486	14,497
Allowance for borrowed funds used during construction	6,284	7,224	8,171
Amortization of debt expense	(4,557)	(6,647)	(5,895)
Other, net	4,658	(792)	4,684
Total other income (expenses)	(298,655)	(285,274)	(263,698)
Income (loss) before income taxes	449,436	(111,665)	(450,594)
Provision for income taxes	181,609	121,418	111,827
Net income (loss)	$ 267,827	$ (233,083)	$ (562,421)
Other comprehensive income, net of tax:			
Change in employee benefit plan funded status, net of tax of ($7,567), $6,381 and ($41,007), respectively	(11,836)	9,981	(64,139)
Pension plan amortized to periodic benefit cost:			
Prior service cost, net of tax of $50, $29 and $17, respectively	79	46	26
Actuarial loss, net of tax of $2,793, $3,832 and $0, respectively	4,368	5,994	1
Foreign currency translation adjustment	620	1,553	244
Other comprehensive income	(6,769)	17,574	(63,868)
Comprehensive income (loss)	$ 261,058	$ (215,509)	$ (626,289)
Income (loss) per common share:			
Basic	$ 1.53	$ (1.39)	$ (3.52)
Diluted	$ 1.53	$ (1.39)	$ (3.52)
Average common shares outstanding during the period:			
Basic	174,833	168,164	159,967
Diluted	175,124	168,164	159,967
Dividends per common share	$ 0.86	$ 0.82	$ 0.40

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENTS - 2010

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Cash Flows

(In thousands, except per share data)

	Years Ended December 31,		
	2010	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income (loss)	$ 267,827	$ (233,083)	$ (562,421)
Adjustments			
Depreciation and amortization	354,650	335,178	312,776
Impairment charge	0	450,000	750,000
Provision for deferred income taxes	157,602	140,821	95,643
Amortization of deferred investment tax credits	(1,567)	(1,433)	(1,338)
Provision for losses on utility accounts receivable	18,697	21,781	17,267
Allowance for other funds used during construction	(10,003)	(11,486)	(14,497)
Loss (gain) on sale of assets	71	(763)	(374)
Pension and non-pension post retirement benefits	89,342	105,133	50,309
Stock-based compensation expense	10,334	7,602	4,534
Other, net	(20,514)	(30,007)	(200)
Changes in assets and liabilities			
Receivables and unbilled utility revenues	(33,044)	(18,751)	(20,702)
Taxes receivable, including income taxes	17,920	(17,920)	23,111
Other current assets	5,149	(6,737)	(11,194)
Pension and non-pension post retirement benefit contributions	(137,257)	(127,446)	(105,053)
Accounts payable	6,487	52	2,978
Taxes accrued, including income taxes	39,577	(13,321)	13,460
Interest accrued	746	6,499	2,790
Other current liabilities	8,916	(9,963)	(4,920)
Net cash provided by operating activities	774,933	596,156	552,169
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures	(765,636)	(785,265)	(1,008,806)
Acquisitions	(1,642)	(18,144)	(12,512)
Proceeds from sale of assets and securities	239	1,237	12,604
Removal costs from property, plant and equipment retirements, net	(43,695)	(29,900)	(24,793)
Net funds released	63,991	129,711	2,457
Other	0	(1,250)	(2,617)
Net cash used in investing activities	(746,743)	(703,611)	(1,033,667)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from long-term debt	268,559	542,926	279,941
Repayment of long-term debt	(272,700)	(178,131)	(241,500)
Proceeds from issuance of common stock (net of 2009 expenses of $7,824)	0	242,301	0
Net borrowings (repayments) under short-term debt agreements	93,029	(352,005)	258,684
Proceeds from issuances of employee stock plans and DRIP	6,711	2,089	836
Advances and contributions for construction, net of refunds of $35,830 in 2010, $27,481 in 2009 and $57,580 in 2008	7,042	21,211	3,078
Change in cash overdraft position	17,173	(7,508)	(188)
Capital contributions	0	0	245,000
Debt issuance costs	(6,619)	(13,165)	(4,008)
Redemption of preferred stocks	(228)	(218)	(229)
Dividends paid	(150,301)	(137,331)	(64,055)
Net cash (used in) provided by financing activities	(37,334)	120,169	477,559
Net (decrease) increase in cash and cash equivalents	(9,144)	12,714	(3,939)
Cash and cash equivalents at beginning of period	22,256	9,542	13,481
Cash and cash equivalents at end of period	$ 13,112	$ 22,256	$ 9,542
Cash paid during the year for:			
Interest, net of capitalized amount	$ 329,417	$ 303,958	$ 294,508
Income taxes, net of refunds of $37,790 in 2010, $2,754 in 2009 and $40,400 in 2008	$ (30,108)	$ 11,205	$ (22,161)
Non-cash investing activity			
Capital expenditures acquired on account but unpaid as of year-end	$ 112,313	$ 59,219	$ 72,657
Non-cash financing activity			
Advances and contributions	$ 27,566	$ 77,094	$ 83,041
Long-term debt (See Note 11)	$ 122,775	$ 179,931	$ —

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENTS - 2010

American Water Works Company, Inc. and Subsidiary Companies

Consolidated Statements of Changes in Stockholders' Equity

(In thousands, except per share data)

	Common Stock					Treasury Stock		Preferred Stock of Subsidiary Companies Without Mandatory Redemption Requirements	Total Stockholders' Equity
	Shares	Par Value	Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Shares	At Cost		
Balance at December 31, 2007	160,000	$ 1,600	$ 5,637,947	$ (1,079,118)	$ (18,383)	0	$ 0	$ 4,568	$ 4,546,614
Net loss	—	—	—	(562,421)	—	—	—	—	(562,421)
Equity investment by RWE	—	—	245,000	—	—	—	—	—	245,000
Contribution of common stock by RWE	—	—	1,933	—	—	(90)	(1,933)	—	—
Employee stock purchase plan (ESPP)	—	—	69	—	—	39	836	—	905
Stock-based compensation activity	—	—	3,304	—	—	51	1,090	—	4,394
Subsidiary preferred stock redemption	—	—	—	—	—	—	—	(11)	(11)
Other comprehensive income (loss), net of tax of ($40,990)	—	—	—	—	(63,868)	—	—	—	(63,868)
Dividends	—	—	—	(64,055)	—	—	—	—	(64,055)
Balance at December 31, 2008	160,000	$ 1,600	$ 5,888,253	$ (1,705,594)	$ (82,251)	0	$ (7)	$ 4,557	$ 4,106,558
Net loss	—	—	—	(233,083)	—	—	—	—	(233,083)
Common stock offering, net of expenses of $7,824	14,500	145	242,156	—	—	—	—	—	242,301
Employee stock purchase plan (ESPP)	128	1	2,453	—	—	1	23	—	2,477
Stock-based compensation activity	2	—	7,215	(279)	—	(1)	(16)	—	6,920
Other comprehensive income (loss), net of tax of $10,242	—	—	—	—	17,574	—	—	—	17,574
Dividends	—	—	—	(137,331)	—	—	—	—	(137,331)
Balance at December 31, 2009	174,630	$ 1,746	$ 6,140,077	$ (2,076,287)	$ (64,677)	0	$ 0	$ 4,557	$ 4,005,416
Net income	—	—	—	267,827	—	—	—	—	267,827
Direct stock reinvestment and purchase plan (DRIP), net of expense of $96	63	1	1,328	—	—	—	—	—	1,329
Employee stock purchase plan (ESPP)	112	1	2,502	—	—	7	127	—	2,630
Stock-based compensation activity	191	2	12,768	(474)	—	(8)	(146)	—	12,150
Subsidiary preferred stock redemption	—	—	—	—	—	—	—	(10)	(10)
Other comprehensive income (loss), net of tax of ($4,724)	—	—	—	—	(6,769)	—	—	—	(6,769)
Dividends	—	—	—	(150,301)	—	—	—	—	(150,301)
Balance at December 31, 2010	174,996	$ 1,750	$ 6,156,675	$ (1,959,235)	$ (71,446)	(1)	$ (19)	$ 4,547	$ 4,132,272

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies

Notes to Consolidated Financial Statements
(In thousands, except per share data)

Note 1: Organization and Operation

American Water Works Company, Inc. ("AWW") and its subsidiaries (collectively referred to herein as the "Company") is the holding company for regulated and market based subsidiaries throughout the United States of America and two Canadian provinces. The regulated subsidiaries provide water and wastewater services as public utilities. These regulated subsidiaries are operationally segregated into 20 U.S. states in which the Company operates regulated utilities. The market based subsidiaries include various lines of business including Homeowner Services, which provides water and sewer line protection plans for homeowners, and the Operations and Maintenance contracts group, which conducts operation and maintenance of water and wastewater facilities for the U.S. Military, municipalities, the food and beverage industry and other customers.

Note 2: Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of AWW and its subsidiaries. Intercompany balances and transactions between subsidiaries have been eliminated. The Company uses the equity method to report its investments in two joint venture investments in each of which the Company holds a 50% voting interest and cannot exercise control over the operations and policies of the investments. Under the equity method, the Company records its interests as an investment and its percentage share of earnings as earnings or losses of investee.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The Company considers benefit plan assumptions; the carrying values of goodwill and other long-lived assets, including regulatory assets; revenue recognition; and accounting for income taxes to be its critical accounting estimates. The Company's significant estimates that are particularly sensitive to change in the near term are amounts reported for pension and other postemployment benefits, contingency-related obligations and goodwill.

Regulation

The Company's regulated utilities are subject to economic regulation by the public utility commissions and the local governments of the states in which they operate (the "Regulators"). These Regulators have allowed recovery of costs and credits which the Company has recorded as regulatory assets and liabilities. Accounting for future recovery of costs and credits as regulatory assets and liabilities is in accordance with authoritative guidance applicable to those companies whose rates are established by or are subject to approval by an independent third-party regulator. Regulated utilities defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate making process in a period different from the period in which they would have been reflected in operations by a market based company. These deferred regulatory assets and liabilities are then reflected in the statement of operations in the period in which the costs and credits are reflected in the rates charged for service. (See Note 7)

Property, Plant and Equipment

Property, plant and equipment consist primarily of utility plant. Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. The costs incurred to acquire and internally develop computer software for internal use are capitalized as a unit of property. The carrying value of these costs amounted to $57,294 and $58,655 at December 31, 2010 and 2009, respectively. The cost of repairs; maintenance, including planned major maintenance activities; and minor replacements of property is charged to maintenance expense as incurred.

When units of property are replaced, retired or abandoned, the recorded value thereof is credited to the asset account and charged to accumulated depreciation. To the extent the Company recovers cost of removal or other retirement costs through rates after the retirement costs are incurred, a regulatory asset is recorded. In some cases, the Company recovers retirement costs through rates during the life of the associated asset and before the costs are incurred. These amounts result in a regulatory liability being reported based on the amounts previously recovered through customer rates, until the costs to retire those assets are incurred.

The cost of property, plant and equipment is depreciated using the straight-line average remaining life method.

Nonutility property consists primarily of buildings and equipment utilized by the Company for internal operations. This property is stated at cost, net of accumulated depreciation calculated using the straight-line method over the estimated useful lives of the assets, ranging from three to 50 years.

Cash and Cash Equivalents

Substantially all cash is invested in interest-bearing accounts. All highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

The Company had book overdrafts for certain of its disbursement accounts of $51,675 and $34,502 at December 31, 2010 and 2009, respectively. A book overdraft represents transactions that have not cleared the bank accounts at the end of the period. The Company transfers cash on an as-needed basis to fund these items as they clear the bank. The balance of the book overdraft is reported as short-term debt and the change in the book overdraft balance is reported as cash flows from financing activities.

Restricted Funds

Restricted funds primarily represent proceeds from financings for the construction and capital improvement of facilities and deposits for future services under operation and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within 12 months subsequent to year-end are classified as current.

Utility Customer Accounts Receivable

Regulated utility customer accounts receivable represent amounts billed to water and wastewater customers on a cycle basis. Credit is extended based on the guidelines of the applicable Regulators and generally, collateral is not required.

Allowance for Uncollectible Accounts

Allowances for uncollectible accounts are maintained for estimated probable losses resulting from the Company's inability to collect receivables from customers. Accounts that are outstanding longer than the payment terms are considered past due. A number of factors are considered in determining the allowance for uncollectible accounts, including the length of time receivables are past due and previous loss history. The Company writes off accounts when they become uncollectible. (See Note 5)

Other Receivables, Net

Other receivables, net consists of market based trade accounts receivable and market based unbilled revenues, net of a reserve for doubtful accounts, and non-utility customer receivables of the regulated subsidiaries. In determining the reserve for uncollectible market based accounts, the Company considers the length of time the trade accounts receivable are past due and the customers' current ability to pay their obligations. Unbilled receivables are accrued when service has been provided but has not been billed to customers. (See Note 6)

Materials and Supplies

Materials and supplies are stated at the lower of cost or net realizable value. Cost is determined using the average cost method.

Goodwill

Goodwill is primarily associated with the acquisitions of American Water Works Company, Inc. in 2003 and E'town Corporation in 2001 (the "Acquisitions") and has been assigned to reporting units based on the fair values at the date of the Acquisitions. The Regulated Businesses segment is a single reporting unit. In the Market-Based Operations segment, the business is organized into seven reporting units for its market based services. Goodwill is reviewed annually, or more frequently if changes in circumstances indicate the carrying value may not be recoverable. Annual impairment reviews are performed in the fourth quarter of the calendar year, in conjunction with the timing of the completion of the Company's annual strategic business plan.

The Company considers the carrying value of goodwill to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to value goodwill to be appropriate. However, if experience differs from the assumptions and considerations used in its analysis, the resulting change could have a material adverse impact on the consolidated financial statements.

No impairment charge was recorded for the year ended December 31, 2010. For the years ended December 31, 2009 and 2008, the Company recorded impairment charges for goodwill of $450,000 and $750,000, respectively. (See Note 8)

Long-Lived Assets

Long-lived assets include land, buildings, equipment and long-term investments. Long-lived assets, other than investments and land, are depreciated over their estimated useful lives, and are reviewed for impairment whenever changes in circumstances indicate the carrying value of the asset may not be recoverable. Such circumstances would include items such as a significant decrease in the market value of a long-lived asset, a significant adverse change in the manner the asset is being used or planned to be used or in its physical condition, or a history of operating or cash flow losses associated with the use of the asset. In addition, changes in the expected useful life of these long-lived assets may also be an impairment indicator. When such events or changes occur, the Company estimates the fair value of the asset from future cash flows expected to result from the use and, if applicable, the eventual disposition of the assets and compares that to the carrying value of the asset. If the carrying value is greater than the fair value, an impairment loss is recorded.

The Company considers the carrying value of long-lived assets to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to evaluate the carrying value of long-lived assets to be appropriate. However, if actual experience differs from the assumptions and considerations used in its estimates, the resulting change could have a material adverse impact on the consolidated financial statements.

The key variables to determine value include assumptions regarding sales volume, rates, operating costs, labor and other benefit costs, capital additions, assumed discount rates and other economic factors. These variables require significant management judgment and include inherent uncertainties since they are forecasting future events. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

The long-lived assets of the regulated utility subsidiaries are grouped on a separate entity basis for impairment testing as they are integrated state-wide operations that do not have the option to curtail service and generally have uniform tariffs. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

The Company holds other investments including investments in privately held companies and investments in joint ventures accounted for using the equity method. The Company's investments in privately held companies and joint ventures are classified as other long-term assets.

The fair values of long-term investments are dependent on the financial performance and solvency of the entities in which the Company invests, as well as volatility inherent in the external markets. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

Advances and Contributions in Aid of Construction

Regulated utility subsidiaries may receive advances and contributions from customers, home builders and real estate developers to fund construction necessary to extend service to new areas. Advances for construction are refundable for limited periods of time as new customers begin to receive service or other contractual obligations are fulfilled. Included in other current liabilities at December 31, 2010 and 2009 in the accompanying Consolidated Balance Sheets are estimated refunds of $25,234 and $34,207, respectively. Those amounts represent expected refunds during the next 12-month period. Advances which are no longer refundable are reclassified to contributions in aid of construction. Contributions in aid of construction are permanent collections of plant assets or cash for a particular construction project. For ratemaking purposes, the amount of such contributions generally serves as a rate base reduction since the contributions represent non-investor supplied funds. Non-cash utility property has been received, primarily from developers, as advances or contributions of $27,566, $77,094 and $83,041 for the years ended December 31, 2010, 2009 and 2008, respectively.

Generally, the Company depreciates utility plant funded by contributions and amortizes its contributions balance as a reduction to depreciation expense, producing a result which is functionally equivalent to reducing the original cost of the utility plant for the contributions. Certain of the Company's subsidiaries do not depreciate contributed property, based on regulatory guidelines. Amortization of contributions in aid of construction was $23,480, $20,227 and $20,219 for the years ended December 31, 2010, 2009 and 2008, respectively.

Recognition of Revenues

Revenues of the regulated utility subsidiaries are recognized as water and wastewater services are provided and include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

The Company has agreements with the United States Government to operate and maintain water and wastewater systems at various military bases pursuant to 50-year contracts ("military agreements"). These contracts also include construction components that are accounted for separately from the operations and management components. The military agreements are subject to periodic price redetermination adjustments and modifications for changes in circumstance. Additionally, the Company has agreements ranging in length from three to 40 years with various industries and municipalities to operate and maintain water and wastewater systems ("O&M agreements"). Revenue from operations and management services are recognized as services are provided. (See Note 16)

Construction Contracts

Revenues from construction projects are recognized over the contract term based on the estimated percentage of completion during the period compared to the total estimated services to be provided over the entire contract. Losses on contracts are recognized during the period in which the loss first becomes probable and estimable. Revenues recognized during the period in excess of billings on construction contracts are recorded as unbilled revenue. Billings in excess of revenues recognized on construction contracts are recorded as other current liabilities until the recognition criteria are met. Changes in contract performance and related estimated contract profitability may result in revisions to costs and revenues and are recognized in the period in which revisions are determined.

Income Taxes

The parent company and its subsidiaries participate in a consolidated federal income tax return for U.S. tax purposes. Members of the consolidated group are charged with the amount of federal income tax expense determined as if they filed separate returns.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. The Company provides deferred income taxes on the difference between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates expected to be in effect when these temporary differences are projected to reverse. In addition, the regulated utility subsidiaries recognize regulatory assets and liabilities for the effect on revenues expected to be realized as the tax effects of temporary differences, previously flowed through to customers, reverse.

Investment tax credits have been deferred by the regulated utility subsidiaries and are being amortized to income over the average estimated service lives of the related assets.

The Company recognizes accrued interest and penalties related to tax positions as a component of income tax expense.

The Company accounts for sales tax collected from customers and remitted to taxing authorities on a net basis.

Allowance for Funds Used During Construction ("AFUDC")

AFUDC is a non-cash credit to income with a corresponding charge to utility plant which represents the cost of borrowed funds or a return on equity funds devoted to plant under construction. The regulated utility subsidiaries record AFUDC to the extent permitted by the Regulators.

Environmental Costs

The Company's water and wastewater operations are subject to federal, state, local and foreign requirements relating to environmental protection, and as such, the Company periodically becomes subject to environmental claims in the normal course of business. Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued, on an undiscounted basis, when it is probable that these costs will be incurred and can be reasonably estimated. Remediation costs accrued amounted to $6,630 and $7,947 at December 31, 2010 and 2009, respectively. At December 31, 2010, $6,600 of the accrual relates to a conservation agreement entered into by a subsidiary of the Company with the National Oceanic and Atmospheric Administration ("NOAA") requiring the Company to, among other provisions, implement certain measures to protect the steelhead trout and its habitat in the Carmel River watershed in the state of California. The Company paid and expensed $3,500 related to this agreement during 2009, and has agreed to pay $1,100 annually from 2010 to 2016. The Company pursues recovery of incurred costs through all appropriate means, including regulatory recovery through customer rates. The Company's regulatory assets at December 31, 2010 and 2009 include $10,642 and $7,700, respectively, related to the NOAA agreement, including an additional $3,500 granted in 2010 for recovery of the 2009 payment.

Derivative Financial Instruments

The Company uses derivative financial instruments for purposes of hedging exposures to fluctuations in interest rates. These derivative contracts are entered into for periods consistent with the related underlying exposures and do not constitute positions

independent of those exposures. The Company does not enter into derivative contracts for speculative purposes and does not use leveraged instruments.

All derivatives are recognized on the balance sheet at fair value. On the date the derivative contract is entered into, the Company may designate the derivative as a hedge of the fair value of a recognized asset or liability (fair-value hedge) or a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash-flow hedge).

Changes in the fair value of a fair-value hedge, along with the gain or loss on the underlying hedged item, are recorded in current-period earnings. The effective portion of gains and losses on cash-flow hedges are recorded in other comprehensive income (loss), until earnings are affected by the variability of cash flows. Any ineffective portion of designated hedges is recognized in current-period earnings.

Cash flows from derivative contracts are included in net cash provided by operating activities.

New Accounting Standards

The following recently announced accounting standards have been adopted by the Company and have been included in the consolidated results of operations, financial position or footnotes of the accompanying Consolidated Financial Statements:

Consolidation of Variable Interest Entities

In June 2009, the Financial Accounting Standards Board ("FASB") issued authoritative guidance that replaces the quantitative-based risk and rewards calculation for determining which reporting entity has a controlling financial interest in a variable interest entity with a qualitative approach. This revised guidance also requires additional disclosures about a reporting entity's involvement in variable interest entities. This guidance is effective for the Company beginning January 1, 2010. These changes did not have an impact on the Company's results of operations, financial position or cash flows; however, these changes could impact the accounting for the Company's interests in a variable interest entity in the future.

Transfers of Financial Assets

In June 2009, the FASB issued authoritative guidance that amends current guidance for accounting for the transfers of financial assets. Key provisions include (i) the removal of the concept of qualifying special purpose entities, (ii) the introduction of the concept of a participating interest, in which a portion of a financial asset has been transferred and (iii) the requirement that to qualify for sale accounting, the transferor must evaluate whether it maintains effective control over transferred financial assets either directly or indirectly. Further, the amendments require enhanced disclosures about the risks that a transferor continues to be exposed to because of its continuing involvement in transferred financial assets. This guidance is effective for the Company beginning January 1, 2010, and is required to be applied prospectively. The adoption of this update did not have an impact on the Company's results of operations, financial position or cash flows.

Fair Value Measurements

In January 2010, the FASB issued authoritative guidance that requires new disclosures of (i) the amounts of significant transfers into and out of Level 1 and Level 2 of the fair value hierarchy and the reasons for those transfers and (ii) information in the reconciliation of recurring Level 3 measurements (those using significant unobservable inputs) about purchases, sales, issuances, and settlements on a gross basis. This update also clarifies existing fair value disclosures about the level of disaggregation and about inputs and valuation techniques used to measure fair value. This guidance is effective for interim and annual periods beginning after December 15, 2009, except for the requirement to disclose information about purchases, sales, issuances and settlements in the reconciliation of Level 3 measurements, which does not become effective until interim and annual periods beginning after December 15, 2010. As this guidance clarifies and provides for additional disclosure requirements only, the adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows. In addition, the Company does not expect the adoption of the requirement to disclose additional information in the reconciliation of Level 3 measurements to have a significant impact on the Company's results of operations, financial position or cash flows

The following recently issued accounting standards are not yet reflected or required to be adopted by the Company or included in the consolidated results of operations or financial position of the Company:

Revenue arrangements with Multiple Deliverables

In October 2009, the FASB issued authoritative guidance that amends existing guidance for identifying separate deliverables in a revenue-generating transaction where multiple deliverables exist, and provides guidance for allocating and recognizing revenue based on those separate deliverables. The guidance is expected to result in more multiple-deliverable arrangements being separable than under current guidance. This guidance is effective for the Company beginning on January 1, 2011 and is required to be applied

prospectively to new or significantly modified revenue arrangements. The Company is currently assessing the impact that the guidance may have on the Company's results of operations, financial position or cash flows.

Business Combinations

In December 2010, the FASB clarified the requirements for reporting of pro forma revenue and earnings disclosures for business combinations. The accounting update specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. As this guidance clarifies and provides for additional disclosure requirements only, the adoption of this guidance is not expected to have an impact on the Company's results of operations, financial position or cash flows.

Intangibles – Goodwill

In December 2010, the FASB issued authoritative guidance that modifies step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. The update requires that for those reporting units, an entity is required to perform step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that impairment may exist. The qualitative factors are consistent with existing authoritative guidance, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. This guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. The Company does not expect the adoption of this update to have a significant impact on the Company's results of operations, financial position or cash flows.

Reclassifications

The Company disclosed in the property, plant and equipment policy note that costs recovered for cost of removal or other retirement obligations are classified as a regulatory asset or regulatory liability depending on the timing of the cost recovered through rates. In either case, the amortization associated with the regulatory asset and regulatory liability for cost of removal had been included within the Company's Consolidated Statements of Operations and Comprehensive Income (Loss) as a component of operations and maintenance expense. The Company has also presented this as amortization of removal costs net of salvage value within the Consolidated Statements of Cash Flows. Beginning with the 2010 year-end consolidated financial statements, the Company is presenting the amortization of removal costs net of salvage value within the depreciation and amortization expense of the Consolidated Statements of Operations and Comprehensive Income (Loss). Based on the manner in which the Company evaluates its results and consistent with the Company's peers, the amortization associated with removal costs is included in depreciation and amortization. The Company has presented this reclassification in all periods within these consolidated financial statements. The following tables set forth the impacts of this reclassification for the prior periods presented in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss).

	2009 Previously Reported	Reclassification	2009 Adjusted Presentation
Operating expenses			
Operations and maintenance	$ 1,324,355	$ (40,938)	$ 1,283,417
Depreciation and amortization	$ 294,240	$ 40,938	$ 335,178

	2008 Previously Reported	Reclassification	2008 Adjusted Presentation
Operating expenses			
Operations and maintenance	$ 1,303,798	$ (41,515)	$ 1,262,283
Depreciation and amortization	$ 271,261	$ 41,515	$ 312,776

The reclassification was made to conform with the Company's current presentation of this expense and had no impact to the total captions presented within the Consolidated Statements of Operations and Comprehensive Income (Loss).

Note 3: Acquisitions and Divestitures

Acquisitions

The Company announced it has entered into a purchase agreement to purchase assets of certain water and wastewater systems in Missouri. The purchase price is approximately $3,000, is subject to regulatory approval, and is expected to close in 2011.

During 2010, the Company closed on six acquisitions of regulated water and wastewater systems for an aggregate purchase price of $1,642. The purchase price for each acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired consisted of plant and equipment of $3,064. Liabilities assumed totaled $1,422, including contributions in aid of construction of $1,109 and regulatory liabilities of $313.

During 2009, the Company closed on seven acquisitions (six regulated water and wastewater systems, and one in its Market-Based Operations segment) for an aggregate purchase price of $18,144. The purchase price for each acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired totaled $29,462, including plant and equipment of $17,843, current assets of $5,857, goodwill of $606, and long-lived assets of $5,156. Liabilities assumed totaled $11,318, including debt of $3,990, current liabilities of $5,732, long-term liabilities of $970, and contributions in aid of construction of $626.

Divestitures

On January 24, 2011, the Company announced that it had entered into a Stock Purchase Agreement (the “Sale Agreement”) to sell all the stock of the Company’s Arizona and New Mexico subsidiaries for $470,000 in cash, subject to certain closing adjustments.

These two subsidiaries are included in the Regulated Businesses segment. The total assets, liabilities and revenues for these two subsidiaries were $769,359, $596,742 and $97,547, respectively, as of and for the year ended December 31, 2010.

Closing of the transaction is subject to customary closing conditions, including approval by the Arizona and New Mexico public utility commissions. The Company plans to use the proceeds from the sale to reduce both equity and debt financing.

Based on a preliminary assessment of the sale price and a review of the carrying value of the subsidiary companies, there is no anticipated impairment expected to be recorded as a result of the Sale Agreement.

The Company also announced prior to December 31, 2010 that it had reached an agreement to sell all the assets and certain liabilities of its Texas subsidiary. The assets and revenues of this subsidiary company are included in the Regulated Businesses segment. The sales price and net carrying value are approximately $6,100. Revenues were $3,321 for the year ended December 31, 2010. The Company has not classified the assets and liabilities as held for sale as it is immaterial to the Consolidated Balance Sheets presented and the segment information presented in Note 21. This sale is subject to approval by the Texas Commission on Environmental Quality and is subject to certain closing adjustments.

Note 4: Utility Plant

The components of utility plant by category at December 31 are as follows:

	Range of Remaining Useful Lives	2010	2009
Water plant			
Land and other non-depreciable assets		$ 156,976	$ 144,295
Sources of supply	15 to 127 Years	598,802	564,886
Treatment and pumping facilities	3 to 101 Years	2,766,548	2,675,718
Transmission and distribution facilities	9 to 127 Years	6,682,273	6,290,578
Services, meters and fire hydrants	4 to 96 Years	2,512,234	2,363,394
General structures and equipment	3 to 112 Years	692,717	645,727
Wastewater plant	4 to 86 Years	735,917	702,725
Construction work in progress		315,564	304,599
		14,461,031	13,691,922
Less accumulated depreciation		3,402,466	3,168,078
		$ 11,058,565	$ 10,523,844

Utility plant depreciation expense amounted to $275,844 in 2010, $262,825 in 2009 and $267,763 in 2008. The Company’s regulated utility subsidiaries record depreciation in conformity with amounts approved by state regulators after regulatory review of information the Company submits to support its estimates of the assets’ remaining useful lives.

The provision for depreciation expressed as a percentage of the aggregate average depreciable asset balan-ces was 2.67% in 2010, 2.68% in 2009 and 2.93% in 2008.

Note 5: Allowance for Uncollectible Accounts

The following table summarizes the changes in the Company's allowances for uncollectible accounts:

	2010	2009	2008
Balance at January 1	$ (19,035)	$ (18,644)	$ (20,923)
Amounts charged to expense	(18,697)	(21,781)	(17,267)
Amounts written off	23,452	25,079	22,583
Recoveries of amounts written off	(3,763)	(3,689)	(3,037)
Balance at December 31	$ (18,043)	$ (19,035)	$ (18,644)

Note 6: Other Receivables, Net

Components of the Company's other receivables, net at December 31 are as follows:

	2010	2009
Market based trade accounts receivable	$ 38,290	$ 33,945
Allowance for doubtful accounts—market based trade accounts receivable	(3,510)	(3,837)
Market based unbilled revenue	14,976	15,678
Other	24,553	29,300
	$ 74,309	$ 75,086

The following table summarizes the changes in the Company's market based allowances for uncollectible accounts:

	2010	2009	2008
Balance at January 1	$ (3,837)	$ (5,221)	$ (5,567)
Amounts charged to expense	(429)	(259)	(1,587)
Amounts written off	777	1,805	1,942
Recoveries of amounts written off	(21)	(162)	(9)
Balance at December 31	$ (3,510)	$ (3,837)	$ (5,221)

Note 7: Regulatory Assets and Liabilities

The regulatory assets represent costs that are expected to be fully recovered from customers in future rates. Except for income taxes, regulatory assets are excluded from the Company's rate base and generally do not earn a return. The components of regulatory assets at December 31 are as follows:

	2010	2009
Income taxes recoverable through rates	$ 252,290	$ 233,806
Debt and preferred stock expense	77,138	75,693
Deferred pension expense	215,008	209,288
Deferred other postretirement benefit expense	126,894	141,830
Deferred security costs	7,479	10,121
Deferred business services project expense	10,670	12,496
Deferred tank painting costs	28,420	24,705
Deferred rate case expense	11,409	10,919
Purchase premium recoverable through rates	60,647	61,101
Environmental remediation recoverable through rates	10,642	7,700
Coastal water project costs	27,084	21,056
San Clemente Dam project costs	18,723	16,392
Removal costs recoverable through rates	59,621	46,090
Other	109,982	80,823
	$ 1,016,007	$ 952,020

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference

between book and tax depreciation on property placed in service before the adoption by the regulatory authorities of full normalization for rate making purposes. Full normalization requires no flow through of tax benefits to customers. The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets. The increase in 2010 included $16,979 due to the change in the Company's future tax deductibility of its Medicare Part D subsidy. (See Note 14)

Debt expense is amortized over the lives of the respective issues. Call premiums on the redemption of long-term debt, as well as unamortized debt expense, are deferred and amortized to the extent they will be recovered through future service rates. Expenses of preferred stock issues without sinking fund provisions are amortized over 30 years from date of issue; expenses of issues with sinking fund provisions are charged to operations as shares are retired.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain subsidiaries. These costs will be recovered in future service rates as contributions are made to the pension plan. The Company also has regulatory assets of $184,937 and $166,441 at December 31, 2010 and 2009, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

Postretirement benefit expense in excess of the amount recovered in rates through 1997 has been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service and will be fully recovered over a 20-year period ending in 2012 as authorized by the regulatory authorities. The Company has regulatory assets of $121,665 and $134,180 at December 31, 2010 and 2009, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

The cost of additional security measures that were implemented to protect facilities after the terrorist attacks on September 11, 2001 has been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service by certain subsidiaries. These costs are being recovered over periods ranging from five to ten years.

Business services project expenses consist of reengineering and start-up activities for consolidated customer and shared administrative service centers that began operations in 2001. These costs are recognized in the rates charged for water service by certain subsidiaries.

Tank painting costs are generally deferred and amortized to current operations on a straight-line basis over periods ranging from 5 to 15 years, as authorized by the regulatory authorities in their determination of rates charged for service.

The Company amortizes rate case expenditures over regulatory approved amortization periods, typically three years. Rate case proceeding expenditures probable of future recovery are deferred.

Purchase premium recoverable through rates is primarily the recovery of the acquisition premiums related to an asset acquisition by the Company's California subsidiary during 2002, and acquisitions in 2007 by the Company's New Jersey subsidiary. As authorized for recovery by the California and New Jersey Regulators, these costs are being amortized to operations through November 2048.

Environmental remediation recoverable through rates is the recovery of costs incurred by the Company's California subsidiary under a settlement agreement entered into with NOAA to improve habitat conditions in the Carmel River Watershed.

Coastal water project costs include all preliminary costs associated with the studying, testing and design of alternatives to help solve water supply shortages in Monterey, California. Coastal water project costs incurred through December 31, 2008 have been reviewed and approved for recovery through a surcharge that went into effect January 1, 2007. Costs deferred during 2010 and 2009 totaled $7,677 and $6,542, respectively. The Company believes it is probable that the costs incurred since the last rate review will also be recoverable.

San Clemente Dam project costs include deferred costs for the Company's California subsidiary to investigate alternatives to strengthen or remove the San Clemente Dam due to potential earthquake or flood safety concerns. These costs are not yet in rates; however, the Company believes it is probable that the costs incurred will be recoverable.

Other regulatory assets include certain deferred employee benefit costs, deferred treatment facility costs, as well as various regulatory balancing accounts.

The components of regulatory liabilities at December 31 are as follows:

	2010	2009
Removal costs recovered through rates	$ 264,789	$ 251,837
Deferred income taxes	0	33,103
Other	38,954	37,341
	$ 303,743	$ 322,281

Removal costs recovered through rates are retirement costs recovered during the life of the associated assets. In December 2008, the Company's subsidiary in New Jersey, at the direction of the New Jersey Regulator, began to amortize $48,000 of the total balance into operations via straight line amortization through November 2048.

Deferred income taxes represent the income tax effect of the adjustment to record the full accumulated postretirement benefit obligation. The elimination of the regulatory liability in 2010 was concurrent with the change in the future tax deductibility of the Company's Medicare Part D subsidy (see Note 14), which eliminated any excess deferred tax assets resulting from that subsidy's portion of the full accumulated postretirement benefit obligation.

Other regulatory liabilities include legal settlement proceeds, deferred gains, future customer refunds, and various regulatory balancing accounts.

Note 8: Goodwill

The Company's annual impairment reviews are performed as of November 30 of each year, in conjunction with the timing of the completion of the Company's annual strategic business plan. At November 30, 2010, the Company's goodwill was $1,250,692. The Company also undertakes interim reviews when the Company determines that a triggering event that would more likely than not reduce the fair value of a reporting unit below its carrying value has occurred.

The Company uses a two-step impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). The step 1 calculation used to identify potential impairment compares the calculated fair value for each of the Company's reporting units to their respective net carrying values (book values), including goodwill, on the measurement date. If the fair value of any reporting unit is less than such reporting unit's carrying value, then step 2 is performed to measure the amount of the impairment loss (if any) for such reporting unit.

The step 2 calculation of the impairment test compares, by reporting unit, the implied fair value of the goodwill to the carrying value of goodwill. The implied fair value of goodwill is equal to the excess of the fair value of each reporting unit above the fair value of such reporting unit's identified assets and liabilities. If the carrying value of goodwill exceeds the implied fair value of goodwill for any reporting unit, an impairment loss is recognized in an amount equal to the excess (not to exceed the carrying value of goodwill) for that reporting unit.

The determination of the fair value of each reporting unit and the fair value of each reporting unit's assets and liabilities is performed as of the measurement date using observable market data before and after the measurement date (if that subsequent information is relevant to the fair value on the measurement date).

For the November 30, 2010 impairment test, the estimated fair value of the Regulated reporting unit for step 1 was based on a combination of the following valuation techniques:

- observable trading prices of comparable equity securities of publicly-traded water utilities considered by us to be the Company's peers; and
- discounted cash flow models developed from the Company's internal forecasts.

The first valuation technique applies average peer multiples to the Regulated reporting unit's historic and forecasted cash flows. The peer multiples are calculated using the average trading prices of comparable equity securities of publicly-traded water utilities, their published cash flows and forecasts of market price and cash flows for those peers.

The second valuation technique forecasts each reporting unit's three-year cash flows using an estimated long-term growth rate and discounts these cash flows at their respective estimated weighted average cost of capital.

Because of the unique nature, small size and lack of historical earnings of most of the Market-Based reporting units, a market approach historically could not be reasonably applied. As such, the estimated fair values of the Market-Based reporting units were determined entirely on the basis of discounted cash flow models. For the November 30, 2010 impairment test a market approach was introduced to the Market-Based reporting units as the larger Market-Based reporting units have begun to mature.

The Company has completed its November 30, 2010 annual impairment review. Based on this review the Company's goodwill balance was not impaired. The Company's fair value calculated in its 2010 impairment test period was greater than the aggregate carrying value of its reporting units.

However, there can be no assurances that the Company will not be required to recognize an impairment of goodwill in the future due to market conditions or other factors related to the Company's performance. These market events could include a decline over a period of time of the Company's stock price, a decline over a period of time in valuation multiples of comparable water utilities, the lack of an increase in the Company's market price consistent with its peer companies, or decreases in control premiums. A decline in the forecasted results in the Company's business plan, such as changes in rate case results or capital investment budgets or changes in the Company's interest rates, could also result in an impairment charge.

The Company also made certain assumptions, which it believes to be appropriate, that support the fair value of its reporting units. The Company considered, in addition to the listed trading price of the Company's shares, the applicability of a control premium to the Company's shares and certain other factors the Company deemed appropriate. As a result, the Company concluded that the Company's fair value exceeds what the Company might otherwise have concluded had it relied on market price alone.

The difference between the Company's calculated market capitalization (which approximates carrying value) and the aggregate fair value of reporting units resulted from an estimated control premium. The estimated control premium represents the incremental premium a buyer is willing to pay to acquire a controlling, majority interest in the Company. In estimating the control premium, management principally considered the current market conditions and historical premiums paid in utility acquisitions observed in the marketplace.

No impairment charge was recorded for the year ended December 31, 2010. For the years ended December 31, 2009 and 2008, the Company recorded impairment charges for goodwill in the amount of $450,000 and $750,000, respectively.

The Company's calculated market capitalization at March 31, 2009 was $1,186,000 below the aggregated carrying value of its reporting units. During the first quarter of 2009, the Company's market price experienced a high degree of volatility and, as of March 31, 2009, had a sustained period for which it was below historical averages and 10% below the market price employed in the Company's 2008 annual goodwill impairment test. Having considered both qualitative and quantitative factors, management concluded that this sustained decline in market value below the market value which existed at the 2008 annual impairment test was an interim triggering event. An interim impairment test was performed and $450,000 was recognized as a goodwill impairment charge, primarily in the Regulated reporting unit, for the three months ended March 31, 2009.

As of March 31, 2008, in light of the initial public offering price and trading levels in the Company's common stock subsequent to the date of the initial public offering, the Company performed an interim impairment test and, on May 9, 2008, management concluded that the carrying value of the Company's goodwill was impaired. The Company believed that the initial public offering price was indicative of the value of the Company at March 31, 2008, and accordingly, based on those factors recorded an impairment charge to the goodwill of its Regulated reporting unit in the amount of $750,000 as of March 31, 2008. The impairment charge was primarily attributed to the market price of the Company's common stock (both the initial public offering price and the price during subsequent trading) being less than the estimate of the initial public offering price used during the 2007 annual test. Also contributing to the impairment was a decline in the fair value of the Company's debt (due to increased market interest rates).

The change in the Company's goodwill assets, as allocated between the reporting units is as follows:

	Regulated Unit		Market Based Units		Consolidated		
	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Total Net
Balance at January 1, 2009	$ 3,565,215	$ (1,995,380)	$ 235,549	$ (105,867)	$ 3,800,764	$ (2,101,247)	$ 1,699,517
Goodwill from acquisitions.....	440	—	166	—	606	—	606
Impairment losses	—	(448,248)	—	(1,752)	—	(450,000)	(450,000)
Reclassifications and other activity.....	258	—	—	—	258	—	258
Balance at December 31, 2009.....	$ 3,565,913	$ (2,443,628)	$ 235,715	$ (107,619)	$ 3,801,628	$ (2,551,247)	$ 1,250,381
Reclassifications and other activity.....	36	—	275	—	311	—	311
Balance at December 31, 2010.....	$ 3,565,949	$ (2,443,628)	$ 235,990	$ (107,619)	$ 3,801,939	$ (2,551,247)	$ 1,250,692

Note 9: Stockholders' Equity

Common Stock

On March 23, 2010, the Company filed a Form S-3 Registration Statement with the SEC to register 5,000 shares of the Company's common stock issuable under American Water Stock Direct, a dividend reinvestment and direct stock purchase plan (the "DRIP"). Under the DRIP, stockholders may reinvest cash dividends and purchase additional Company common stock, up to certain limits, through a transfer agent without commission fees. The Company's transfer agent may buy newly issued shares directly from the Company or shares held in the Company's treasury. The transfer agent may also buy shares in the public markets or in privately negotiated transactions. Purchases generally will be made and credited to DRIP accounts once each week. As of December 31, 2010, there remained 4,937 shares available for issuance under the DRIP. The Company issued 63 shares of common stock with proceeds of $1,425 during 2010 under the DRIP.

During 2009, RWE Aktiengesellschaft ("RWE") completed the divestiture of its investment in the Company that began with the April 28, 2008 initial public offering ("IPO") of the Company's stock. In April and May 2008, RWE sold 63,173 shares of common stock, including an underwriters' option of 5,173 shares, at an IPO price of $21.50. The Company did not receive any proceeds from the sale of shares. Prior to the IPO, the Company was an indirect wholly-owned subsidiary of RWE. After the IPO and exercise of the underwriters' over-allotment option, RWE owned approximately 60% of the Company's common shares.

Pursuant to a public offering in June 2009, the Company completed the sale of 14,500 shares of common stock at $17.25 per share. The proceeds from the offering, net of underwriters' discounts and expenses payable by the Company, were $242,301. The Company used the proceeds to repay short-term debt.

RWE completed the divestiture of its investment in the Company in 2009 through a June 2009 sale of 15,400 shares, including an underwriters' option of 3,900 shares, at a price per share of $17.25; an August 2009 sale of 40,250 shares, including underwriters' options of 5,250 shares, at a price of $19.25; and a November 2009 sale of 41,087 shares, including an underwriters' option of 3,735 shares, at a price of $21.63. The Company did not receive any proceeds from these sales by RWE of the Company's shares.

Effective the first quarter of 2008, the Company's Board of Directors' authorized 50,000 shares of par value $0.01 per share preferred stock. As of December 31, 2010 there were no shares outstanding.

In September of 2008, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of August 15, 2008, amounting to $31,992. In December 2008, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of November 18, 2008, amounting to $31,997.

In March 2009, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of February 18, 2009, amounting to $32,000. In June 2009, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of May 18, 2009, amounting to $32,006. In September 2009, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of August 18, 2009, amounting to $36,658. In December 2009, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of November 18, 2009, amounting to $36,667.

In March 2010, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of February 18, 2010, amounting to $36,679. In June 2010, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of May 18, 2010, amounting to $36,689. In September 2010, the Company made a cash dividend payment of $0.22 per share to all common shareholders of record as of August 18, 2010, amounting to $38,457. In December 2010, the Company made a cash dividend payment of $0.22 per share to all common shareholders of record as of November 18, 2010, amounting to $38,476.

On January 28, 2011, the Company's Board of Directors declared a quarterly cash dividend payment of $0.22 per share payable on March 1, 2011 to all shareholders of record as of February 18, 2011.

Accumulated Other Comprehensive Loss

The following table presents accumulated other comprehensive loss:

	2010	2009
Employee benefit plans funded status adjustments	$ (75,639)	$ (68,250)
Foreign currency translation	4,193	3,573
Balance at December 31	$ (71,446)	$ (64,677)

Stock Based Compensation

The Company has granted stock option and restricted stock unit awards to non-employee directors, officers and other key employees of the Company pursuant to the terms of its 2007 Omnibus Equity Compensation Plan (the "Plan"). The total aggregate number of shares of common stock that may be issued under the Plan was increased to 15,500 from 6,000 in May of 2009. As of December 31, 2010, a total of 11,801 shares are available for grant under the Plan. Shares issued under the Plan may be authorized but unissued shares of Company stock or reacquired shares of Company stock, including shares purchased by the Company on the open market for purposes of the Plan.

The Company recognizes compensation expense for stock awards over the vesting period of the award. The following table presents stock-based compensation expense recorded in operations and maintenance expense in the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss) for the years ended December 31, 2010, 2009 and 2008:

	2010	2009	2008
Stock options	$ 4,116	$ 3,415	$ 1,607
Restricted stock units	5,863	3,799	957
Restricted stock	—	—	1,798
Employee stock purchase plan	355	388	172
Stock-based compensation in operation and maintenance expense	10,334	7,602	4,534
Income tax benefit	(4,030)	(2,965)	(1,768)
After-tax stock-based compensation expense	$ 6,304	$ 4,637	$ 2,766

There were no significant stock-based compensation costs capitalized during the years ended December 31, 2010, 2009 and 2008.

The cost of services received from employees in exchange for the issuance of stock options and restricted stock awards is measured based on the grant date fair value of the awards issued. The value of stock options and restricted stock awards at the date of the grant is amortized through expense over the requisite service period, which is generally three years. All awards granted in 2010, 2009 and 2008 are classified as equity.

The Company receives a tax deduction based on the intrinsic value of the award at the exercise date for stock options and the distribution date for restricted stock and restricted stock units. For each award, throughout the requisite service period, the Company recognizes the tax benefit related to compensation costs, which have been included in deferred tax assets. The tax deductions in excess of the benefits recorded throughout the requisite service period are recorded to shareholders' equity or the income statement and are included in the financing section of the statement of cash flows.

The Company stratified its grant populations and used historic employee turnover rates to estimate employee forfeitures. The estimated rate is compared to the actual forfeitures at the end of the period and adjusted as necessary.

Stock Options

On April 22, 2008, the Company granted 2,078 non-qualified stock options to certain employees and non-employee directors under the Plan. The stock options were awarded in two grants with "Grant 1" vesting on January 1, 2010 and "Grant 2" vesting January 1, 2011. These awards included 1,470 stock options that are subject to performance based vesting requirements. The performance conditions for Grant 1 are based on the achievement of 120% of net income targets in 2007 and 2008. Grant 2 performance conditions are based on the achievement of 120% of net income targets in 2008 and 2009. In February 2009, the Company cancelled 311 of the stock options related to the first performance vesting period because the performance goals were not fully met at December 31, 2008. In February 2010, the Company cancelled 459 of the stock options related to the second performance vesting period because the second performance goals were not fully met at December 31, 2009. The Company continued to recognize expense on the remaining stock options during the service period, which ended December 31, 2010.

Additionally during August 2008, the Company granted 5 stock options to newly appointed non-employee directors in two grants vesting on January 1, 2011. These awards had no performance vesting conditions.

In the first quarter of 2009 and 2010, the Company granted 1,091 and 867 non-qualified stock options, respectively, to certain employees under the Plan. The stock options vest ratably over the three-year service period beginning on January 1 of the year of grant. These awards have no performance vesting conditions.

On August 15, 2010, the Company's Board of Directors elected a new President and Chief Executive Officer ("CEO") of the Company. In connection with his election to these offices, the Company's new CEO was granted 25 non-qualified stock options that

cliff vest two years from the date of grant. Additionally in August of 2010, the CEO was granted 53 non-qualified stock options that vest ratably over a three-year period beginning January 1, 2010. These awards have no performance vesting conditions.

Also on August 15, 2010, the Company's former President and Chief Executive Officer resigned as an officer and director of the Company. Pursuant to his resignation, the Company cancelled options to purchase 33 shares of Company stock, accelerated the vesting of 247 options, extended the termination dates of vested options and recognized $315 additional expense related to the modifications that is recorded in operations and maintenance expense in the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss) for the year ended December 31, 2010.

The following table presents the weighted average assumptions used in the pricing model for grants and the resulting weighted average grant date fair value of stock options granted in the years ended December 31, 2010, 2009 and 2008.

	2010	2009	2008
Dividend yield	3.83%	3.86%	3.72%
Expected volatility	31.77%	31.67%	29.00%
Risk-free interest rate	2.14%	1.79%	2.82%
Expected life (years)	4.29	4.36	4.29
Exercise price	$ 22.01	$ 20.70	$ 21.50
Grant date fair value per share	$ 4.33	$ 3.96	$ 4.05

The Company utilized the "simplified method" to determine the expected stock option life due to insufficient historical experience to estimate the exercise patterns of the stock options granted. The Company began granting stock options at the time of the IPO in April 2008. Expected volatility is based on a weighted average of historic volatilities of traded common stock of peer companies (regulated water companies) over the expected term of the stock options and historic volatilities of the Company's common stock during the period it has been publicly traded. The dividend yield is based on the Company's expected dividend payments and the stock price on the date of grant, which was the IPO price for Grants 1 and 2. The risk-free interest rate is the market yield on U.S. Treasury strips with maturities similar to the expected term of the stock options. The exercise price of the stock options is equal to the fair market value of the underlying stock on the date of option grant. Stock options granted vest over periods ranging from one to three years and expire seven years from the effective date of the grant. The fair value of each option is estimated on the date of grant using the Black-Scholes option-pricing model.

The value of stock options at the date of the grant is amortized through expense over the requisite service period using the straight-line method. As of December 31, 2010, $3,074 of total unrecognized compensation costs related to the nonvested stock options is expected to be recognized over the remaining weighted-average period of 1.6 years. The total grant date fair value of stock options vested during the years ended December 31, 2010 and 2009 was $4,505 and $92, respectively.

The table below summarizes stock option activity for the year ended December 31, 2010.

	Shares	Weighted Average Exercise Price (per share)	Weighted Average Remaining Life (years)	Aggregate Intrinsic Value
Options outstanding at January 1, 2010	2,724	$ 21.19		
Granted	945	22.01		
Cancelled	(459)	21.50		
Forfeited or expired	(199)	21.51		
Exercised	(141)	21.30		
Options outstanding at December 31, 2010	2,870	$ 21.38	4.72	$ 11,209
Exercisable at December 31, 2010 (a)	1,008	$ 21.24	3.96	$ 4,085

(a) Includes stock options issued to retired employees

Cash received for stock options exercised during the year ended December 31, 2010 was $3,010 and the intrinsic value of the options was $333, on which the Company recognized an income tax benefit of $130. There were no exercises of options in 2009 and 2008.

Restricted Stock Units

On April 22, 2008, the Company granted 269 restricted stock units to certain employees and non-employee directors under the Plan. The restricted stock units were awarded in two grants with "Grant 1" vesting on January 1, 2010 and "Grant 2" vesting January 1, 2011. The grant date fair value of these restricted stock units is $21.50. These awards included 190 restricted stock units that are subject to performance-based vesting requirements. The performance conditions for Grant 1 are based on the achievement of 120% of net income targets in 2007 and 2008. Grant 2 performance conditions are based on the achievement of 120% of net income targets in 2008 and 2009. In February 2009, the Company cancelled 39 of these restricted stock units related to the first performance vesting period because the performance goals were not fully met at December 31, 2008. In February 2010, the Company cancelled 60 of these restricted stock units related to the second performance vesting period because the second performance goals were not fully met at December 31, 2009. The Company continued to recognize expense on the remaining restricted stock units during the service period, which ended December 31, 2010.

Additionally during August 2008, the Company granted 1 restricted stock units to newly appointed non-employee directors in two grants vesting on January 1, 2011. The weighted average grant date fair value of these restricted stock units is $20.32. These awards had no performance vesting conditions.

In February 2009, the Company granted 195 restricted stock units to certain employees under the Plan. The restricted stock units vest ratably over the three year performance period beginning January 1, 2009 (the "2009 Performance Period"); however, distribution of the shares is contingent upon the achievement of certain market thresholds over the 2009 Performance Period. The grant date fair value of the restricted stock units awarded in February 2009 is $22.08.

In May and June 2009, the Company granted 15 and 5 restricted stock units, respectively, to certain non-employee directors under the Plan. The weighted average grant date fair value of these restricted stock units is $18.56. The restricted stock units vested on the date of the grant and were distributed in August 2010.

In the first quarter of 2010, the Company granted 243 restricted stock units to certain employees under the Plan. The restricted stock units vest ratably over the three year performance period beginning January 1, 2010 (the "2010 Performance Period"); however, distribution of the shares is contingent upon the achievement of internal performance measures and, separately, certain market thresholds over the 2010 Performance Period. The weighted average fair value of the restricted stock units granted with performance and service conditions is $21.95 and for the restricted stock units granted with market and service conditions, the weighted average fair value is $24.16.

On May 7, 2010, the Company granted 19 restricted stock units to non-employee directors under the Plan. The restricted stock units vested on the date of grant; however, distribution of the shares will be made within 30 days of the earlier of August 11, 2011 or the participant's separation from service. The grant date fair value of these restricted stock units was $20.71.

On August 27, 2010, the Company's new CEO was granted 12 restricted stock units that vest over the period beginning August 27, 2010 and ending December 31, 2012; however, distribution of the shares is contingent upon the achievement of internal performance measures and, separately, certain market thresholds over the vesting period. The fair value of the restricted stock units granted with performance and service conditions is $22.74 and for the restricted stock units granted with market and service conditions, the fair value is $25.46.

Also in August 2010, the Company accelerated the vesting of 12 restricted stock units granted in 2008 to the Company's former CEO. Additionally the Company cancelled 9 restricted stock units granted in 2009 and 2010; the remaining outstanding awards will be subject to the Company's achievement of internal performance measures and certain market thresholds over the applicable three-year performance periods as if he had remained in the employ of the Company during the entire performance periods. The net impact associated with these modifications was a reduction to operations and maintenance expense of $12 for the year ended December 31, 2010.

On September 24, 2010, the Company granted 6 restricted stock units to non-employee directors under the Plan. The restricted stock units vested on the date of grant; however, distribution of the shares will be made within 30 days of the earlier of October 15, 2011 or the participant's separation from service. The grant date fair value of these restricted stock units was $23.49.

Restricted stock units generally vest over periods ranging from one to three years. Restricted stock units granted without market conditions are valued at the market value of the Company's common stock on the date of grant. Restricted stock units granted with market conditions are valued using a Monte Carlo model. Expected volatility is based on historical volatilities of traded common stock of the Company and comparative companies using daily stock prices over the past three years. The Company's volatility was calculated using a weighted average of eight and nine companies for the 2010 and 2009 periods, respectively, before the Company's

stock was publically traded. The expected term is three years and the risk-free interest rate is based on the three-year U.S. Treasury rate in effect as of the measurement date. Based on these considerations, weighted average assumptions used in the Monte Carlo simulation are as follows for the years ended December 31, 2010 and 2009:

	2010	2009
Expected volatility	30.74%	32.00%
Risk-free interest rate	1.50%	1.30%
Expected life (years)	3	3

The value of restricted stock awards at the date of the grant is amortized through expense over the requisite service period using the straight-line method for restricted stock units with service and/or performance vesting. The grant date fair value of restricted stock awards that have (a) market and/or performance and service conditions and (b) vest ratably is amortized through expense over the requisite service period using the graded-vesting method. As of December 31, 2010, $2,283 of total unrecognized compensation cost related to the nonvested restricted stock units is expected to be recognized over the weighted-average remaining life of 1.8 years.

The table below summarizes restricted stock unit activity for the year ended December 31, 2010.

	Shares	Weighted Average Grant Date Fair Value (per share)
Nonvested total at January 1, 2010	402	$ 21.77
Granted	280	23.23
Distributed	(58)	20.72
Cancelled	(60)	21.50
Forfeited	(40)	23.13
Undistributed vested awards(a)	(45)	22.47
Nonvested total at December 31, 2010	479	$ 22.60

(a) Includes restricted stock units granted to retired employees and members of the Company's Board of Directors.

The aggregate intrinsic value of restricted stock units distributed during the year ended December 31, 2010 was $1,241, on which the Company recognized an income tax benefit of $15, which has been recorded in the accompanying Consolidated Balance Sheets.

If dividends are declared with respect to shares of the Company's common stock before the restricted stock units are distributed, the Company credits a liability for the value of the dividends that would have been paid if the restricted stock units were shares of Company common stock. When the restricted stock units are distributed, the Company pays the employee a lump sum cash payment equal to the value of the dividend equivalents accrued. The Company accrued dividend equivalents totaling $474, $279 and $66 to retained earnings during the years ended December 31, 2010, 2009 and 2008, respectively.

Employee Stock Purchase Plan

The Company's Nonqualified Employee Stock Purchase Plan ("ESPP") was effective as of July 1, 2008. Under the ESPP, employees can use payroll deductions to acquire Company stock at the lesser of 90% of the fair market value of a) the beginning or b) the end of each three-month purchase period. As of December 31, 2010 there were 1,713 shares of common stock reserved for issuance under the ESPP. The Company's ESPP is considered compensatory. Compensation costs of $355, $388 and $172 were recognized for the years ended December 31, 2010, 2009 and 2008, respectively. During the years ended December 31, 2010, 2009 and 2008, the Company issued 119, 129 and 39 shares, respectively, under the ESPP.

Restricted Stock

On April 22, 2008, a subsidiary of RWE contributed 90 shares of the Company's common stock to the Company and the Company granted 90 restricted stock awards under the 2007 Plan. The requisite service period for the restricted stock was three months and the grant date fair value was $21.50. As of December 31, 2008, the restricted stock was fully vested and there were no unrecognized compensation costs related to the nonvested restricted stock units. The Company issued 84 shares of common stock under this award. The aggregate intrinsic value of restricted stock awards on the date of vesting was $1,647. The Company recognized an income tax shortfall of $60, which was recorded in the Consolidated Statement of Operations and Comprehensive Income (Loss) at the vesting of these awards.

Note 10: Preferred Stock Without Mandatory Redemption Requirements

Certain preferred stock agreements do not require annual sinking fund payments or redemption except at the option of the subsidiaries and are as follows:

	Balance at December 31,	
Dividend Yield	2010	2009
4.50%	$ 1,720	$ 1,720
5.00%	1,952	1,962
5.50%	486	486
5.75%	389	389
	$ 4,547	$ 4,557

Dividends issued totaled $224 in 2010 and $225 in 2009 and 2008, respectively.

The Company reflects its subsidiaries' preferred stock without mandatory redemption requirements in the total stockholders' equity section of the accompanying Consolidated Balance Sheets and represents the Company's noncontrolling interest. The dividends on these preferred shares have not been reflected as income attributable to noncontrolling interest in the Consolidated Statements of Operations and Comprehensive Income (Loss) as the total amount of dividends is not considered material. The dividends issued were $224, $225 and $225 for 2010, 2009 and 2008, respectively. The amounts have been included as a component of other income (expenses) in the accompanying Consolidated Statements of Operations and Comprehensive Income (Loss).

Note 11: Long-Term Debt

The Company primarily incurs long-term debt to fund capital expenditures at the regulated subsidiaries. The components of long-term at December 31 are:

	Rate	Weighted Average Rate	Maturity Date	2010	2009
Long-term debt of American Water Capital Corp. ("AWCC")(a)					
Private activity bonds and government funded debt(b)					
Fixed rate	4.85%-6.75%	5.72%	2018-2040	$ 322,610	$ 200,975
Senior notes					
Fixed rate	5.39%-10.00%	6.26%	2011-2040	3,117,696	3,115,853
Long-term debt of other subsidiaries					
Private activity bonds and government funded debt					
Fixed rate	0.00%-6.20%	4.43%	2011-2039	1,203,834	1,197,611
Floating rate(c)	0.85%-1.05%	0.90%	2015	8,560	8,560
Mortgage bonds					
Fixed rate	5.48%-9.71%	7.48%	2011-2039	744,691	754,966
Mandatory redeemable preferred stock	4.60%-9.75%	8.40%	2013-2036	23,989	24,207
Notes payable and other(d)	4.90%-14.57%	7.49%	2011-2026	5,769	6,561
Long-term debt				5,427,149	5,308,733
Unamortized debt discount, net(e)				51,498	57,461
Fair value adjustment to interest rate hedge				(345)	0
Total long-term debt				$ 5,478,302	$ 5,366,194

(a) AWCC, which is a wholly-owned subsidiary of the Company, has a strong support agreement with its parent, which under certain circumstances, is the functional equivalent of a guarantee.

(b) As of December 31, 2009, the Company held $10,635 of floating rate debt in its treasury, as it had not been able to re-issue the debt to investors at acceptable interest rates. On July 27, 2010, the Company re-issued this debt as fixed rate of 5.25% due 2028.

(c) Represents variable rate tax-exempt bonds remarketed for periods up to 270 days. The $8,560 balance is classified as current portion of long-term debt in the accompanying Consolidated Balance Sheets because it was repurchased by the Company during

the first quarter of 2009 when no investor was willing to purchase it at market rates. This debt was subsequently remarketed as floating rate debt in the second quarter of 2009.

(d) Includes capital lease obligations of $5,076 and $5,679 at December 31, 2010 and 2009, respectively.

(e) Includes fair value adjustments previously recognized in acquisition purchase accounting.

All $744,691 of the subsidiaries' mortgage bonds and $1,154,634 of the $1,203,834 total subsidiaries' private activity bonds and government funded debt are collateralized by utility plant.

Long-term debt indentures contain a number of covenants that, among other things, limit, subject to certain exceptions, the Company from issuing debt secured by the Company's assets. Certain long term notes require the Company to maintain a ratio of consolidated total indebtedness to consolidated total capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2010 was 0.58 to 1.00. In addition, the Company has $2,056,369 of notes which include the right to redeem the notes in whole or in part from time to time subject to certain restrictions.

A portion of senior notes redeemed in 2007 were obtained for the use of certain of the Company's regulated subsidiaries. These notes were redeemed early resulting in a difference of $8,655 between the book value of the notes and the cash consideration required to extinguish the notes. As agreed with the applicable Regulators, the difference on extinguishment was deferred as a regulatory liability by the Company's regulated subsidiaries and will be amortized to Interest, net over the remaining lives of the original notes for periods ranging from 2014 to 2034. The amount amortized was $833, $1,967, and $1,044 in 2010, 2009, and 2008, respectively.

The future sinking fund payments and maturities are as follows:

Year	Amount
2011	$ 44,760
2012	32,915
2013	113,710
2014	10,541
2015	50,707
Thereafter	5,174,516

The following long-term debt was issued in 2010:

Company	Type	Interest Rate	Maturity	Amount
American Water Capital Corp.(1)	Private activity bonds and government funded debt – fixed rate	4.85%-6.00%	2028-2040	$ 151,635
Other subsidiaries	Private activity bonds and government funded debt – fixed rate	0.00%-5.60%	2021-2034	239,699
Total issuances				$ 391,334

(1) Includes $122,775 of proceeds from issuances which are initially kept in Trust, pending the Company's certification that it has incurred qualifying capital expenditures. These issuances have been presented as non-cash on the accompanying Consolidated Statements of Cash Flows. Subsequent release of all or a lesser portion of these funds by the applicable Trust are reflected as the release of restricted funds, and are included in investing activities in the accompanying Consolidated Statements of Cash Flows.

The following long-term debt was retired through optional redemption or payment at maturity during 2010:

Company	Type	Interest Rate	Maturity	Amount
American Water Capital Corp.	Senior notes-fixed rate	6.00%-6.87%	2011-2039	$ 28,157
Other subsidiaries	Private activity bonds and government funded debt-fixed rate	0.00%-6.88%	2010-2036	233,476
Other subsidiaries	Mortgage bond	7.86%-8.98%	2010-2011	10,275
Other subsidiaries	Mandatory redeemable preferred stock	4.60%-6.00%	2013-2019	218
Other	Capital leases & other			792
Total retirements & redemptions				$ 272,918

Interest, net includes interest income of approximately $10,184, $10,422 and $5,690 in 2010, 2009 and 2008, respectively.

One of the principal market risks to which the Company is exposed are changes in interest rates. In order to manage the exposure, the Company follows risk management policies and procedures, including the use of derivative contracts such as swaps. The Company uses a combination of fixed-rate and variable-rate debt to manage interest rate exposure. The Company does not enter into derivative contracts for speculative purposes and does not use leveraged instruments. The derivative contracts entered into are for periods consistent with the related underlying exposures. The Company is exposed to the risk that counterparties to derivative contracts will fail to meet their contractual obligations. The Company minimizes the counterparty credit risk on these transactions by dealing only with leading, credit-worthy financial institutions having long-term credit ratings of "A" or better.

On July 12, 2010, the Company entered into an interest rate swap to hedge $100,000 of its 6.085% fixed rate debt maturing 2017. The Company will pay variable interest of six-month LIBOR plus 3.422%. The swap is accounted for as a fair value hedge, and matures with the fixed rate debt in 2017. The Company uses a combination of fixed-rate and variable-rate debt to manage interest rate exposure.

At December 31, 2010 and December 31, 2009, the Company had a $100,000 and $0 notional amount variable interest rate swap fair value hedge outstanding, respectively. The following table provides a summary of the derivative fair value balance recorded by the Company as of December 31, 2010 and the line item in the Consolidated Balance Sheet in which such amount is recorded:

Balance sheet classification	December 31, 2010	December 31, 2009
Regulatory and other long-term liabilities		
Other	$ 898	$ 0
Long-term debt		
Long-term debt	$ (345)	$ 0

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the hedge instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current net income (loss). The Company includes the gain or loss on the derivative instrument and the offsetting loss or gain on the hedged item in interest expense as follows:

Income Statement Classification	Gain (Loss) on Swap December 31, 2010	Gain (Loss) on Borrowings December 31, 2010	Hedge Ineffectiveness December 31, 2010
Interest, net	$ (898)	$ 345	$ (553)

Note 12: Short-Term Debt

The components of short-term debt at December 31 are as follows:

	2010	2009
Revolving credit lines	$ 2,734	$ 0
Commercial paper, net of $10 and $5 discount at 2010 and 2009, respectively	175,290	84,995
Book overdraft	51,675	34,502
Total short-term debt	$ 229,699	$ 119,497

AWCC had the following available capacity under its commercial paper program at December 31:

	2010	2009
Commercial paper program	$ 700,000	$ 700,000
Commercial paper program available capacity	524,700	615,000

AWCC has entered into an $840,000 senior unsecured credit facility syndicated among the following group of 11 banks with JPMorgan Chase Bank, N.A. acting as administrative agent:

Bank	Commitment Amount Through September 15, 2012	Commitment Amount Through September 15, 2013
JPMorgan Chase Bank, N.A.	$ 115,000	$ 0
Citibank, N.A.	115,000	115,000
Citizens Bank of Pennsylvania	80,000	80,000
Credit Suisse	80,000	80,000
William Street Commitment Corporation	80,000	80,000
Merrill Lynch Bank USA	80,000	80,000
Morgan Stanley Bank	80,000	80,000
UBS Loan Finance LLC	80,000	80,000
National City Bank	50,000	50,000
PNC Bank, N.A.	40,000	40,000
The Bank of New York Mellon	40,000	0
	$ 840,000	$ 685,000

Bank	Commitment Amount Through September 15, 2012	Commitment Amount Through September 15, 2013

This revolving credit facility is principally used to support the commercial paper program at AWCC and to provide up to $150,000 in letters of credit. On September 15, 2008, a majority of the banks agreed to further extend $685,000 of commitments under this revolving credit facility to September 15, 2013. On December 18, 2008, The Bank of New York Mellon joined the credit facility syndicate with a commitment amount of $40,000 through September 15, 2012. If any lender defaults in its obligation to fund advances, the Company may request the other lenders to assume the default lender's commitment or replace such defaulting lender by designating an assignee willing to assume the commitment, however the remaining lenders have no obligation to assume a defaulting lender's commitment and we can provide no assurances that we will replace a defaulting lender.

At December 31, AWCC had the following sub-limits and available capacity under the credit facility.

	2010	2009
Letter of credit sublimit	$ 150,000	$ 150,000
Letter of credit available capacity	113,203	101,754

At December 31, 2010, the Company had $37,275 of outstanding letters of credit, $36,797 of which was issued under the revolving credit facility noted above.

The following table presents the short-term borrowing activity for AWCC for the years ended December 31, 2010 and 2009:

	2010	2009
Average borrowings	$ 164,782	$ 347,413
Maximum borrowings outstanding	263,500	708,691
Weighted average interest rates, computed on a daily basis	0.42%	0.82%
Weighted average interest rates, at December 31	0.46%	0.39%

Interest rates on advances under the credit facility are based on either prime or the London Interbank Offering Rate ("LIBOR") plus an applicable margin based upon credit ratings of the Company, as well as total outstanding amounts under the agreement at the time of the borrowing. The maximum LIBOR margin is 55 basis points.

The credit facility requires the Company to maintain a ratio of consolidated debt to consolidated capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2010 was 0.58 to 1.00.

None of the Company's borrowings are subject to default or prepayment as a result of a downgrading of securities, although such a downgrading could increase fees and interest charges under the Company's credit facilities.

As part of the normal course of business, the Company routinely enters contracts for the purchase and sale of water, energy, fuels and other services. These contracts either contain express provisions or otherwise permit the Company and its counterparties to demand adequate assurance of future performance when there are reasonable grounds for doing so. In accordance with the contracts and applicable contract law, if the Company is downgraded by a credit rating agency, especially if such downgrade is to a level below investment grade, it is possible that a counterparty would attempt to rely on such a downgrade as a basis for making a demand for adequate assurance of future performance. Depending on its net position with a counterparty, the demand could be for the posting of collateral. In the absence of expressly agreed provisions that specify the collateral that must be provided, the obligation to supply the collateral requested will be a function of the facts and circumstances of the Company's situation at the time of the demand. If the Company can reasonably claim that it is willing and financially able to perform its obligations, it may be possible to successfully argue that no collateral should be posted or that only an amount equal to two or three months of future payments should be sufficient. The Company does not expect to post any collateral which will have a material adverse impact on the Company's results of operations, financial position or cash flows.

AWCC has entered into a one year $10,000 committed revolving line of credit with PNC Bank, N.A. Outstanding borrowings against this line totaled $2,734 and $0 at December 31, 2010 and 2009, respectively. This line of credit will terminate on December 31, 2011 unless extended and is used primarily for short-term working capital needs. Interest rates on advances under this line of credit are based on either the prime rate of the financial institution or the applicable LIBOR rate for the term selected plus 175 basis points.

Note 13: General Taxes

Components of general tax expense from continuing operations for the years ended December 31 are as follows:

	2010	2009	2008
Gross receipts and franchise	$ 87,938	$ 81,244	$ 79,228
Property and capital stock	87,028	79,420	80,025
Payroll	33,029	29,749	31,060
Other general	10,658	8,849	8,826
	$ 218,653	$ 199,262	$ 199,139

Note 14: Income Taxes

Components of income tax expense from continuing operations for the years ended December 31 are as follows:

	2010	2009	2008
State income taxes			
Current	$ 25,753	$ (18,525)	$ 16,196
Deferred			
Current	128	(1,599)	409
Non-current	10,410	40,687	10,332
	36,291	20,563	26,937
Federal income taxes			
Current	(179)	555	1,522
Deferred			
Current	306	(11,929)	1,973
Non-current	146,758	113,662	82,929
Amortization of deferred investment tax credits	(1,567)	(1,433)	(1,534)
	145,318	100,855	84,890
	$ 181,609	$ 121,418	$ 111,827

A reconciliation of income tax expense from continuing operations at the statutory federal income tax rate to actual income tax expense for the years ended December 31 is as follows:

	2010	2009	2008
Income tax at statutory rate	$ 157,303	$ (39,083)	$ (157,708)
Increases (decreases) resulting from:			
State taxes, net of federal taxes	23,589	13,366	17,509
Change in valuation allowance	(533)	(6,578)	(158)
Flow through differences	2,969	2,918	2,731
Amortization of deferred investment tax credits	(1,567)	(1,433)	(1,534)
Subsidiary preferred dividends	708	714	716
Impairment charges	0	150,705	252,158
Other, net	(860)	809	(1,887)
Actual income tax expense	$ 181,609	$ 121,418	$ 111,827

The following table provides the components of the net deferred tax liability from continuing operations at December 31:

	2010	2009
Deferred tax assets:		
Advances and contributions	$ 586,595	$ 568,422
Deferred investment tax credits	11,810	12,417
Other postretirement benefits	93,136	100,936
Tax losses and credits	349,710	352,426
Pension benefits	142,185	147,904
Unamortized debt discount, net	22,848	24,100
Other	12,796	23,891
	1,219,080	1,230,096
Valuation allowance	(23,788)	(25,621)
	1,195,292	1,204,475
Deferred tax liabilities:		
Utility plant, principally due to depreciation differences	1,973,613	1,771,263
Income taxes recoverable through rates	93,538	76,697
Deferred security costs	3,065	4,144
Deferred business services project expenses	4,456	4,456
Deferred other postretirement benefits	48,324	53,152
Deferred pension benefits	79,924	77,924
Other	85,427	68,516
	2,288,347	2,056,152
	$ (1,093,055)	$ (851,677)

At December 31, 2010 and 2009, the Company recorded federal net operating loss (“NOL”) carryforwards of $1,185,337 and $1,123,938, respectively. The Company believes the federal NOL carryforwards are more likely than not to be recovered and require no valuation allowance. The Company evaluated its ability to fully utilize the existing federal NOL carryforwards in light of the RWE divestiture in November 2009. Under Internal Revenue Code (“I.R.C.”) Section 382, an ownership change occurs if there is a greater than fifty percent (50%) change in equity ownership of a company over a three year period determined by reference to the ownership of persons holding five percent (5%) or more of that company’s equity securities. If a company undergoes an ownership change as defined by I.R.C. Section 382, the company’s ability to utilize its pre-change NOL carryforwards to offset post-change income may be limited.

The Company believes that the limitation imposed by I.R.C. Section 382 generally should not preclude use of its federal NOL carryforwards, assuming the Company has sufficient taxable income in future carryforward periods to utilize those NOL carryforwards. The Company’s federal NOL carryforwards do not begin expiring until 2024.

At December 31, 2010 and 2009, the Company had state NOLs of $714,674 and $760,190, respectively, a portion of which are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The state NOL carryforwards will expire between 2011 and 2030.

At December 31, 2010 and 2009, the Company had Canadian NOL carryforwards of $5,398 and $13,033, respectively. The majority of these carryforwards are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The Canadian NOL carryforwards will expire between 2014 and 2029.

The Company files income tax returns in the United States federal jurisdiction and various state and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state or local or non-U.S income tax examinations by tax authorities for years before 2005.

In March 2010, the Company filed refund claims of $25,314. The refund claims are attributable to the carry back of Alternative Minimum Tax NOLs generated in 2008. These claims procedurally require approval by the Joint Committee of Taxation (“JCT”). The Company received the refund in April 2010. In August 2010, the IRS notified the Company that additional audit procedures were necessary to support the filing of the JCT report. The audit has not been concluded at December 31, 2010, and no adjustments have been proposed so far.

The Company has state income tax examinations in progress and does not expect material adjustments to result.

The Patient Protection and Affordable Care Act (the "PPACA") became law on March 23, 2010, and the Health Care and Education Reconciliation Act of 2010 became law on March 30, 2010, which makes various amendments to certain aspects of the PPACA (together, the "Acts"). The PPACA effectively changes the tax treatment of federal subsidies paid to sponsors of retiree health benefit plans that provide a benefit that is at least actuarially equivalent to the benefits under Medicare Part D. As a result of the Acts, these subsidy payments will effectively become taxable in tax years beginning after December 31, 2012.

Although this change does not take effect immediately, companies are required to recognize the full accounting impact in their financial statements in the period in which the legislation was enacted. As a result, the Company followed its original accounting for the underfunded status of the other postretirement benefits for the Medicare Part D adjustment and recorded a reduction in deferred tax assets and an increase in its regulatory assets amounting to $16,979.

The following table summarizes the changes in the Company's gross liability, excluding interest and penalties, for unrecognized tax benefits:

Balance at January 1, 2009	$ 1,351
Increases in prior period tax positions	88,248
Increases in current period tax positions	22,631
Decreases due to lapse of statute of limitations	(209)
Balance at December 31, 2009	112,021
Increases in current period tax positions	7,434
Decreases due to lapse of statute of limitations	(1,141)
Balance at December 31, 2010	$ 118,314

The liability balance as of December 31, 2010 and 2009 does not include interest and penalties of $80 and $439, respectively, which is recorded as a component of income tax expense. The majority of the increased tax position is attributable to temporary differences. The increase in 2010 current period tax positions relates primarily to the Company's change in tax accounting method filed in 2008 for repair and maintenance costs on its utility assets. At December 31, 2010, the unrecognized tax benefits for the prior and current periods associated with the change in tax accounting method were approximately $0 and $7,434. At December 31, 2009, the unrecognized tax benefits for the prior and current periods associated with the change in tax accounting method were approximately $88,248 and $15,987. The Company increased the current period tax position in the 2009 unrecognized tax benefits roll forward schedule by an additional $6,644 related to transaction costs deducted in 2009 as a result of RWE's full divestiture of the Company's stock.

The Company does not anticipate material changes to its unrecognized tax benefits within the next year. If the Company sustains all of its positions at December 31, 2010 and 2009, an unrecognized tax benefit of $6,644 and $7,785, respectively, excluding interest and penalties, would impact the Company's effective tax rate.

The following table summarizes the changes in the Company's valuation allowance:

Balance at January 1, 2008	$ 29,021
Increases in current period tax positions	2,369
Decreases in prior period tax positions	(2,528)
Balance at December 31, 2008	$ 28,862
Increases in current period tax positions	2,778
Decreases in current period tax positions	(5,698)
Decreases in prior period tax positions	(321)
Balance at December 31, 2009	$ 25,621
Increases in current period tax positions	907
Decreases in current period tax positions	(2,740)
Balance at December 31, 2010	$ 23,788

Note 15: Employee Benefits

Pension and Other Postretirement Benefits

The Company maintains noncontributory defined benefit pension plans covering eligible non-union employees of its regulated utility and shared services operations. Benefits under the plans are based on the employee's years of service and compensation. The pension plans have been closed for any employees hired on or after January 1, 2006. Union employees hired on or after January 1, 2001 had their accrued benefit frozen and will be able to receive this benefit as a lump sum upon termination or retirement. Union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006 are provided with a 5.25% of base pay defined contribution plan.

The Company's funding policy is to contribute at least the minimum amount required by the Employee Retirement Income Security Act of 1974. Pension plan assets are invested in a number of investments including equity and bond mutual funds, fixed income securities and guaranteed interest contracts with insurance companies.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain regulated subsidiaries pending future recovery in rates charged for utility services as contributions are made to the plans. (See Note 7)

The Company also has several unfunded noncontributory supplemental non-qualified pension plans that provide additional retirement benefits to certain employees.

The Company maintains postretirement benefit plans providing varying levels of medical and life insurance to eligible retirees. The retiree welfare plans are closed for union employees hired on or after January 1, 2006. The plans had previously closed for non-union employees hired on or after January 1, 2002.

The Company's policy is to fund postretirement benefit costs for rate-making purposes. Plan assets are invested in equity and bond mutual funds.

The obligations of the plans are dominated by obligations for active employees. Because the timing of expected benefit payments is so far in the future and the size of the plan assets are small relative to the Company's assets, the investment strategy is to allocate a large portion of assets to equities, which the Company believes will provide the highest return over the long-term period. The fixed income assets are invested in long duration debt securities in order to better match the duration of the plan liability.

The Company periodically conducts an asset liability modeling study to ensure the investment strategy is aligned with the profile of the obligations. The long-term goals are to maximize the plan funded status and minimize contributions and pension expense, while taking into account the potential volatility risks on each of these items.

None of the Company's securities are included in pension or other postretirement benefit plan assets.

The asset allocations for the Company's U.S. pension plan at December 31, 2010 and 2009, by asset category, are as follows:

	Target Allocation	Percentage of Plan Assets At December 31,	
Asset category	2010	2010	2009
Equity securities	70%	70%	71%
Fixed income (including cash)	30%	30%	29%
Total	100%	100%	100%

The investment policy guidelines of the pension plan require that the fixed income portfolio has an overall weighted average credit rating of AA or better by Standard & Poor's and the minimum credit quality for fixed income securities must be BBB- or better. Up to 20% of the portfolio may be invested in collateralized mortgage obligations backed by the United States Government.

The fair values of pension plan assets at December 31, 2010, by asset category, follow:

Asset Category	Target Allocation 2011	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2010
Cash	—	$ 6,467	$ 6,467	—	—	—
Equity securities:						
U.S. large cap	36%	299,548	299,548	—	—	35%
U.S. small cap value	12%	113,356	113,356	—	—	13%
International	22%	190,330	190,330	—	—	22%
Fixed income securities:	30%					30%
U.S. Treasury and government bonds	—	63,469	63,469	—	—	—
Corporate bonds	—	33,118	—	$ 33,118	—	—
Mortgage-backed securities	—	99,478	—	99,478	—	—
Guaranteed annuity contracts	—	55,207	—	9,089	$ 46,118	—
Total	100%	$ 860,973	$ 673,170	$ 141,685	$ 46,118	100%

The following table presents a reconciliation of the beginning and ending balances of the fair value measurements using significant unobservable inputs (Level 3):

	Guaranteed Annuity Contract
Balance, January 1, 2010	$ 47,447
Actual return on assets	2,587
Transfers in(out)	(3,916)
Balance, December 31, 2010	$ 46,118

The fair values of pension plan assets at December 31, 2009, by asset category, follow:

Asset Category	Target Allocation 2010	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2009
Cash	—	$ 10,156	$ 10,156	—	—	—
Equity securities:						
U.S. large cap	36%	250,353	250,353	—	—	36%
U.S.small cap value	12%	88,397	88,397	—	—	13%
International	22%	153,719	153,719	—	—	22%
Fixed income securities:	30%					29%
U.S. Treasury and government bonds	—	23,495	23,495	—	—	—
Corporate Bonds	—	23,624	—	$ 23,624	—	—
Mortgage-backed securities	—	89,736	—	89,736	—	—
Guaranteed annuity contracts	—	56,040	—	8,593	$ 47,447	—
Total	100%	$ 695,520	$ 526,120	$ 121,953	$ 47,447	100%

The following table presents a reconciliation of the beginning and ending balances of the fair value measurements using significant unobservable inputs (Level 3):

	Guaranteed Annuity Contract
Balance, January 1, 2009	$ 42,386
Actual return on assets	9,959
Transfers in(out)	(4,898)
Balance, December 31, 2009	$ 47,447

The Company's other postretirement benefit plans are partially funded. The asset allocations for the Company's other postretirement benefit plans at December 31, 2010 and 2009, by asset category, are as follows:

Asset category	Target Allocation 2010	Percentage of Plan Assets At December 31, 2010	2009
Equity securities	70%	70%	70%
Fixed income (including cash)	30%	30%	30%
Total	100%	100%	100%

The postretirement benefit plan assets are invested in a manner consistent with the pension plan investment policy.

The fair values of postretirement benefit plan assets at December 31, 2010, by asset category, follow:

Asset Category	Target Allocation 2011	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2010
Cash	—	$ 12,500	$ 12,500	—	—	—
Equity securities:						
U.S. large cap	36%	131,775	131,775	—	—	35%
U.S. small cap value	12%	53,898	53,898	—	—	14%
International	22%	77,935	77,935	—	—	21%
Fixed income securities:	30%					30%
U.S. Treasury securities	—	16,025	16,025	—	—	—
Corporate bonds	—	34,746	—	$ 34,746	—	—
Mortgage-backed securities	—	47,524	—	47,524	—	—
Total	100%	$ 374,403	$ 292,133	$ 82,270	—	100%

The fair values of postretirement benefit plan assets at December 31, 2009, by asset category, follow:

Asset Category	Target Allocation 2010	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2009
Cash	—	$ 2,459	$ 2,459	—	—	—
Equity securities:						
U.S. large cap	36%	108,703	108,703	—	—	35%
U.S. small cap value	12%	40,575	40,575	—	—	13%
International	22%	70,111	70,111	—	—	22%
Fixed income securities:	30%					30%
U.S. Treasury securities	—	25,072	25,072	—	—	—
Corporate Bonds	—	31,265	—	$ 31,265	—	—
Mortgage-backed securities	—	33,857	—	33,857	—	—
Total	100%	$ 312,042	$ 246,920	$ 65,122	—	100%

Valuation Techniques Used to Determine Fair Value

Cash—Cash and investments with maturities of three months or less when purchased, including certain short-term fixed-income securities, are considered cash and are included in the recurring fair value measurements hierarchy as Level 1.

Equity securities—With respect to equity securities, the trustees obtain prices from pricing services, whose prices are obtained from direct feeds from market exchanges, which the Company is able to independently corroborate. Equity securities are valued based on quoted prices in active markets and categorized as Level 1.

Fixed-income securities—U.S. Treasury securities and government bonds have been categorized in Level 1 because they trade in highly-liquid and transparent markets that the Company can corroborate. The fair values of corporate bonds, mortgage backed securities and a certain guaranteed annuity contract are based on evaluated prices that reflect observable market information, such as actual trade information of similar securities and have been categorized as Level 2 because the valuations are calculated using models which utilize actively traded market data that the Company can corroborate. Certain other guaranteed annuity contracts are invested in a commingled fund and categorized as Level 3 because the investments are not publicly quoted. The fund administrator values the fund using the net asset value per fund share, derived from the quoted prices in active markets of the underlying securities. Since these valuation inputs are not highly observable, the commingled funds have been categorized as Level 3.

The following table provides a rollforward of the changes in the benefit obligation and plan assets for the most recent two years for all plans combined:

	Pension Benefits		Other Benefits	
	2010	2009	2010	2009
Change in benefit obligation				
Benefit obligation at January 1	$ 1,128,162	$ 1,016,889	$ 548,139	$ 475,742
Service cost	30,675	28,426	14,663	13,172
Interest cost	67,602	62,919	32,149	29,180
Plan participants' contributions	—	—	2,307	2,216
Amendments	3,762	1,600	(8,195)	0
Actuarial (gain) loss	93,399	53,135	23,764	50,357
Gross benefits paid	(38,144)	(34,807)	(23,989)	(24,297)
Federal subsidy	—	—	1,349	1,769
Benefit obligation at December 31	$ 1,285,456	$ 1,128,162	$ 590,187	$ 548,139
Change in Plan Assets				
Fair value of plan assets at January 1	$ 695,520	$ 513,283	$ 312,042	$ 234,501
Actual return on plan assets	105,078	131,252	45,305	57,968
Employer contributions	98,519	85,792	38,738	41,654
Plan participants' contributions	—	—	2,307	2,216
Benefits paid	(38,144)	(34,807)	(23,989)	(24,297)
Fair value of plan assets at December 31	$ 860,973	$ 695,520	$ 374,403	$ 312,042
Funded status at December 31	$ (424,483)	$ (432,642)	$ (215,784)	$ (236,097)
Amounts recognized in the balance sheet consist of:				
Current liability	$ (2,097)	$ (1,632)	$ (33)	$ (52)
Noncurrent liability	(422,386)	(431,010)	(215,751)	(236,045)
Net amount recognized	$ (424,483)	$ (432,642)	$ (215,784)	$ (236,097)

The following table provides the components of the Company's accumulated other comprehensive income and regulatory assets that have not been recognized as components of periodic benefit costs as of December 31.

	Pension Benefits		Other Benefits	
	2010	2009	2010	2009
Net actuarial loss (gain)	$ 302,357	$ 275,188	$ 140,453	$ 145,780
Prior service cost (credit)	6,580	3,140	(18,788)	(12,120)
Transition obligation (asset)	—	—	0	520
Net amount recognized	$ 308,937	$ 278,328	$ 121,665	$ 134,180
Regulatory assets	$ 184,937	$ 166,441	$ 121,665	$ 134,180
Accumulated other comprehensive income	124,000	111,887	—	—
	$ 308,937	$ 278,328	$ 121,665	$ 134,180

At December 31, 2010 and 2009, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with a projected obligation in excess of plan assets were as follows:

	Projected Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2010	2009
Projected benefit obligation	$ 1,285,000	$ 1,128,000
Fair value of plan assets	861,000	696,000

	Accumulated Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2010	2009
Accumulated benefit obligation	$ 1,138,000	$ 993,000
Fair value of plan assets	861,000	696,000

The accumulated postretirement benefit obligation exceeds plan assets for all of the Company's other postretirement benefit plans.

In August 2006, the Pension Protection Act ("PPA") was signed into law in the U.S. The PPA replaces the funding requirements for defined benefit pension plans by requiring that defined benefit plans contribute to 100% of the current liability funding target over seven years. Defined benefit plans with a funding status of less than 80% of the current liability are defined as being "at risk" and additional funding requirements and benefit restrictions may apply. The PPA was effective for the 2008 plan year with short-term phase-in provisions for both the funding target and at-risk determination. The Company's qualified defined benefit plan is currently funded above the at-risk threshold, and therefore the Company expects that the plans will not be subject to the "at risk" funding requirements of the PPA. The Company is proactively monitoring the plan's funded status and projected contributions under the new law to appropriately manage the potential impact on cash requirements.

Minimum funding requirements for the qualified defined benefit pension plan are determined by government regulations and not by accounting pronouncements. The Company plans to contribute amounts at least equal to the minimum required contributions in 2011 to the qualified pension plans. The Company plans to contribute its 2011 other postretirement benefit cost for rate-making purposes.

Information about the expected cash flows for the pension and postretirement benefit plans is as follows:

	Pension Benefits	Other Benefits
2011 expected employer contributions		
To plan trusts	$ 139,600	$ 27,212
To plan participants	1,913	52

The Company made 2011 contributions to fund pension benefits and other benefits of $21,000 and $0, respectively through February 2011.

The following table reflects the net benefits expected to be paid from the plan assets or the Company's assets:

	Pension Benefits	Other Benefits	
	Expected Benefit Payments	Expected Benefit Payments	Expected Federal Subsidy Payments
2011	$ 42,997	$ 25,388	$ 1,617
2012	48,086	27,811	1,801
2013	53,566	30,401	1,978
2014	59,352	33,256	2,134
2015	65,512	36,093	2,292
2016—2020	425,136	218,483	14,143

Because the above amounts are net benefits, plan participants' contributions have been excluded from the expected benefits.

Accounting for pensions and other postretirement benefits requires an extensive use of assumptions about the discount rate, expected return on plan assets, the rate of future compensation increases received by the Company's employees, mortality, turnover and medical costs. Each assumption is reviewed annually. The assumptions are selected to represent the average expected experience over time and may differ in any one year from actual experience due to changes in capital markets and the overall economy. These differences will impact the amount of pension and other postretirement benefit expense that the Company recognizes.

The significant assumptions related to the Company's pension and other postretirement benefit plans are as follows:

	Pension Benefits			Other Benefits		
	2010	2009	2008	2010	2009	2008
Weighted-average assumptions used to determine December 31 benefit obligations						
Discount rate	5.32%	5.93%	6.12%	5.27%	5.82%	6.09%
Rate of compensation increase	3.50%	4.00%	4.00%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 8% in 2011 to 5% in 2017+	graded from 8.5% in 2010 to 5% in 2017+	graded from 8% in 2009 to 5% in 2015+
Weighted-average assumptions used to determine net periodic cost						
Discount rate	5.93%	6.12%	6.27%	5.82%	6.09%	6.20%
Expected return on plan assets	7.90%	7.90%	7.90%	7.60%	7.60%	7.75%
Rate of compensation increase	4.00%	4.00%	4.25%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 8.5% in 2010 to 5% in 2017+	graded from 8% in 2009 to 5% in 2015+	graded from 8% in 2008 to 5% in 2014+

N/A—Assumption is not applicable.

The discount rate assumption was determined for the pension and postretirement benefit plans independently. A yield curve was developed for a universe containing the majority of U.S.-issued Aa-graded corporate bonds, all of which were non callable (or callable with make-whole provisions). For each plan, the discount rate was developed as the level equivalent rate that would produce the same present value as that using spot rates aligned with the projected benefit payments.

The expected long-term rate of return on plan assets is based on historical and projected rates of return for current and planned asset classes in the plans' investment portfolios. Assumed projected rates of return for each of the plans' projected asset classes were selected after analyzing historical experience and future expectations of the returns and volatility of the various asset classes. Based on the target asset allocation for each asset class, the overall expected rate of return for the portfolio was developed, adjusted for historical and expected experience of active portfolio management results compared to the benchmark returns and for the effect of expenses paid from plan assets. The Company's pension expense increases as the expected return on assets decreases.

Assumed health care cost trend rates have a significant effect on the amounts reported for the other postretirement benefit plans. The health care cost trend rate is based on historical rates and expected market conditions. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total of service and interest cost components	$ 7,236	$ 5,933
Effect on other postretirement benefit obligation	$ 79,087	$ 65,679

The following table provides the components of net periodic benefit costs for the years ended December 31:

	2010	2009	2008
Components of net periodic pension benefit cost			
Service cost	$ 30,675	$ 28,426	$ 26,206
Interest cost	67,602	62,919	58,195
Expected return on plan assets	(56,751)	(42,224)	(51,701)
Amortization of:			
Prior service cost (credit)	322	182	181
Actuarial (gain) loss	17,902	23,968	5
Net periodic pension benefit cost	$ 59,750	$ 73,271	$ 32,886
Other changes in plan assets and benefit obligations recognized in other comprehensive income, net of tax			
Amortization of prior service credit (cost)	$ (79)	$ (46)	$ (26)
Current year actuarial (gain) loss	11,836	(9,981)	64,139
Amortization of actuarial gain (loss)	(4,368)	(5,994)	(1)
Total recognized in other comprehensive income	$ 7,389	$ (16,021)	$ 64,112
Total recognized in net periodic benefit cost and comprehensive income	$ 67,139	$ 57,250	$ 96,998
Components of net periodic other postretirement benefit cost			
Service cost	$ 14,663	$ 13,172	$ 12,425
Interest cost	32,149	29,180	28,197
Expected return on plan assets	(24,372)	(18,638)	(23,002)
Amortization of:			
Transition obligation (asset)	173	173	173
Prior service cost (credit)	(1,180)	(1,180)	(1,180)
Actuarial (gain) loss	8,159	9,155	810
Net periodic other postretirement benefit cost	$ 29,592	$ 31,862	$ 17,423

The Company's policy is to recognize curtailments when the total expected future service of plan participants is reduced by greater than 10% due to an event that results in terminations and/or retirements.

The estimated amounts that will be amortized from accumulated other comprehensive income and regulatory assets into net periodic benefit cost in 2011 are as follows:

	Pension Benefits	Other Benefits
Actuarial (gain) loss	$ 18,551	$ 7,365
Prior service cost (credit)	722	(1,924)
Total	$ 19,273	$ 5,441

Savings Plans for Employees

The Company maintains 401(k) savings plans that allow employees to save for retirement on a tax-deferred basis. Employees can make contributions that are invested at their direction in one or more funds. The Company makes matching contributions based on a percentage of an employee's contribution, subject to certain limitations. Due to the Company's discontinuing new entrants into the defined benefit pension plan, on January 1, 2006 the Company began providing an additional 5.25% of base pay defined contribution benefit for union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006. The Company expensed contributions to the plans totaling $8,651 for 2010, $8,082 for 2009, and $7,789 for 2008, respectively. All of the Company's contributions are invested in one or more funds at the direction of the employee.

Note 16: Commitments and Contingencies

OMI/Thames Water Stockton, Inc. ("OMI/TW") is a 50/50 joint venture between a subsidiary of the Company and Operations Management International, Inc. ("OMI"). In February 2003, OMI/TW and the City of Stockton, California (the "City") entered into a 20-year service contract for capital improvements and management services of water, wastewater and storm water utilities. By mutual agreement, OMI/TW and the City of Stockton terminated the contract effective February 29, 2008 (the "Termination Date"). Upon termination, responsibility for management and operation of the system was returned to the City. OMI/TW agreed to provide a limited twelve-month warranty relating to certain components of the facilities that OMI/TW constructed (the "WW39 Plant"), which expired on December 31, 2008. OMI/TW also agreed to correct any latent defects relating to significant deficiencies in the structural components of certain capital improvements discovered prior to November 15, 2009, if any. Additionally OMI/TW committed to pay for certain employee transition costs and assumed financial responsibility for regulatory fines levied through the Termination Date, if any, resulting from OMI/TW's failure to comply with applicable National Pollutant Discharge Elimination System permit requirements and/or incidents traced to design defects in the WW39 Plant. During 2007, the California State Water Resources Control Board (the "Board") issued a notice of violation and a corresponding Settlement Communication related to a discharge into an adjacent river. The City has reached a final settlement agreement with the Board related to the discharge. In connection with the final settlement agreement, OMI/TW has agreed to pay a civil penalty and monitoring costs of $425. The Company had recorded a contingent liability related to the issues above; $1,300 was outstanding at December 31, 2009. The contingency was resolved and the contingent liability was reversed to income during the first quarter of 2010.

The Company is also routinely involved in legal actions incident to the normal conduct of its business. At December 31, 2010, the Company has accrued approximately $3,600 as probable costs and it is reasonably possible that additional losses could range up to $16,400 for these matters. For certain matters, the Company is unable to estimate possible losses. The Company believes that damages or settlements, if any, recovered by plaintiffs in such claims or actions will not have a material adverse effect on the Company's results of operations, financial position or cash flows.

The Company enters into agreements for the provision of services to water and wastewater facilities for the United States military, municipalities and other customers. The Company's military services agreements expire between 2051 and 2060 and have remaining performance commitments as measured by estimated remaining contract revenue of $2,082,000 at December 31, 2010. The military contracts are subject to customary termination provisions held by the U.S. Federal Government prior to the agreed upon contract expiration. The Company's Operations and Maintenance agreements with municipalities and other customers expire between 2011 and 2048 and have remaining performance commitments as measured by estimated remaining contract revenue of $1,197,000 at December 31, 2010. Some of the Company's long-term contracts to operate and maintain a municipality's, federal government's or other party's water or wastewater treatment and delivery facilities include responsibility for certain maintenance for some of those facilities, in exchange for an annual fee. Unless specifically required to perform certain maintenance activities, the maintenance costs are recognized when the maintenance is performed.

Commitments have been made in connection with certain construction programs. The estimated capital expenditures required under legal and binding contractual obligations amounted to $241,350 at December 31, 2010.

The Company's regulated subsidiaries maintain agreements with other water purveyors for the purchase of water to supplement their water supply. The Company's subsidiaries purchased water expense under these types of agreements amounted to approximately $107,121, $98,821 and $95,739 during the years ended December 31, 2010, 2009 and 2008, respectively. The estimated annual commitment related to the minimum quantities of water purchased is expected to approximate $51,600 in 2011, $47,409 in 2012, $46,095 in 2013, $46,077 in 2014, $45,659 in 2015 and $486,489 thereafter.

Note 17: Net Income (Loss) per Common Share

Earnings per share is calculated using the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security. The Company has participating securities related to restricted stock units, granted under the Company's 2007 Omnibus Equity Compensation Plan, that earn dividend equivalents on an equal basis with common shares. In applying the two-class method, undistributed earnings are allocated to both common shares and participating securities. There were 21 participating securities that were not included in the basic net loss per common share calculation at December 31, 2009 because they were anti-dilutive. There were no participating securities for the year ended December 31, 2008. The following is a reconciliation of the Company's net income (loss) and weighted average common shares outstanding for calculating basic net income (loss) per share:

	Years Ended December 31,		
	2010	2009	2008
Basic			
Net income (loss)	$ 267,827	$ (233,083)	$ (562,421)
Less: Distributed earnings to common shareholders (a)	150,724	137,597	64,055
Less: Distributed earnings to participating securities	51	0	0
Undistributed earnings	117,052	(370,680)	(626,476)
Undistributed earnings allocated to common shareholders (b)	117,014	(370,680)	(626,476)
Undistributed earnings allocated to participating securities	38	0	0
Total income (loss) available to common shareholders, basic (a)+(b)	$ 267,738	$ (233,083)	$ (562,421)
Weighted average common shares outstanding, basic	174,833	168,164	159,967
Basic net income (loss) per common share	$ 1.53	$ (1.39)	$ (3.52)

Diluted net income (loss) per common share is based on the weighted average number of common shares outstanding adjusted for the dilutive effect of common stock equivalents related to the restricted stock units, stock options, employee stock purchase plan and restricted stock. The dilutive effect of the common stock equivalents is calculated using the treasury stock method and expected proceeds on vesting of the restricted stock units and restricted stock, exercise of the stock options and purchases under the employee stock purchase plan. The following is a reconciliation of the Company's net income (loss) and weighted average common shares outstanding for calculating diluted net income (loss) per share:

	Years Ended December 31,		
	2010	2009	2008
Diluted			
Total income (loss) available to common shareholders, basic	$ 267,738	$ (233,083)	$ (562,421)
Undistributed earnings allocated to participating securities	38	0	0
Total income (loss) available to common shareholders, diluted	$ 267,776	$ (233,083)	$ (562,421)
Weighted average common shares outstanding, basic	174,833	168,164	159,967
Restricted stock units	264	0	0
Stock options	26	0	0
Employee stock purchase plan	1	0	0
Weighted average common shares outstanding, diluted	175,124	168,164	159,967
Diluted net income (loss) per common share	$ 1.53	$ (1.39)	$ (3.52)

Options to purchase 1,781, 2,265 and 926 shares of the Company's common stock were excluded from the calculation of diluted common shares outstanding because they were anti-dilutive for the years ended December 31, 2010, 2009 and 2008, respectively. Additionally, 258 restricted stock units and 32 shares under the employee stock purchase plan at December 31, 2009 and 119 restricted stock units and 33 shares under the employee stock purchase plan at December 31, 2008 were excluded from the diluted net loss per share calculation because they were anti-dilutive. There were also 0, 459 and 1,134 stock options and 69, 144 and 148 restricted stock units which were excluded from the calculation of diluted common shares outstanding because certain performance conditions were not satisfied as of December 31, 2010, 2009 and 2008, respectively.

Note 18: Fair Values of Financial Instruments

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments.

Current assets and current liabilities: The carrying amount reported in the Consolidated Balance Sheets for current assets and current liabilities, including revolving credit debt due to the short-term maturities and variable interest rates, approximates their fair values.

Preferred stock with mandatory redemption requirements and long-term debt: The fair values of preferred stock with mandatory redemption requirements and long-term debt are determined by a valuation model which is based on a conventional discounted cash flow methodology and utilizes assumptions of current market rates. As a majority of the Company's debts do not trade in active markets, the Company calculated a base yield curve using a risk-free rate (a U.S. Treasury securities yield curve) plus a credit spread that is based on the following two factors: an average of the Company's own publicly-traded debt securities and the current market rates for U.S. Utility BBB+ debt securities. The Company used these yield curve assumptions to derive a base yield and then adjusted the base yield for specific features of the debt securities of call features, coupon tax treatment and collateral.

The carrying amounts (including fair value adjustments previously recognized in acquisition purchase accounting) and fair values of the financial instruments at December 31 are as follows:

2010	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 23,939	$ 26,759
Long-term debt (excluding capital lease obligations)	5,449,287	5,867,654

2009	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 24,164	$ 26,257
Long-term debt (excluding capital lease obligations)	5,336,351	5,633,384

Fair Value Measurements

To increase consistency and comparability in fair value measurements, FASB guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels as follows:

- Level 1—quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access as of the reporting date. Financial assets and liabilities utilizing Level 1 inputs include active exchange-traded equity securities, exchange-based derivatives, mutual funds and money market funds.
- Level 2—inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data. Financial assets and liabilities utilizing Level 2 inputs include fixed income securities, non-exchange-based derivatives, commingled investment funds not subject to purchase and sale restrictions and fair-value hedges.
- Level 3—unobservable inputs, such as internally-developed pricing models for the asset or liability due to little or no market activity for the asset or liability. Financial assets and liabilities utilizing Level 3 inputs include infrequently-traded non-exchange-based derivatives and commingled investment funds subject to purchase and sale restrictions.

Recurring Fair Value Measurements

The following table presents assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of December 31, 2010 and 2009, respectively:

	At Fair Value as of December 31, 2010			
Recurring Fair Value Measures	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets:				
Restricted funds	$ 120,784	—	—	$ 120,784
Rabbi trust investments	—	$ 1,552	—	1,552
Deposits	1,629	—	—	1,629
Total assets	122,413	1,552	—	123,965
Liabilities:				
Deferred compensation obligation	—	9,183	—	9,183
Mark-to-market derivative liability	—	898	—	898
Total liabilities	—	10,081	—	10,081
Total net assets (liabilities)	$ 122,413	$ (8,529)	—	$ 113,884

	At Fair Value as of December 31, 2009			
Recurring Fair Value Measures	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets:				
Restricted funds	$ 61,232	—	—	$ 61,232
Rabbi trust investments	—	$ 2,551	—	2,551
Deposits	11,612	—	—	11,612
Total assets	72,844	2,551	—	75,395
Liabilities:				
Deferred compensation obligation	—	8,881	—	8,881
Total liabilities	—	8,881	—	8,881
Total net assets (liabilities)	$ 72,844	$ (6,330)	—	$ 66,514

Restricted funds—The Company's restricted funds primarily represent proceeds received from financings for the construction and capital improvement of facilities and from customers for future services under operations and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within twelve months subsequent to year-end are classified as current.

Rabbi trust investments—The Company's rabbi trust investments consist primarily of fixed income investments from which supplemental executive retirement plan benefits are paid. The Company includes these assets in other long-term assets.

Deposits—Deposits includes escrow funds and certain other deposits held in trust. The Company includes cash deposits in other current assets. The December 31, 2009 balance included $10,170 for an escrow account related to an agreement the Company's New Jersey regulated subsidiary had entered into with the City of Trenton, New Jersey to purchase certain assets of Trenton's water system located in four surrounding townships. The purchase agreement was contested in litigation with a group of Trenton residents, and ultimately put to a voter referendum. The result of the referendum was unfavorable to the Company, and as a result, the agreement to purchase the assets was terminated in June 2010. The escrow deposit, plus accrued interest, was returned to the Company on June 30, 2010.

Deferred compensation obligations—The Company's deferred compensation plans allow participants to defer certain cash compensation into notional investment accounts. The Company includes such plans in other long-term liabilities. The value of the Company's deferred compensation obligations is based on the market value of the participants' notional investment accounts. The notional investments are comprised primarily of mutual funds, which are based on observable market prices.

Mark-to-market derivative liability—The Company utilizes fixed-to-floating interest-rate swaps, typically designated as fair-value hedges, to achieve a targeted level of variable-rate debt as a percentage of total debt. The Company uses a calculation of future cash inflows and estimated future outflows, which are discounted, to determine the current fair value. Additional inputs to the present value calculation include the contract terms, counterparty credit risk, interest rates and market volatility.

See Note 15 for the Company's fair value of qualified pension and postretirement welfare plans' assets.

Non-recurring Fair Value Measurements

As discussed in Note 8, the Company recognized goodwill impairment charges of $0, $450,000 and $750,000 for the years ended December 31, 2010, 2009 and 2008, respectively. The Company's goodwill valuation model includes significant unobservable inputs and falls within level 3 of the fair value hierarchy.

Note 19: Operating Leases

The Company has entered into operating leases involving certain facilities and equipment. Rental expenses under operating leases were $38,516 for 2010, $37,004 for 2009 and $36,200 for 2008. The operating leases for facilities will expire over the next 20 years and the operating leases for equipment will expire over the next five years. Certain operating leases have renewal options ranging from one to five years.

At December 31, 2010, the minimum annual future rental commitment under operating leases that have initial or remaining non-cancelable lease terms in excess of one year are $25,706 in 2011, $24,419 in 2012, $17,225 in 2013, $14,104 in 2014, $10,805 in 2015 and $105,539 thereafter.

The Company has a series of agreements with various public entities (the "Partners") to establish certain joint ventures, commonly referred to as "public-private partnerships." Under the public-private partnerships, the Company constructed utility plant, financed by the Company, and the Partners constructed utility plant (connected to the Company's property), financed by the Partners. The Company agreed to transfer and convey some of its real and personal property to the Partners in exchange for an equal principal amount of Industrial Development Bonds ("IDBs"), issued by the Partners under a state Industrial Development Bond and Commercial Development Act. The Company leased back the total facilities, including portions funded by both the Company and the Partners, under leases for a period of 40 years.

The leases related to the portion of the facilities funded by the Company have required payments from the Company to the Partners that approximate the payments required by the terms of the IDBs from the Partners to the Company (as the holder of the IDBs). As the ownership of the portion of the facilities constructed by the Company will revert back to the Company at the end of the lease, the Company has recorded these as capital leases. The lease obligation and the receivable for the principal amount of the IDBs are presented by the Company on a net basis. The carrying value of the facilities funded by the Company recognized as a capital lease asset was $159,707 and $160,259 at December 31, 2010 and 2009, respectively, which is presented within utility plant. The future payments under the lease obligations are equal to and offset by the payments receivable under the IDBs.

At December 31, 2010, the minimum annual future rental commitment under the operating leases for the portion of the facilities funded by the Partners that have initial or remaining non-cancelable lease terms in excess of one year included in the proceeding minimum annual rental commitments are $3,551 in 2011, $3,616 in 2012, $3,615 in 2013 through 2015, and $83,361 thereafter.

Note 20: Related Party Transactions

One of the Company's Directors was employed by an electrical utility that supplies electricity and electrical services to the Company's subsidiaries in Ohio, Pennsylvania, and New Jersey. The Company purchased, from various subsidiaries of this electrical utility, approximately $8,558 and $7,183 of such services in 2009 and 2008, respectively. The Director retired from that electrical utility effective March 31, 2010. The Company purchased, from various subsidiaries of this electrical utility, approximately $3,225 of such services in the first quarter of 2010.

Note 21: Segment Information

The Company has two operating segments referred to as the Regulated Businesses and Market-Based Operations segments. The Company's chief operating decision maker regularly reviews the operating results of the Regulated Businesses and Market-Based Operations segments to assess segment performance and allocate resources. The evaluation of segment performance and the allocation of resources are based on several measures. The measure that is most consistent with that used by management is adjusted earnings before interest and income taxes from continuing operations ("Adjusted EBIT").

The Regulated Businesses segment includes the Company's 23 utility subsidiaries that provide water and wastewater services to customers in 20 U.S. states. With the exception of one company, each of these public utility subsidiaries is subject to regulation by public utility commissions and local governments. In addition to providing similar products and services and being subject to the public utility regulatory environment, each of the regulated subsidiaries has similar economic characteristics, production processes, types and classes of customers and water distribution or wastewater collection processes. Each of these companies is also subject to both federal and state regulation regarding the quality of water distributed and the discharge of wastewater residuals.

The Market-Based Operations segment is comprised of market based businesses that provide a broad range of market based water and wastewater services and products including homeowner water and sewer line maintenance services, water and wastewater facility operations and maintenance services, granular carbon technologies and products for cleansing water and wastewater, wastewater residuals management services and water and wastewater facility engineering services.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see Note 2). The Regulated Businesses and Market-Based Operations segment information includes intercompany costs that are allocated by American Water Works Service Company, Inc. and intercompany interest that is charged by AWCC, which are eliminated to reconcile to the consolidated results of operations. Inter-segment revenues, which are primarily recorded at cost plus mark-up that approximates current market prices, include carbon regeneration services and leased office space, furniture and equipment provided by the Company's market based subsidiaries to its regulated subsidiaries. Other includes corporate costs that are not allocated to the Company's subsidiaries, eliminations of inter-segment transactions, fair value adjustments and associated income and deductions related to the Acquisitions that have not been allocated to the segments for evaluation of segment performance and allocation of resource purposes. The adjustments related to the Acquisitions are reported in Other, as they are excluded from segment performance measures evaluated by management. The following table includes the Company's summarized segment information:

	As of or for the Year Ended December 31, 2010			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,424,186	$ 311,835	$ (25,344)	$ 2,710,677
Depreciation and amortization	327,327	7,431	19,892	354,650
Total operating expenses, net	1,707,060	287,924	(32,398)	1,962,586
Adjusted EBIT(1)	721,213	26,983		
Total assets	12,275,280	241,763	1,562,730	14,079,773
Capital expenditures	758,150	7,486	0	765,636

	As of or for the Year Ended December 31, 2009			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,207,290	$ 257,710	$ (24,297)	$ 2,440,703
Depreciation and amortization	313,400	5,871	15,907	335,178
Impairment charge	0	0	450,000	450,000
Total operating expenses, net	1,617,815	238,072	411,207	2,267,094
Adjusted EBIT(1)	591,606	21,264		
Total assets	11,659,525	247,594	1,545,532	13,452,651
Capital expenditures	779,428	5,837	0	785,265

	As of or for the Year Ended December 31, 2008			
	Regulated Businesses	Market-Based Operations	Other	Consolidated
Net operating revenues	$ 2,082,740	$ 272,186	$ (17,998)	$ 2,336,928
Depreciation and amortization	296,318	5,858	10,600	312,776
Impairment charge	0	0	750,000	750,000
Total operating expenses, net	1,554,731	248,425	720,668	2,523,824
Adjusted EBIT(1)	531,774	26,307		
Total assets	10,941,133	244,891	2,045,794	13,231,818
Capital expenditures	1,005,360	3,446	0	1,008,806

(1) Management evaluates the performance of its segments and allocates resources based on several factors, of which the primary measure is Adjusted EBIT. Adjusted EBIT does not represent cash flows for periods presented and should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a source of liquidity. Adjusted EBIT as defined by the Company may not be comparable with Adjusted EBIT as defined by other companies.

The following table reconciles Adjusted EBIT, as defined by the Company, to income (loss) before income taxes:

	For the Year Ended December 31, 2010		
	Regulated Businesses	Markert-Based Operations	Total Segments
Adjusted EBIT	$ 721,213	$ 26,983	$ 748,196
Add:			
Allowance for other funds used during construction	10,003	—	10,003
Allowance for borrowed funds used during construction	6,284	—	6,284
Less:			
Interest, net	(249,045)	1,576	(247,469)
Amortization of debt expense	(4,001)	0	(4,001)
Segments income before income taxes	$ 484,454	$ 28,559	513,013
Interest, net			(67,574)
Other			3,997
Income before income taxes			$ 449,436

	For the Year Ended December 31, 2009		
	Regulated Businesses	Market-Based Operations	Total Segments
Adjusted EBIT	$ 591,606	$ 21,264	$ 612,870
Add:			
Allowance for other funds used during construction	11,486	—	11,486
Allowance for borrowed funds used during construction	7,224	—	7,224
Less:			
Interest, net	(231,858)	3,005	(228,853)
Amortization of debt expense	(6,089)	0	(6,089)
Segments income before income taxes	$ 372,369	$ 24,269	396,638
Impairment charge			(450,000)
Interest, net			(67,692)
Other			9,389
Loss before income taxes			$ (111,665)

	For the Year Ended December 31, 2008		
	Regulated Businesses	Market-Based Operations	Total Segments
Adjusted EBIT	$ 531,774	$ 26,307	$ 558,081
Add:			
Allowance for other funds used during construction	14,497	—	14,497
Allowance for borrowed funds used during construction	8,171	—	8,171
Less:			
Interest, net	(227,384)	2,958	(224,426)
Amortization of debt expense	(5,346)	0	(5,346)
Segments income before income taxes	$ 321,712	$ 29,265	350,977
Impairment charge			(750,000)
Interest, net			(60,729)
Other			9,158
Loss before income taxes			$ (450,594)

Note 22: Unaudited Quarterly Data

The following table sets forth certain supplemental unaudited consolidated quarterly financial data for each of the four quarters in the period ended December 31, 2010 and 2009, respectively. The operating results for any quarter are not indicative of results that may be expected for a full year or any future periods.

2010	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in thousands, except per share data)			
Operating revenues	$ 588,053	$ 671,223	$ 786,946	$ 664,455
Operating income (loss)	126,065	195,983	273,955	152,088
Net income (loss)	30,808	72,751	124,114	40,154
Basic and diluted income (loss) per common share	$ 0.18	$ 0.42	$ 0.71	$ 0.23

2009	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in thousands, except per share data)			
Operating revenues	$ 550,170	$ 612,740	$ 679,956	$ 597,837
Operating income (loss)	(335,370)	157,192	214,406	137,381
Net income (loss)	(413,079)	51,989	91,636	36,371
Basic and diluted income (loss) per common share	$ (2.58)	$ 0.32	$ 0.52	$ 0.21

Amounts may not sum due to rounding; per share amounts may not sum due to changes in shares outstanding during the year.

Operating income (loss) includes impairment loss of $450,000 in the first quarter of 2009.

American Water Works Company, Inc.

Audited Consolidated Financial Statement

Excerpted from SEC Form 10-K Annual Report
Filed on 03/01/2010

Filed Period 12/31/2009

AMERICAN WATER

Annual Report Available At : http://ir.amwater.com/phoenix.zhtml?c=215126&p=irol-sec

AUDITED CONSOLIDATED FINANCIAL STATEMENTS – 2009

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2009 and 2008

Consolidated Statements of Operations and Comprehensive Income (Loss) for the years ended December 31, 2009, 2008 and 2007

Consolidated Statements of Cash Flows for the years ended December 31, 2009, 2008 and 2007

Consolidated Statements of Changes in Common Stockholders' Equity for the years ended December 31, 2009, 2008 and 2007

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
American Water Works Company, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of cash flows, of changes in common stockholders' equity, and of comprehensive income (loss) present fairly, in all material respects, the financial position of American Water Works Company, Inc. and Subsidiary Companies at December 31, 2009 and December 31, 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our audits (which was an integrated audit in 2009). We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
March 1, 2010

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Balance Sheets
(In thousands, except per share data)

	December 31,	
	2009	2008
ASSETS		
Property, plant and equipment		
Utility plant—at original cost, net of accumulated depreciation of $3,168,078 in 2009 and $2,969,869 in 2008	$10,523,844	$ 9,991,783
Nonutility property, net of accumulated depreciation of $117,245 in 2009 and $101,287 in 2008	153,549	132,145
Total property, plant and equipment	10,677,393	10,123,928
Current assets		
Cash and cash equivalents	22,256	9,542
Restricted funds	41,020	454
Utility customer accounts receivable	149,417	149,198
Allowance for uncollectible accounts	(19,035)	(18,644)
Unbilled utility revenues	130,262	134,204
Non-regulated trade and other receivables, net	75,086	68,877
State income taxes receivable	17,920	—
Materials and supplies	29,521	28,948
Other	52,680	45,096
Total current assets	499,127	417,675
Regulatory and other long-term assets		
Regulatory assets	952,020	919,654
Restricted funds	20,212	10,599
Goodwill	1,250,381	1,699,517
Other	53,518	60,445
Total regulatory and other long-term assets	2,276,131	2,690,215
TOTAL ASSETS	$13,452,651	$13,231,818

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Balance Sheets—(Continued)
(In thousands, except per share data)

	December 31, 2009	December 31, 2008
CAPITALIZATION AND LIABILITIES		
Capitalization		
Common stock ($.01 par value, 500,000 shares authorized, 174,630 shares outstanding in 2009 and 160,000 in 2008)	$ 1,746	$ 1,600
Paid-in capital	6,140,077	5,888,253
Accumulated deficit	(2,076,287)	(1,705,594)
Accumulated other comprehensive loss	(64,677)	(82,251)
Treasury stock	—	(7)
Common stockholders' equity	4,000,859	4,102,001
Preferred stock without mandatory redemption requirements	4,557	4,557
Total stockholders' equity	4,005,416	4,106,558
Long-term debt		
Long-term debt	5,288,180	4,624,063
Redeemable preferred stock at redemption value	23,946	24,150
Total capitalization	9,317,542	8,754,771
Current liabilities		
Short-term debt	119,497	479,010
Current portion of long-term debt	54,068	175,822
Accounts payable	138,609	149,795
Taxes accrued, including income taxes of $1,777 in 2009 and $6,061 in 2008	45,552	52,488
Interest accrued	60,128	53,629
Other	189,538	194,016
Total current liabilities	607,392	1,104,760
Regulatory and other long-term liabilities		
Advances for construction	633,509	622,227
Deferred income taxes	851,677	705,587
Deferred investment tax credits	32,590	34,023
Regulatory liabilities	322,281	307,324
Accrued pension expense	431,010	502,062
Accrued postretirement benefit expense	236,045	241,193
Other	47,325	48,456
Total regulatory and other long-term liabilities	2,554,437	2,460,872
Contributions in aid of construction	973,280	911,415
Commitments and contingencies (See Note 16)	—	—
TOTAL CAPITALIZATION AND LIABILITIES	$13,452,651	$13,231,818

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Statements of Operations
(In thousands, except per share data)

	Years Ended December 31,		
	2009	2008	2007
Operating revenues	$2,440,703	$2,336,928	$2,214,215
Operating expenses			
Operation and maintenance	1,324,355	1,303,798	1,246,479
Depreciation and amortization	294,240	271,261	267,335
General taxes	199,262	199,139	183,253
Gain on sales of assets	(763)	(374)	(7,326)
Impairment charge	450,000	750,000	509,345
Total operating expenses, net	2,267,094	2,523,824	2,199,086
Operating income (loss)	173,609	(186,896)	15,129
Other income (deductions)			
Interest, net	(296,545)	(285,155)	(283,165)
Allowance for other funds used during construction	11,486	14,497	7,759
Allowance for borrowed funds used during construction	7,224	8,171	3,449
Amortization of debt expense	(6,647)	(5,895)	(4,867)
Other, net	(792)	4,684	6,176
Total other income (deductions)	(285,274)	(263,698)	(270,648)
Loss from continuing operations before income taxes	(111,665)	(450,594)	(255,519)
Provision for income taxes	121,418	111,827	86,756
Loss from continuing operations	(233,083)	(562,421)	(342,275)
Loss from discontinued operations, net of tax	—	—	(551)
Net loss	$ (233,083)	$ (562,421)	$ (342,826)
Basic earnings per common share:			
Loss from continuing operations	$ (1.39)	$ (3.52)	$ (2.14)
Loss from discontinued operations, net of tax	$ —	$ —	$ (0.00)
Net loss	$ (1.39)	$ (3.52)	$ (2.14)
Diluted earnings per common share:			
Loss from continuing operations	$ (1.39)	$ (3.52)	$ (2.14)
Loss from discontinued operations, net of tax	$ —	$ —	$ (0.00)
Net loss	$ (1.39)	$ (3.52)	$ (2.14)
Average common shares outstanding during the period:			
Basic	168,164	159,967	160,000
Diluted	168,164	159,967	160,000
Dividends per common share	$ 0.82	$ 0.40	$ —

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Statements of Cash Flows
(In thousands, except per share data)

	Years Ended December 31,		
	2009	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	$(233,083)	$ (562,421)	$ (342,826)
Adjustments			
Depreciation and amortization	294,240	271,261	267,335
Impairment charge	450,000	750,000	509,345
Amortization of removal costs net of salvage	40,919	41,515	38,442
Provision for deferred income taxes	140,821	95,643	41,918
Amortization of deferred investment tax credits	(1,433)	(1,338)	(1,510)
Provision for losses on utility accounts receivable	21,781	17,267	17,553
Allowance for other funds used during construction	(11,486)	(14,497)	(7,759)
Gain on sale of assets	(763)	(374)	(7,326)
Gain on early extinguishment of debt	—	—	(13,113)
Pension and non-pension post retirement benefits	106,901	51,571	49,693
Other, net	(24,154)	3,072	(13,565)
Changes in assets and liabilities			
Receivables and unbilled utility revenues	(18,751)	(20,702)	(35,097)
Taxes receivable, including income taxes	(17,920)	23,111	(23,111)
Other current assets	(6,737)	(11,194)	(1,171)
Pension and non-pension post retirement benefit contributions	(127,446)	(105,053)	(81,245)
Accounts payable	52	2,978	6,860
Taxes accrued, including income taxes	(13,321)	13,460	42,430
Interest accrued	6,499	2,790	16,092
Other current liabilities	(9,963)	(4,920)	10,767
Net cash provided by operating activities	596,156	552,169	473,712
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures	(785,265)	(1,008,806)	(750,810)
Acquisitions	(18,144)	(12,512)	(15,877)
Proceeds from sale of assets and securities	1,237	12,604	16,346
Proceeds from sale of discontinued operations	—	—	9,660
Removal costs from property, plant and equipment retirements, net	(29,900)	(24,793)	(9,852)
Net funds released	129,711	2,457	5,829
Other	(1,250)	(2,617)	(1,874)
Net cash used in investing activities	(703,611)	(1,033,667)	(746,578)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from long-term debt	542,926	279,941	3,869,109
Repayment of long-term debt	(178,131)	(241,500)	(2,350,725)
Proceeds from issuance of common stock (net of expenses of $7,824)	242,301	—	—
Net (repayments) borrowings under short-term debt agreements	(352,005)	258,684	(541,623)
Proceeds from employee stock plan issuances	2,089	836	—
Advances and contributions for construction, net of refunds of $27,481 in 2009, $57,580 in 2008 and $36,963 in 2007	21,211	3,078	35,846
Change in cash overdraft position	(7,508)	(188)	42,198
Capital contributions	—	245,000	967,092
Debt issuance costs	(13,165)	(4,008)	(14,916)
Redemption of preferred stocks	(218)	(229)	(1,750,388)
Dividends paid	(137,331)	(64,055)	—
Net cash provided by financing activities	120,169	477,559	256,593
Net increase (decrease) in cash and cash equivalents	12,714	(3,939)	(16,273)
Cash and cash equivalents at beginning of period	9,542	13,481	29,754
Cash and cash equivalents at end of period	$ 22,256	$ 9,542	$ 13,481
Cash paid during the year for:			
Interest, net of capitalized amount	$ 303,958	$ 294,508	$ 295,707
Income taxes, net of refunds of $2,754 in 2009, $40,400 in 2008 and $16,111 in 2007	$ 11,205	$ (22,161)	$ 17,823
Non-cash investing activity			
Capital expenditures acquired on account but unpaid as of year-end	$ 59,219	$ 72,657	$ 94,930
Non-cash financing activity			
Advances and contributions	$ 77,094	$ 83,041	$ 101,226
Long-term debt (See Note 11)	$ 179,931	$ —	$ —
Capital contribution (See Note 11)	$ —	$ —	$ 100,000

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Statements of Changes in Stockholders' Equity
(In thousands, except per share data)

	Common Stock					Treasury Stock			
	Shares	Par Value	Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Shares	At Cost	Preferred Stock of Subsidiary Companies Without Mandatory Redemption Requirements	Total Stockholders' Equity
Balance at December 31, 2006	160,000	$1,600	$4,570,855	$ (736,292)	$ (18,766)	—	$ —	$ 4,568	$ 3,821,965
Net loss	—	—	—	(342,826)	—	—	—	—	(342,826)
Equity investment by RWE	—	—	1,067,092	—	—	—	—	—	1,067,092
Other comprehensive income (loss), net of tax of $660	—	—	—	—	383	—	—	—	383
Balance at December 31, 2007	160,000	$1,600	$5,637,947	$ (1,079,118)	$ (18,383)	—	$ —	$ 4,568	$ 4,546,614
Net loss	—	—	—	(562,421)	—	—	—	—	(562,421)
Equity investment by RWE	—	—	245,000	—	—	—	—	—	245,000
Contribution of common stock by RWE	—	—	1,933	—	—	(90)	(1,933)	—	—
Stock-based compensation activity	—	—	3,373	—	—	90	1,926	—	5,299
Subsidiary preferred stock redemption	—	—	—	—	—	—	—	(11)	(11)
Other comprehensive income (loss), net of tax of ($40,990)	—	—	—	—	(63,868)	—	—	—	(63,868)
Dividends	—	—	—	(64,055)	—	—	—	—	(64,055)
Balance at December 31, 2008	160,000	$1,600	$5,888,253	$ (1,705,594)	$ (82,251)	—	$ (7)	$ 4,557	$ 4,106,558
Net loss	—	—	—	(233,083)	—	—	—	—	(233,083)
Common stock offering, net of expenses of $7,824	14,500	145	242,156	—	—	—	—	—	242,301
Stock-based compensation activity	130	1	9,668	(279)	—	—	7	—	9,397
Other comprehensive income (loss), net of tax of $10,242	—	—	—	—	17,574	—	—	—	17,574
Dividends	—	—	—	(137,331)	—	—	—	—	(137,331)
Balance at December 31, 2009	174,630	$1,746	$6,140,077	$ (2,076,287)	$ (64,677)	—	$ —	$ 4,557	$ 4,005,416

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies
Consolidated Statements of Comprehensive Income (Loss)
(In thousands, except per share data)

	Years Ended December 31		
	2009	2008	2007
Net loss	$(233,083)	$(562,421)	$(342,826)
Change in employee benefit plan funded status, net of tax of $6,381, ($41,007) and $591, respectively	9,981	(64,139)	924
Pension plan amortized to periodic benefit cost:			
Prior service cost, net of tax of $29, $17 and $23, respectively	46	26	36
Actuarial loss, net of tax of $3,832, $0 and $46, respectively	5,994	1	72
Foreign currency translation adjustment	1,553	244	(649)
Total comprehensive loss	$(215,509)	$(626,289)	$(342,443)

The accompanying notes are an integral part of these consolidated financial statements.

American Water Works Company, Inc. and Subsidiary Companies
Notes to Consolidated Financial Statements
(In thousands, except per share data)

Note 1: Organization and Operation

American Water Works Company, Inc. ("AWW") and its subsidiaries (collectively referred to herein as the "Company") is the holding company for regulated and non-regulated subsidiaries throughout the United States of America and two Canadian provinces. The regulated subsidiaries provide water and wastewater services and, as public utilities, function under rules and regulations prescribed by state regulators. These regulated subsidiaries have similar long-term economic characteristics and are operationally segregated into the 20 U.S. states in which the Company operates regulated utilities. The non-regulated subsidiaries include various lines of business including Homeowner Services, which provides water and sewer line protection plans for homeowners; the Operations and Maintenance contracts group, which conducts operation and maintenance of water and wastewater facilities for municipalities and the U.S. Military, among others; and Carbon Regeneration, which sells granular activated carbon technologies to help remove contaminants and improve the quality of drinking water.

Note 2: Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of AWW and its subsidiaries. Intercompany balances and transactions between subsidiaries have been eliminated. The Company uses the equity method to report its investments in two joint venture investments in each of which the Company holds a 50% voting interest and cannot exercise control over the operations and policies of the investments. Under the equity method, the Company records its interests as an investment and its percentage share of earnings as earnings or losses of investee.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The Company considers benefit plan assumptions; the carrying values of goodwill and other long-lived assets, including regulatory assets; revenue recognition; and accounting for income taxes to be its critical accounting estimates. The Company's significant estimates that are particularly sensitive to change in the near term are amounts reported for pension and other postemployment benefits, contingency-related obligations and goodwill.

Regulation

The Company's regulated utilities are subject to regulation by the public utility commissions and the local governments of the states in which they operate (the "Regulators"). These Regulators have allowed recovery of costs and credits which the Company has recorded as regulatory assets and liabilities. Accounting for future recovery of costs and credits as regulatory assets and liabilities is in accordance with authoritative guidance applicable to those companies whose rates are established by or are subject to approval by an independent third-party regulator. Regulated utilities defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate making process in a period different from the period in which they would have been reflected in operations by an non-regulated company. These deferred regulatory assets and liabilities are then reflected in the statement of operations in the period in which the costs and credits are reflected in the rates charged for service. (See Note 7)

Property, Plant and Equipment

Property, plant and equipment consist primarily of utility plant. Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. The costs incurred to acquire and internally develop computer software for internal use are capitalized as a unit of property. The carrying value of these costs amounted to $47,279 and $35,971 at December 31, 2009 and 2008, respectively. The cost of repairs; maintenance, including planned major maintenance activities; and minor replacements of property is charged to maintenance expense as incurred.

When units of property are replaced, retired or abandoned, the recorded value thereof is credited to the asset account and charged to accumulated depreciation. To the extent the Company recovers cost of removal or other retirement costs through rates after the retirement costs are incurred, a regulatory asset is recorded. In some cases, the Company recovers retirement costs through rates during the life of the associated asset and before the costs are incurred. These amounts result in a regulatory liability being reported based on the amounts previously recovered through customer rates, until the costs to retire those assets are incurred.

The cost of property, plant and equipment is depreciated using the straight-line average remaining life method.

Nonutility property consists primarily of buildings and equipment utilized by the Company for internal operations. This property is stated at cost, net of accumulated depreciation calculated using the straight-line method over the estimated useful lives of the assets, ranging from three to fifty years.

Cash and Cash Equivalents

Substantially all cash is invested in interest-bearing accounts. All highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

The Company had book overdrafts for certain of its disbursement accounts of $34,502 and $42,010 at December 31, 2009 and 2008, respectively. A book overdraft represents transactions that have not cleared the bank accounts at the end of the period. The Company transfers cash on an as-needed basis to fund these items as they clear the bank. The balance of the book overdraft is reported as short-term debt and the change in the book overdraft balance is reported as cash flows from financing activities.

Restricted Funds

Restricted funds primarily represent proceeds received from financings for the construction and capital improvement of facilities and from customers for future services under operation and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within 12 months subsequent to year-end are classified as current.

Utility Customer Accounts Receivable

Regulated utility customer accounts receivable represent amounts billed to water and wastewater customers on a cycle basis. Credit is extended based on the guidelines of the applicable Regulators and generally, collateral is not required.

Allowance for Uncollectible Accounts

Allowances for uncollectible accounts are maintained for estimated probable losses resulting from the Company’s inability to collect receivables from customers. Accounts that are outstanding longer than the payment terms are considered past due. A number of factors are considered in determining the allowance for

uncollectible accounts, including the length of time receivables are past due and previous loss history. The Company writes off accounts when they become uncollectible. (See Note 5)

Non-regulated Trade and Other Receivables, Net

Non-regulated trade and other receivables, net consists of non-regulated trade accounts receivable and non-regulated unbilled revenues, net of a reserve for doubtful accounts, and non-utility customer receivables of the regulated subsidiaries. In determining the reserve for uncollectible non-regulated accounts, the Company considers the length of time the trade accounts receivable are past due and the customers' current ability to pay their obligations. Unbilled receivables are accrued when service has been provided but has not been billed to customers. (See Note 6)

Materials and Supplies

Materials and supplies are stated at the lower of cost or net realizable value. Cost is determined using the average cost method.

Goodwill

The Company considers the carrying value of goodwill to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to value goodwill to be appropriate. However, if experience differs from the assumptions and considerations used in its analysis, the resulting change could have a material adverse impact on the consolidated financial statements.

Goodwill is primarily associated with the acquisitions of American Water Works Company, Inc. in 2003 and E'town Corporation in 2001 (the "Acquisitions") and has been assigned to reporting units based on the fair values at the date of the Acquisitions. The regulated utility subsidiaries have been aggregated and deemed a single reporting unit as they have similar economic characteristics. In the non-regulated segment, the business is organized into seven reporting units for its non-regulated services. Goodwill is reviewed annually, or more frequently if changes in circumstances indicate the carrying value may not be recoverable. Annual impairment reviews are performed in the fourth quarter of the calendar year, in conjunction with the timing of the completion of the Company's annual strategic business plan.

For each of the years ended December 31, 2009, 2008 and 2007, the Company determined that its goodwill was impaired and recorded impairments of $450,000, $750,000, and $509,345, respectively. (See Note 8)

Long-Lived Assets

The Company considers the carrying value of long-lived assets to be one of its critical accounting estimates. The Company believes the assumptions and other considerations used to evaluate the carrying value of long-lived assets to be appropriate. However, if actual experience differs from the assumptions and considerations used in its estimates, the resulting change could have a material adverse impact on the consolidated financial statements.

Long-lived assets, other than goodwill, include land, buildings, equipment and long-term investments. Long-lived assets, other than investments and land, are depreciated over their estimated useful lives, and are reviewed for impairment whenever changes in circumstances indicate the carrying value of the asset may not be recoverable. Such circumstances would include items such as a significant decrease in the market value of a long-lived asset, a significant adverse change in the manner the asset is being used or planned to be used or in its physical condition, or a history of operating or cash flow losses associated with the use of the asset. In addition, changes in the expected useful life of these long-lived assets may also be an impairment indicator. When such events or changes occur, the Company estimates the fair value of the asset from future cash flows expected to result from the use and, if applicable, the eventual disposition of the assets and compares that to the carrying value of the asset. If the carrying value is greater than the fair value, an impairment loss is recorded.

The key variables that must be estimated include assumptions regarding sales volume, rates, operating costs, labor and other benefit costs, capital additions, assumed discount rates and other economic factors. These variables require significant management judgment and include inherent uncertainties since they are forecasting future events. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

The long-lived assets of the regulated utility subsidiaries are grouped on a separate entity basis for impairment testing as they are integrated state-wide operations that do not have the option to curtail service and generally have uniform tariffs. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

The Company holds other investments including investments in privately held companies and investments in joint ventures accounted for using the equity method. The Company's investments in privately held companies and joint ventures are classified as other long-term assets.

The fair values of long-term investments are dependent on the financial performance and solvency of the entities in which the Company invests, as well as volatility inherent in the external markets. If such assets are considered impaired, an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value.

Advances and Contributions in Aid of Construction

Regulated utility subsidiaries may receive advances and contributions from customers, home builders and real estate developers to fund construction necessary to extend service to new areas. Advances for construction are refundable for limited periods of time as new customers begin to receive service or other contractual obligations are fulfilled. Included in other current liabilities at December 31, 2009 and 2008 in the accompanying balance sheets are estimated refunds of $34,207 and $32,305, respectively. Those amounts represent expected refunds during the next 12-month period. Advances which are no longer refundable are reclassified to contributions in aid of construction. Contributions in aid of construction are permanent collections of plant assets or cash for a particular construction project. For ratemaking purposes, the amount of such contributions generally serves as a rate base reduction since the contributions represent non-investor supplied funds. Non-cash utility property has been received, primarily from developers, as advances or contributions of $77,094, $83,041 and $101,226 for the years ended December 31, 2009, 2008 and 2007, respectively.

Generally, the Company depreciates utility plant funded by contributions and amortizes its contributions balance as a reduction to depreciation expense, producing a result which is functionally equivalent to reducing the original cost of the utility plant for the contributions. Certain of the Company's subsidiaries do not depreciate contributed property, based on regulatory guidelines. Amortization of contributions in aid of construction was $20,227, $20,219 and $20,720 for the years ended December 31, 2009, 2008 and 2007, respectively.

Recognition of Revenues

Revenues of the regulated utility subsidiaries are recognized as water and wastewater services are provided and include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

The Company has agreements with the United States Government to operate and maintain water and wastewater systems at various military bases pursuant to 50-year contracts ("military agreements"). These contracts also include construction components that are accounted for separately from the operations and management components. The military agreements are subject to periodic price redetermination adjustments and modifications for changes in circumstance. Additionally, the Company has agreements ranging in length from three to 40 years with various municipalities to operate and maintain water and wastewater systems ("O&M agreements"). Revenue from operations and management services are recognized as services are provided. (See Note 16)

Construction Contracts

Revenues from construction projects are recognized over the contract term based on the estimated percentage of completion during the period compared to the total estimated services to be provided over the entire contract. Losses on contracts are recognized during the period in which the loss first becomes probable and estimable. Revenues recognized during the period in excess of billings on construction contracts are recorded as unbilled revenue. Billings in excess of revenues recognized on construction contracts are recorded as other current liabilities until the recognition criteria are met. Changes in contract performance and related estimated contract profitability may result in revisions to costs and revenues and are recognized in the period in which revisions are determined.

Under these agreements, revenues were $28,796, $47,889 and $32,141 and operation and maintenance expenses were $25,060, $44,227 and $34,543 as of December 31, 2009, 2008 and 2007, respectively. Included in the amounts are construction revenues of $5,614, $25,766 and $12,902 and operation and maintenance expenses of $5,439, $24,852 and $12,601 related to the Company's Fillmore contract at December 31, 2009, 2008, and 2007, respectively. The construction phase of the contract was substantially complete and in service at December 31, 2009.

Income Taxes

The parent company and its subsidiaries participate in a consolidated federal income tax return for U.S. tax purposes. Members of the consolidated group are charged with the amount of federal income tax expense determined as if they filed separate returns.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. The Company provides deferred income taxes on the difference between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates expected to be in effect when these temporary differences are projected to reverse. In addition, the regulated utility subsidiaries recognize regulatory assets and liabilities for the effect on revenues expected to be realized as the tax effects of temporary differences, previously flowed through to customers, reverse.

Investment tax credits have been deferred by the regulated utility subsidiaries and are being amortized to income over the average estimated service lives of the related assets.

The Company recognizes accrued interest and penalties related to tax positions as a component of income tax expense.

The Company accounts for sales tax collected from customers and remitted to taxing authorities on a net basis.

Allowance for Funds Used During Construction ("AFUDC")

AFUDC is a non-cash credit to income with a corresponding charge to utility plant which represents the cost of borrowed funds or a return on equity funds devoted to plant under construction. The regulated utility subsidiaries record AFUDC to the extent permitted by the Regulators.

Environmental Costs

The Company's water and wastewater operations are subject to federal, state, local and foreign requirements relating to environmental protection, and as such, the Company periodically becomes subject to environmental claims in the normal course of business. Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized as appropriate. Remediation costs that relate to an existing condition

caused by past operations are accrued, on an undiscounted basis, when it is probable that these costs will be incurred and can be reasonably estimated. Remediation costs accrued amounted to $7,947 and $10,538 at December 31, 2009 and 2008, respectively. At December 31, 2009, $7,700 of the accrual (including $1,100 accrued in 2009) relates to a conservation agreement entered into by a subsidiary of the Company with the National Oceanic and Atmospheric Administration requiring the Company to, among other provisions, implement certain measures to protect the steelhead trout and its habitat in the Carmel River watershed in the state of California. The Company paid $3,500 related to this agreement during 2009, and has agreed to pay $1,100 annually from July 2010 to July 2016. The Company pursues recovery of incurred costs through all appropriate means, including regulatory recovery through customer rates.

New Accounting Standards

Fair Value Measurements

In January 2010, the Financial Accounting Standards Board ("FASB") issued authoritative guidance that requires new disclosures of (i) the amounts of significant transfers into and out of Level 1 and Level 2 of the fair value hierarchy and the reasons for those transfers and (ii) information in the reconciliation of recurring Level 3 measurements (those using significant unobservable inputs) about purchases, sales, issuances, and settlements on a gross basis. This update also clarifies existing fair value disclosures about the level of disaggregation and about inputs and valuation techniques used to measure fair value. This guidance is effective for interim and annual periods beginning after December 15, 2009, except for the requirement to disclose information about purchases, sales, issuances and settlements in the reconciliation of Level 3 measurements, which does not become effective until interim and annual periods beginning after December 15, 2010. As this guidance clarifies and provides for additional disclosure requirements only, the adoption of this guidance is not expected to have an impact on the Company's results of operations, financial position or cash flows.

In August 2009, the FASB issued authoritative guidance clarifying the measurement of the fair value of liabilities. The amendments reduce potential ambiguity in financial reporting when measuring the fair value of liabilities and help to improve consistency in the application of authoritative guidance. This update is effective for the first reporting period, including interim periods, beginning after issuance, which for the Company was October 1, 2009. The adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows.

In April 2009, the FASB provided additional guidance on fair value measurements in inactive markets when the volume and level of activity for the asset and liability have significantly decreased. This amendment also includes guidance on identifying circumstances that indicate a transaction is not orderly. This guidance is effective for interim reporting periods ending after June 15, 2009. The adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows. (See Note 18)

In February 2008, the FASB issued guidance that allowed a one-year deferral of adoption of the guidance for nonfinancial assets and nonfinancial liabilities (such as intangible assets, property, plant and equipment and goodwill) that are required to be measured at fair value on a periodic basis (such as at acquisition or impairment). The Company elected to use this deferral option and accordingly, adopted this guidance for the Company's nonfinancial assets and liabilities valued on a non-recurring basis on January 1, 2009. The adoption of this guidance did not have a significant impact on the Company's results of operations, financial position or cash flows.

Accounting Standards Codification

In June 2009, the FASB issued authoritative guidance that establishes the FASB Accounting Standards Codification ("Codification") as the source of authoritative U.S. GAAP recognized by the FASB to be applied by non-governmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. All other

non-grandfathered, non-SEC accounting literature not included in the Codification is non-authoritative. This guidance is effective for interim and annual periods ending after September 15, 2009. The adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows.

Consolidation of Variable Interest Entities

In June 2009, the FASB issued authoritative guidance that replaces the quantitative-based risk and rewards calculation for determining which reporting entity has a controlling financial interest in a variable interest entity with a qualitative approach. This revised guidance also requires additional disclosures about a reporting entity's involvement in variable interest entities. This guidance is effective for the Company beginning January 1, 2010. The Company does not expect the adoption of this update to have a significant impact on the Company's results of operations, financial position or cash flows; however, due to evolving interpretations of this guidance, the Company has not fully completed its assessment.

Transfers of Financial Assets

In June 2009, the FASB issued authoritative guidance that amends current guidance for accounting for the transfers of financial assets. Key provisions include (i) the removal of the concept of qualifying special purpose entities, (ii) the introduction of the concept of a participating interest, in which a portion of a financial asset has been transferred and (iii) the requirement that to qualify for sale accounting, the transferor must evaluate whether it maintains effective control over transferred financial assets either directly or indirectly. Further, the amendments require enhanced disclosures about the risks that a transferor continues to be exposed to because of its continuing involvement in transferred financial assets. This guidance is effective for the Company beginning January 1, 2010, and is required to be applied prospectively. The Company does not expect the adoption of this update to have an impact on the Company's results of operations, financial position or cash flows.

Subsequent Events

In May 2009 and clarified in February 2010, the FASB issued authoritative guidance that establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. This standard sets forth: (i) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions, (ii) the circumstances under which an entity should recognize events or transactions and (iii) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. This guidance is effective for interim and annual periods ending after June 15, 2009. The adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows.

Fair Value of Financial Instruments Disclosures

In April 2009, the FASB issued revised authoritative guidance to require disclosures about the fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This amendment is effective for interim reporting periods ending after June 15, 2009. In periods after initial adoption, this guidance requires comparative disclosures only for periods ending after initial adoption. As this revised guidance provides for additional disclosure requirements only, the adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows.

Recognition and Presentation of Other-Than-Temporary Impairments

In April, 2009, the FASB amended authoritative guidance related to the impairment of certain debt securities and will require an entity to assess whether it (i) has the intent to sell the debt security or (ii) more likely than not will be required to sell the debt security before its anticipated recovery. If either of these conditions is met, the entity must recognize an other-than-temporary impairment. If an entity is able to meet the criteria to assert that it will not have to sell the security before recovery, impairment charges related to credit

losses would be recognized in earnings, while impairment charges related to non-credit losses (for example, liquidity risk) would be reflected in other comprehensive income. The amended guidance is effective for interim reporting periods ending after June 15, 2009. The adoption of this guidance did not have an impact on the Company's results of operations, financial position or cash flows.

Contingencies Acquired in a Business Combination

In April 2009, the FASB amended and clarified the authoritative guidance related to accounting for the initial recognition and measurement, subsequent measurement and accounting, and related disclosures arising from contingencies in a business combination. Assets acquired and liabilities assumed in a business combination that arise from contingencies should be recognized at fair value on the acquisition date if fair value can be determined during the measurement period. If fair value can not be determined, companies should account for the acquired contingencies using existing guidance. This guidance is effective for the Company for business combinations finalized after January 1, 2009.

Pension and Other Postretirement Benefit Plan Asset Disclosures

In December 2008, the FASB issued authoritative guidance that requires additional disclosures for employers' pension and other postretirement benefit plan assets. This guidance requires employers to disclose information about fair value measurements of plan assets, the investment policies and strategies for the major categories of plan assets, and significant concentrations of risk within plan assets. This guidance is effective for the Company as of December 31, 2009. As this guidance provides only disclosure requirements, its adoption did not have an impact on the Company's results of operations, financial position or cash flows.

Noncontrolling Interests in Consolidated Financial Statements

In December 2007 and clarified in January 2010, the FASB issued authoritative guidance clarifying that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. With certain exceptions, this guidance requires that changes in a parent's ownership interest in a subsidiary or group of assets that is a business or a nonprofit activity be reported as an equity transaction in the consolidated financial statements when it does not result in a change in control. When change in a parent's ownership interest results in deconsolidation, a gain or loss should be recognized in the consolidated financial statements. This guidance was applied prospectively as of January 1, 2009, except for the presentation and disclosure requirements, which were applied retrospectively for all periods presented. The adoption of this guidance did not have a material impact on the Company's results of operations, cash flows or financial positions; however, it could impact future transactions entered into by the Company. As a result of the adoption of this guidance, beginning in the first quarter of 2009, the Company reflects its subsidiaries' preferred stock without mandatory redemption requirements in its consolidated financial statements within equity. The Company reclassified these preferred shares to equity within the Company's Consolidated Balance Sheets and Statements of Changes in Stockholders' Equity for all periods presented. In the Company's 2008 Form 10-K, these preferred shares were presented as preferred stock without mandatory redemption requirements separate from equity within the Company's Consolidated Balance Sheets. The dividends on these preferred shares have not been reflected separately on the Company's Statements of Operations or the Company's Statements of Comprehensive Loss, as the amounts are not considered material.

Reclassifications

Certain reclassifications have been made to conform previously reported data to the current presentation.

Note 3: Acquisitions and Divestitures

Acquisitions

During 2009, the Company closed on seven acquisitions (six regulated water and wastewater systems, and one in its non-regulated segment) for an aggregate purchase price of $18,144. The purchase price for each

acquisition was allocated to the net tangible and intangible assets based upon their estimated fair values at the acquisition date. Assets acquired totaled $29,462, including plant and equipment of $17,843, current assets of $5,857, goodwill of $606, and long-lived assets of $5,156. Liabilities assumed totaled $11,318, including debt of $3,990, current liabilities of $5,732, long-term liabilities of $970, and contributions in aid of construction of $626.

During 2008, the Company closed on acquisitions of 10 regulated water and wastewater systems, for an aggregate purchase price of $12,512, including transaction costs of $2,622. Assets acquired (primarily plant and equipment) totaled $16,291, and liabilities assumed were $3,779 of contributions in aid of construction.

During 2007, the Company acquired nine regulated water systems for a total aggregate purchase price of $15,877. Included in this total was the Company's acquisition on November 1, 2007 of all of the capital stock of S.J. Services, Inc. ("SJS") for $13,458. The acquisition was accounted for as a business combination. Accordingly, operating results of SJS from November 1, 2007 were included in the Company's results of operations. The purchase price was allocated to the net tangible and intangible assets based upon their estimated fair values at the date of acquisition. Total SJS assets acquired were $23,420, including $4,727 of goodwill (See Note 8), and liabilities assumed totaled $9,962, including long-term debt of $2,791 and contributions in aid of construction of $5,566.

Also during 2007, the Company's New Jersey subsidiary entered into an agreement with the City of Trenton, New Jersey to purchase the assets of the City's water system located in the four surrounding townships. The agreement required approval from the New Jersey Regulator. The initial proposed purchase price of $100,000 was subsequently amended to $75,000 plus the provision of technical services from the City over seven years to ensure a smooth transition of ownership at a total cost of $5,000. Since February 2009, a small group of City residents ("Petitioners") has been involved in litigation with City and NJAWC seeking to force the sale to a referendum. In April 2009, the New Jersey Regulator issued an order, which was extended on December 1, 2009, approving the stipulation of the parties (the "Stipulation"); however, the effective date of the Stipulation is automatically stayed pending resolution of court proceedings. On December 19, 2009, a New Jersey Superior Court Appellate Division panel unanimously upheld lower trial court rulings affirming the City and the Company's position. The New Jersey Supreme Court ("Supreme Court") has granted Petitioners' request for certification and oral argument is scheduled before the Supreme Court on March 22, 2010. The Company can provide no assurance as to the outcome of the litigation. The Stipulation includes the Company's agreement to purchase finished water from the City for the next 20 years under a water supply agreement. The acquisition is expected to add approximately forty thousand customers to the Company's customer base. Included in other current assets is a $10,000 refundable deposit the Company made in December 2007 that is being held in an interest bearing escrow account as required by the bidding process.

Divestitures

In September of 2008, the Company's California subsidiary completed its transfer of ownership of the Felton water system to the San Lorenzo Valley Water District ("SLVWD"). Under the terms of the agreement, SLVWD paid $13,400 for the operating assets of the water system that serves approximately 1,330 customers. The payment included a $10,568 cash payment and the assumption of $2,832 in debt. Including goodwill, the Company recognized a loss of $381 on the sale of these assets. (See Note 8)

Table of Contents

Note 4: Utility Plant

The components of utility plant by category at December 31 are as follows:

	Range of Remaining Useful Lives	2009	2008
Water plant			
Land and other non-depreciable assets		$ 144,295	$ 144,624
Sources of supply	7 to 127 Years	564,886	512,222
Treatment and pumping facilities	3 to 101 Years	2,675,718	2,514,155
Transmission and distribution facilities	9 to 127 Years	6,290,578	5,940,177
Services, meters and fire hydrants	4 to 96 Years	2,363,394	2,224,568
General structures and equipment	3 to 112 Years	645,727	656,043
Wastewater plant	4 to 86 Years	702,725	630,983
Construction work in progress		304,599	338,880
		13,691,922	12,961,652
Less accumulated depreciation		3,168,078	2,969,869
		$ 10,523,844	$ 9,991,783

Utility plant depreciation expense amounted to $262,825 in 2009, $267,763 in 2008 and $263,737 in 2007.

The provision for depreciation expressed as a percentage of the aggregate average depreciable asset balances was 2.68% in 2009, 2.93% in 2008 and 3.11% in 2007.

Note 5: Allowance for Uncollectible Accounts

The following table summarizes the changes in the Company's allowances for uncollectible accounts:

	2009	2008	2007
Balance at January 1	$(18,644)	$(20,923)	$(23,061)
Amounts charged to expense	(21,781)	(17,267)	(17,553)
Amounts written off	25,079	22,583	22,192
Recoveries of amounts written off	(3,689)	(3,037)	(2,501)
Balance at December 31	$(19,035)	$(18,644)	$(20,923)

Note 6: Non-regulated Trade and Other Receivables, Net

Components of the Company's non-regulated trade and other receivables, net at December 31 are as follows:

	2009	2008
Non-regulated trade accounts receivable	$33,945	$29,613
Allowance for doubtful accounts—non-regulated trade accounts receivable	(3,837)	(5,221)
Non-regulated unbilled revenue	15,678	16,602
Other	29,300	27,883
	$75,086	$68,877

The following table summarizes the changes in the Company's non-regulated allowances for uncollectible accounts:

	2009	2008	2007
Balance at January 1	$(5,221)	$(5,567)	$(9,345)
Amounts (charged) credited to expense	(259)	(1,587)	1,597
Amounts written off	1,805	1,942	2,184
Recoveries of amounts written off	(162)	(9)	(3)
Balance at December 31	$(3,837)	$(5,221)	$(5,567)

Note 7: Regulatory Assets and Liabilities

The regulatory assets represent costs that are expected to be fully recovered from customers in future rates. Except for income taxes, regulatory assets are excluded from the Company's rate base and do not earn a return. The components of regulatory assets at December 31 are as follows:

	2009	2008
Income taxes recoverable through rates	$233,806	$231,439
Debt and preferred stock expense	75,693	67,271
Deferred pension expense	209,288	237,665
Deferred other postretirement benefit expense	141,830	136,937
Deferred security costs	10,121	12,763
Deferred business services project expense	12,496	14,322
Deferred tank painting costs	24,705	22,347
Deferred rate case expense	10,919	14,000
Purchase premium recoverable through rates	61,101	61,003
Environmental remediation recoverable through rates	7,700	6,600
Coastal water project costs	21,056	18,262
San Clemente Dam project costs	16,392	15,341
Removal costs recoverable through rates	46,090	35,097
Other	80,823	46,607
	$952,020	$919,654

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the regulatory authorities of full normalization for rate making purposes. Full normalization requires no flow through of tax benefits to customers. The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets.

Debt expense is amortized over the lives of the respective issues. Call premiums on the redemption of long-term debt, as well as unamortized debt expense, are deferred and amortized to the extent they will be recovered through future service rates. Expenses of preferred stock issues without sinking fund provisions are amortized over 30 years from date of issue; expenses of issues with sinking fund provisions are charged to operations as shares are retired.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain subsidiaries. These costs will be recovered in future service rates as contributions are made to the pension plan. The Company

also has regulatory assets of $166,441 and $198,506 at December 31, 2009 and 2008, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

Postretirement benefit expense in excess of the amount recovered in rates through 1997 has been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service and will be fully recovered over a 20-year period ending in 2012 as authorized by the regulatory authorities. The Company has regulatory assets of $134,180 and $131,300 at December 31, 2009 and 2008, respectively, which is the portion of the underfunded status that is probable of recovery through rates in future periods.

The cost of additional security measures that were implemented to protect facilities after the terrorist attacks on September 11, 2001 has been deferred by certain subsidiaries. These costs are recognized in the rates charged for water service by certain subsidiaries. These costs are being recovered over periods ranging from five to ten years.

Business services project expenses consist of reengineering and start-up activities for consolidated customer and shared administrative service centers that began operations in 2001. These costs are recognized in the rates charged for water service by certain subsidiaries.

Tank painting costs are generally deferred and amortized to current operations on a straight-line basis over periods ranging from 5 to 15 years, as authorized by the regulatory authorities in their determination of rates charged for service.

The Company amortizes rate case expenditures over regulatory approved amortization periods, typically three years. Rate case proceeding expenditures probable of future recovery are deferred.

Purchase premium recoverable through rates is primarily the recovery of the acquisition premiums related to an asset acquisition by the Company’s California subsidiary during 2002, and acquisitions in 2007 by the Company’s New Jersey subsidiary. As authorized for recovery by the California and New Jersey Regulators, these costs are being amortized to operations through November 2048.

Environmental remediation recoverable through rates is the recovery of costs incurred by the Company’s California subsidiary under a settlement agreement entered into with the National Oceanic and Atmospheric Administration to improve habitat conditions in the Carmel River Watershed.

Coastal water project costs include all preliminary costs associated with the studying, testing, and design of alternatives to help solve water supply shortages in Monterey, California. Coastal water project costs incurred through December 31, 2007 have been reviewed and approved for recovery through a surcharge that went into effect January 1, 2007. Costs deferred during 2009 and 2008 totaled $6,542 and $4,731, respectively. The Company believes it is probable that the costs incurred since the last rate review will also be recoverable.

San Clemente Dam project costs include deferred costs for the Company’s California subsidiary to investigate alternatives to strengthen or remove the San Clemente Dam due to potential earthquake or flood safety concerns. These costs are not yet in rates; however, the Company believes it is probable that the costs incurred will be recoverable.

Other regulatory assets include certain deferred employee benefit costs, deferred treatment facility costs, as well as various regulatory balancing accounts.

The components of regulatory liabilities at December 31 are as follows:

	2009	2008
Removal costs recovered through rates	$251,837	$231,789
Deferred income taxes	33,103	34,180
Other	37,341	41,355
	$322,281	$307,324

Removal costs recovered through rates are retirement costs recovered through customer rates during the life of the associated assets. In December 2008, the Company's subsidiary in New Jersey, at the direction of the New Jersey Regulator, began to amortize $48,000 of the total balance into operations via straight line amortization through November 2048.

Deferred income taxes represent the income tax effect of the adjustment to record the full accumulated postretirement benefit obligation.

Other regulatory liabilities include legal settlement proceeds, deferred gains, future customer refunds, and various regulatory balancing accounts.

Note 8: Goodwill

The Company's annual impairment reviews are performed as of November 30 of each year, in conjunction with the timing of the completion of the Company's annual strategic business plan. At November 30, 2009, the Company's goodwill was $1,250,067. The Company also undertakes interim reviews when the Company determines that a triggering event that would more likely than not reduce the fair value of a reporting unit below its carrying value has occurred.

The Company uses a two-step impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). The step 1 calculation used to identify potential impairment compares the calculated fair value for each of the Company's reporting units to their respective net carrying values (book values), including goodwill, on the measurement date. If the fair value of any reporting unit is less than such reporting unit's carrying value, then step 2 is performed to measure the amount of the impairment loss (if any) for such reporting unit.

The step 2 calculation of the impairment test compares, by reporting unit, the implied fair value of the goodwill to the carrying value of goodwill. The implied fair value of goodwill is equal to the excess of the fair value of each reporting unit above the fair value of such reporting unit's identified assets and liabilities. If the carrying value of goodwill exceeds the implied fair value of goodwill for any reporting unit, an impairment loss is recognized in an amount equal to the excess (not to exceed the carrying value of goodwill) for that reporting unit.

The determination of the fair value of each reporting unit and the fair value of each reporting unit's assets and liabilities is performed as of the measurement date using observable market data before and after the measurement date (if that subsequent information is relevant to the fair value on the measurement date).

For the November 30, 2009 impairment test, the estimated fair value of the Regulated reporting unit for step 1 was based on a combination of the following valuation techniques:

- observable trading prices of comparable equity securities of publicly-traded water utilities considered by us to be the Company's peers; and
- discounted cash flow models developed from the Company's internal forecasts.

The first valuation technique applies average peer multiples to the Regulated reporting unit's historic and forecasted cash flows. The peer multiples are calculated using the average trading prices of comparable equity securities of publicly-traded water utilities, their published cash flows and forecasts of market price and cash flows for those peers.

The second valuation technique forecasts each reporting unit's five-year cash flows using an estimated long-term growth rate and discounts these cash flows at their respective estimated weighted average cost of capital.

Because of the unique nature, small size and lack of historical earnings of most of the Non-Regulated reporting units, a market approach could not be reasonably applied. As such the estimated fair values of the Non-regulated reporting units were determined entirely on the basis of discounted cash flow models.

The Company has completed its November 30, 2009 annual impairment review and does not believe that the Company's goodwill balance was impaired. The Company's fair value calculated in its 2009 impairment test period was approximately 6% above the aggregate carrying value of its reporting units.

However, there can be no assurances that the Company will not be required to recognize an impairment of goodwill in the future due to market conditions or other factors related to the Company's performance. These market events could include a decline over a period of time of the Company's stock price, a decline over a period of time in valuation multiples of comparable water utilities, the lack of an increase in the Company's market price consistent with its peer companies, or decreases in control premiums. A decline in the forecasted results in our business plan, such as changes in rate case results or capital investment budgets or changes in our interest rates, could also result in an impairment charge.

The Company also made certain assumptions, which it believes to be appropriate, that support the fair value of its reporting units. The Company considered, in addition to the listed trading price of the Company's shares, the applicability of a control premium to the Company's shares and certain other factors the Company deemed appropriate. As a result, the Company concluded that the Company's fair value exceeds what the Company might otherwise have concluded had it relied on market price alone.

The difference between the Company's calculated market capitalization (which approximates carrying value) and the aggregate fair value of reporting units resulted from an estimated control premium. The estimated control premium represents the incremental premium a buyer is willing to pay to acquire a controlling, majority interest in the Company. In estimating the control premium, management principally considered the current market conditions and historical premiums paid in utility acquisitions observed in the marketplace.

For the years ended December 31, 2009, 2008 and 2007, the Company recorded impairment charges for goodwill in the amount of $450,000, $750,000, and $509,345, respectively.

The Company's calculated market capitalization at March 31, 2009 was $1,186,000 below the aggregated carrying value of its reporting units. During the first quarter of 2009, the Company's market price experienced a high degree of volatility and, as of March 31, 2009, had a sustained period for which it was below historical averages and 10% below the market price employed in the Company's 2008 annual goodwill impairment test. Having considered both qualitative and quantitative factors, management concluded that this sustained decline in market value below the market value which existed at the 2008 annual impairment test, was an interim triggering event. An interim impairment test was performed and $450,000 was recognized as a goodwill impairment charge, primarily in the Regulated reporting unit, for the three months ended March 31, 2009.

As of March 31, 2008, in light of the initial public offering price and trading levels in the Company's common stock subsequent to the date of the initial public offering, the Company performed an interim impairment test and, on May 9, 2008, management concluded that the carrying value of the Company's goodwill was impaired. The Company believed that the initial public offering price was indicative of the value of the

Company at March 31, 2008, and accordingly, based on those factors recorded an impairment charge to the goodwill of its Regulated reporting unit in the amount of $750,000 as of March 31, 2008. The impairment charge was primarily attributed to the market price of the Company's common stock (both the initial public offering price and the price during subsequent trading) being less than the estimate of the initial public offering price used during the 2007 annual test. Also contributing to the impairment was a decline in the fair value of the Company's debt (due to increased market interest rates).

The Company completed its scheduled annual impairment test in the fourth quarter of 2007 and determined an impairment had occurred based upon information regarding the Company's market value in connection with the initial public offering. Management determined that the indicative fair value of the Company based on estimates of the initial public offering price range was the best evidence of the Company's market value and incorporated this indicated market value into the Company's valuation methodology, which also considered other items, such as peer multiples, discounted cash flows and a control premium. Based on the results of the impairment test, an impairment of $266,000 to the Company's carrying value was recognized as of December 31, 2007.

During the third quarter of 2007, as a result of the Company's debt being placed on review for a possible downgrade and the proposed sale of a portion of the Company in the initial public offering, management determined at that time it was appropriate to update its valuation analysis before the next scheduled annual test. Based on this assessment, the Company performed an interim impairment test and recorded an impairment charge to goodwill related to its Regulated reporting unit in the amount of $243,345 as of September 30, 2007. The decline was primarily due to a slightly lower long-term earnings forecast caused by updated customer demand and usage expectations and expectations for timing of capital expenditures and rate recovery.

The change in the Company's goodwill assets, as allocated between the reporting units is as follows:

	Regulated Unit		Non-regulated Units		Consolidated		
	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Cost	Accumulated Impairment	Total Net
Balance at January 1, 2008	$3,572,650	$(1,245,380)	$235,549	$ (105,867)	$3,808,199	$(1,351,247)	$2,456,952
Impairment losses	—	(750,000)	—	—	—	(750,000)	(750,000)
Felton water system sale	(2,373)	—	—	—	(2,373)	—	(2,373)
Reclassifications and other activity(a)	(5,062)	—	—	—	(5,062)	—	(5,062)
Balance at December 31, 2008	3,565,215	(1,995,380)	235,549	(105,867)	3,800,764	(2,101,247)	1,699,517
Goodwill from acquisitions	440	—	166	—	606	—	606
Impairment losses	—	(448,248)	—	(1,752)	—	(450,000)	(450,000)
Reclassifications and other activity	258	—	—	—	258	—	258
Balance at December 31, 2009	$3,565,913	$(2,443,628)	$235,715	$ (107,619)	$3,801,628	$(2,551,247)	$1,250,381

(a) Includes $4,793 of goodwill transferred to regulatory assets in December 2008 for acquisition premiums recoverable through rates.

Note 9: Stockholders' Equity

Common Stock

During 2009, RWE Aktiengesellschaft ("RWE") completed the divestiture of its investment in the Company that began with the April 28, 2008 initial public offering ("IPO") of the Company's stock. In April and May 2008, RWE sold 63,173 shares of common stock, including an underwriters' option of 5,173 shares, at an IPO

price of $21.50. The Company did not receive any proceeds from the sale of shares. Prior to the IPO, the Company was an indirect wholly-owned subsidiary of RWE. After the IPO and exercise of the underwriters' over-allotment option, RWE owned approximately 60% of the Company's common shares.

On June 10, 2009 the Company completed a public offering of 29,900 shares of its common stock. Pursuant to the offering, the Company sold 14,500 shares of common stock and 15,400 shares were sold by RWE. The Company completed the sale of 14,500 shares of common stock at $17.25 per share. The proceeds from the offering, net of underwriters' discounts and expenses payable by the Company, were $242,301. The Company used the proceeds to repay short-term debt.

RWE completed the divestiture of its investment in the Company in 2009 through the aforementioned June 2009 sale of 15,400 shares, including an underwriters' option of 3,900 shares, at a price per share of $17.25; an August 2009 sale of 40,250 shares, including underwriters' options of 5,250 shares, at a price of $19.25; and a November 2009 sale of 41,087 shares, including an underwriters' option of 3,735 shares, at a price of $21.63. The Company did not receive any proceeds from these sales by RWE of the Company's shares.

Effective the first quarter of 2008, the Company's Board of Directors' authorized 50,000 shares of par value $0.01 per share preferred stock. As of December 31, 2009 there are no shares outstanding.

In September of 2008, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of August 15, 2008, amounting to $31,992. In December 2008, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of November 18, 2008, amounting to $31,997.

In March 2009, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of February 18, 2009, amounting to $32,000. In June 2009, the Company made a cash dividend payment of $0.20 per share to all common shareholders of record as of May 18, 2009, amounting to $32,006. In September 2009, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of August 18, 2009, amounting to $36,658. In December 2009, the Company made a cash dividend payment of $0.21 per share to all common shareholders of record as of November 18, 2009, amounting to $36,667.

On January 29, 2010, the Company's Board of Directors declared a quarterly cash dividend payment of $0.21 per share payable on March 1, 2010 to all shareholders of record as of February 18, 2010.

Accumulated Other Comprehensive Loss

The following table presents accumulated other comprehensive loss:

	2009	2008
Employee benefit plans funded status adjustments	$(68,250)	$(84,271)
Foreign currency translation	3,573	2,020
Balance at December 31	$(64,677)	$(82,251)

Stock Based Compensation

The Company has granted stock option and restricted stock unit awards to non-employee directors, officers and other key employees of the Company pursuant to the terms of its 2007 Omnibus Equity Compensation Plan (the "Plan"). The total aggregate number of shares of common stock that may be issued under the Plan was increased to 15,500 from 6,000 in May of 2009. As of December 31, 2009, a total of 12,267 shares are available for grant under the Plan. Shares issued under the Plan may be authorized but unissued shares of Company stock or reacquired shares of Company stock, including shares purchased by the Company on the open market for purposes of the Plan.

The Company recognizes compensation expense for stock awards over the vesting period of the award. The following table presents stock-based compensation expense recorded in operations and maintenance expense in the accompanying Consolidated Statement of Operations for the years ended December 31, 2009, 2008 and 2007:

	2009	2008	2007
Stock options	$ 3,415	$ 1,607	$ —
Restricted stock units	3,799	957	680
Restricted stock	—	1,798	—
Employee stock purchase plan	388	172	—
Stock-based compensation in operation and maintenance expense	7,602	4,534	680
Income tax benefit	(2,965)	(1,768)	(265)
After-tax stock-based compensation expense	$ 4,637	$ 2,766	$ 415

There were no significant stock-based compensation costs capitalized during the years ended December 31, 2009, 2008 and 2007.

The cost of services received from employees in exchange for the issuance of stock options and restricted stock awards is required to be measured based on the grant date fair value of the awards issued. The value of stock options and restricted stock awards at the date of the grant is amortized through expense over the requisite service period, which is generally three years. All awards granted in 2009 and 2008 are classified as equity.

The Company receives a tax deduction based on the intrinsic value of the award at the exercise date for stock options and the distribution date for restricted stock and restricted stock units. For each award, throughout the requisite service period, the Company recognizes the tax benefit related to compensation costs, which have been included in deferred tax assets. The tax deductions in excess of the benefits recorded throughout the requisite service period are recorded to shareholders' equity or the income statement and are included in the financing section of the cash flow statement.

The Company stratified its grant populations and used historic employee turnover rates and general market data to estimate employee forfeitures. The estimated rate is compared to the actual forfeitures at the end of the period and adjusted as necessary.

Stock Options

On April 22, 2008, the Company granted 2,078 non-qualified stock options to certain employees and non-employee directors under the Plan. The stock options were awarded in two grants with "Grant 1" vesting on January 1, 2010 and "Grant 2" vesting January 1, 2011. These awards included 1,470 stock options that are subject to performance based vesting requirements. The performance conditions for Grant 1 are based on the achievement of 120% of net income targets in 2007 and 2008. Grant 2 performance conditions are based on the achievement of 120% of net income targets in 2008 and 2009. On February 20, 2009, the Company cancelled 311 of the stock options related to the first performance vesting period because the performance goals were not fully met at December 31, 2008. The Grant 2 performance vesting period ended December 31, 2009 and according to the plan, the Company must certify the level of achievement no later than 90 days after January 1, 2010. Any portion of the stock options that do not fully satisfy the performance goals will be forfeited as of the date the level of achievement is certified. In February 2010, 459 stock options were forfeited because the performance goals were not fully met. The Company continues to recognize expense on the remaining stock options during the service period, which ends December 31, 2010.

Additionally during August 2008, the Company granted 5 stock options to newly appointed non-employee directors in two grants vesting on January 1, 2011. These awards have no performance vesting conditions.

On February 20, 2009, the Company granted 1,091 non-qualified stock options to certain employees under the Plan. The stock options vest ratably over a three-year service period from January 1, 2009. These awards have no performance vesting conditions.

The following table presents the weighted average assumptions used in the pricing model for grants and the resulting weighted average grant date fair value of stock options granted in the years ended December 31, 2009 and 2008.

	2009	2008
Dividend yield	3.86%	3.72%
Expected volatility	31.67%	29.00%
Risk-free interest rate	1.79%	2.82%
Expected life (years)	4.36	4.29
Exercise price	$20.70	$21.50
Grant date fair value	$ 3.96	$ 4.05

The Company utilized the “simplified method” to determine the expected stock option life due to insufficient historical experience to estimate the exercise patterns of the stock options granted. The Company began granting stock options at the time of the IPO in April 2008. Expected volatility is based on a weighted average of historic volatilities of traded common stock of peer companies (regulated water companies) over the expected term of the stock options and historic volatilities of the Company’s common stock during the period it has been publicly traded. The dividend yield is based on the Company’s expected dividend payments and the stock price on the date of grant, which was the IPO price for Grants 1 and 2. The risk-free interest rate is the market yield on U.S. Treasury strips with maturities similar to the expected term of the stock options. The exercise price of the stock options is equal to the fair market value of the underlying stock on the date of option grant. Stock options granted vest over periods ranging from one to three years and expire seven years from the effective date of the grant. The fair value of each option is estimated on the date of grant using the Black-Scholes option-pricing model.

The value of stock options at the date of the grant is amortized through expense over the requisite service period using the straight-line method. As of December 31, 2009, $3,665 of total unrecognized compensation costs related to the nonvested stock options is expected to be recognized over the remaining weighted-average period of 1.20 years.

The table below summarizes stock option activity for the year ended December 31, 2009.

	Shares	Weighted Average Exercise Price (per share)	Weighted Average Remaining Life (years)	Aggregate Intrinsic Value
Options outstanding at January 1, 2009	2,060	$ 21.50		
Granted	1,091	20.70		
Cancelled	(311)	21.50		
Forfeited or expired	(116)	21.16		
Exercised	—	—		
Options outstanding at December 31, 2009	2,724	$ 21.19	5.17	$ 3,317
Exercisable at December 31, 2009(a)	24	$ 21.50	0.64	$ 22

(a) Includes stock options issued to retired employees for Grants 1 and 2.

Restricted Stock Units

On April 22, 2008, the Company granted 269 restricted stock units to certain employees and non-employee directors under the Plan. The restricted stock units were awarded in two grants with “Grant 1” vesting on January 1, 2010 and “Grant 2” vesting January 1, 2011. The grant date fair value of these restricted stock units is $21.50. These awards included 190 restricted stock units that are subject to performance-based vesting requirements. The performance conditions for Grant 1 are based on the achievement of 120% of net income targets in 2007 and 2008. Grant 2 performance conditions are based on the achievement of 120% of net income targets in 2008 and 2009. On February 20, 2009, the Company cancelled 39 of these restricted stock units related to the first performance vesting period because the performance goals were not fully met at December 31, 2008. The Grant 2 performance vesting period ended December 31, 2009 and according to the Plan, the Company must certify the level of achievement no later than 90 days after January 1, 2010. Any portion of the restricted stock units that do not fully satisfy the performance goals will be forfeited as of the date the level of achievement is certified. In February 2010, 60 restricted stock units were forfeited because the performance goals were not fully met. The Company continues to recognize expense on the remaining restricted stock units during the service period, which ends December 31, 2010.

Additionally during August 2008, the Company granted 1 restricted stock units to newly appointed non-employee directors in two grants vesting on January 1, 2011. The weighted average grant date fair value of these restricted stock units is $20.32. These awards have no performance vesting conditions.

On February 20, 2009, the Company granted 195 restricted stock units to certain employees under the Plan. The restricted stock units vest ratably over the three year performance period beginning January 1, 2009 (the “Performance Period”); however, distribution of the shares is contingent upon the achievement of certain market thresholds over the Performance Period. The grant date fair value of the restricted stock units awarded in February 2009 is $22.08.

On May 8, 2009 and June 19, 2009, the Company granted 15 and 5 restricted stock units, respectively, to certain non-employee directors under the Plan. The restricted stock units vested on the date of the grant; however, distribution of the shares will be made within 30 days of the earlier of August 12, 2010 or the participant’s separation from service. The weighted average grant date fair value of these restricted stock units is $18.56.

Restricted stock units generally vest over periods ranging from one to three years. Restricted stock units granted without market conditions are valued at the market value of the Company’s common stock on the date of grant. Restricted stock units granted with market conditions are valued using a Monte Carlo model. As of December 31, 2009, $2,160 of total unrecognized compensation cost related to the nonvested restricted stock units is expected to be recognized over the weighted-average remaining life of 1.22 years.

The value of restricted stock awards at the date of the grant is amortized through expense over the requisite service period using the straight-line method for restricted stock units with service and/or performance vesting. The grant date fair value of restricted stock awards that have market and service conditions and vest ratably is amortized through expense over the requisite service period using the graded-vesting method.

The table below summarizes restricted stock unit activity for the year ended December 31, 2009.

	Shares	Weighted Average Grant Date Fair Value (per share)
Nonvested total at January 1, 2009	267	$ 21.50
Granted	215	21.75
Distributed	(3)	21.50
Cancelled	(39)	21.50
Forfeited	(18)	21.80
Undistributed vested awards(a)	(20)	18.62
Nonvested total at December 31, 2009	402	$ 21.77

(a) Includes restricted stock units granted to retired employees and members of the Company's Board of Directors.

The aggregate intrinsic value of restricted stock units distributed was $51, on which the Company recognized an income tax shortfall of $5, which has been recorded in the accompanying Consolidated Statement of Operations.

If dividends are declared with respect to shares of the Company's common stock before the restricted stock units are distributed, the Company credits a liability for the value of the dividends that would have been paid if the restricted stock units were shares of Company common stock. When the restricted stock units are distributed, the Company pays the employee a lump sum cash payment equal to the value of the dividend equivalents accrued. The Company accrued dividend equivalents totaling $279 and $66 to retained earnings during the years ended December 31, 2009 and 2008, respectively.

Employee Stock Purchase Plan

The Company's Nonqualified Employee Stock Purchase Plan ("ESPP") was effective as of July 1, 2008. Under the ESPP, employees can use payroll deductions to acquire Company stock at the lesser of 90% of the fair market value of a) the beginning or b) the end of each three-month purchase period. As of December 31, 2009 there were 1,832 shares of common stock reserved for issuance under the ESPP. The Company's ESPP is considered compensatory. Compensation costs of $388 and $172 were recognized for the years ended December 31, 2009 and 2008, respectively. During the year ended December 31, 2009 and 2008, the Company issued 129 and 39 shares, respectively, under the ESPP.

Restricted Stock

On April 22, 2008, a subsidiary of RWE contributed 90 shares of the Company's common stock to the Company and the Company granted 90 restricted stock awards under the 2007 Plan. The requisite service period for the restricted stock was three months and the grant date fair value was $21.50. As of December 31, 2008, the restricted stock was fully vested and there were no unrecognized compensation costs related to the nonvested restricted stock units. The Company issued 84 shares of common stock under this award. The aggregate intrinsic value of restricted stock awards on the date of vesting was $1,647. The Company recognized an income tax shortfall of $60, which was recorded in the Consolidated Statement of Operations at the vesting of these awards.

Table of Contents

Note 10: Preferred Stock Without Mandatory Redemption Requirements

Certain preferred stock agreements do not require annual sinking fund payments or redemption except at the option of the subsidiaries and are as follows:

Dividend Yield	Balance at December 31, 2009	Balance at December 31, 2008
4.50%	$1,720	$1,720
5.00%	1,962	1,962
5.50%	486	486
5.75%	389	389
	$4,557	$4,557

Dividends issued totaled $225 in 2009, 2008, and 2007, respectively, and were included in other, net on the accompanying Consolidated Statements of Operations.

Note 11: Long-Term Debt

The Company primarily incurs long-term debt to fund capital expenditures at the regulated subsidiaries. The components of long-term at December 31 are:

	Rate	Weighted Average Rate	Maturity Date	2009	2008
Long-term debt of American Water Capital Corp. (“AWCC”)					
Private activity bonds and government funded debt					
Fixed rate	5.25%-6.75%	6.03%	2018-2039	$ 200,975	$ —
Floating rate(a)				—	86,860
Senior notes					
Fixed rate	5.39%-10.00%	6.26%	2011-2039	3,115,853	2,959,000
Long-term debt of other subsidiaries					
Private activity bonds and government funded debt					
Fixed rate	0.00%-6.88%	5.29%	2010-2039	1,197,611	937,835
Floating rate(b)	0.90%-2.40%	1.05%	2015	8,560	33,420
Mortgage bonds					
Fixed rate	5.48%-9.71%	7.50%	2010-2039	754,966	675,200
Senior debt					
Fixed rate				—	40,613
Mandatory redeemable preferred stock	4.60%-9.75%	8.37%	2013-2036	24,207	24,425
Notes payable and other(c)	4.90%-13.31%	7.27%	2011-2026	6,561	2,882
Long-term debt				5,308,733	4,760,235
Unamortized debt discount, net(d)				57,461	63,800
Total long-term debt				$ 5,366,194	$ 4,824,035

(a) Variable rate tax-exempt bonds remarketed for periods up to 270 days. These bonds may be converted to other short-term variable-rate structures, a fixed-rate structure or subject to redemption. During 2009, AWCC remarketed $76,225 of these bonds to fixed rate private activity bonds. The remaining $10,635 is held in the Company’s treasury at December 31, 2009.

(b) Variable rate tax-exempt bonds which are remarketed for periods up to 270 days. During 2009, $24,860 was remarketed to fixed rate private activity bonds, and the remaining $8,560 was remarketed to floating rate bonds. The $8,560 is classified as current portion of long-term debt in the accompanying balance sheets because it was repurchased by the Company during the first quarter of 2009 when no investor was willing to purchase it at the market rate. This debt was subsequently remarketed as floating rate debt in the second quarter of 2009.

(c) Includes capital lease obligations of $5,679 (including $3,990 from 2009 acquisitions) and $1,829 at December 31, 2009 and 2008, respectively. Lease payments of $608, $637, $673, $580, $512 and $2,669 will be made in 2010, 2011, 2012, 2013, 2014 and thereafter, respectively.

(d) Includes fair value adjustments previously recognized in acquisition purchase accounting.

All $754,966 of the subsidiaries' mortgage bonds and $1,122,065 of the $1,197,611 total subsidiaries' private activity bonds and government funded debt are collateralized by utility plant.

Long-term debt indentures contain a number of covenants that, among other things, limit, subject to certain exceptions, the Company from issuing debt secured by the Company's assets. Certain long term notes require the Company to maintain a ratio of consolidated total indebtedness to consolidated total capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2009 was 0.58 to 1.00. In addition, the Company has $1,929,208 of notes which include the right to redeem the notes in whole or in part from time to time subject to certain restrictions.

In 2007, the Company borrowed $1,750,000 from RWE and used the proceeds to redeem $1,750,000 of its 5.9% mandatory redeemable preferred stock.

Also during 2007, the Company issued senior notes in the principal amount of $2,117,000 and received equity contributions from RWE in the amount of $1,067,092. The Company used the proceeds from the senior notes and equity contributions to repay long-term and short-term RWE notes, repay outstanding commercial paper and for other corporate purposes amounting to $2,011,530, $624,446 and $548,116, respectively.

A portion of the RWE notes that were redeemed in 2007 were obtained for the use of certain of the Company's regulated subsidiaries. These notes were redeemed early resulting in a difference of $8,655 between the book value of the RWE notes and the cash consideration required to extinguish the notes. As agreed with the applicable Regulators, the difference on extinguishment was deferred as a regulatory liability by the Company's regulated subsidiaries and will be amortized to Interest, net over the remaining lives of the original RWE notes for periods ranging from 2014 to 2034. The amount amortized was $1,967, $1,044, and $531 in 2009, 2008, and 2007, respectively.

The future sinking fund payments and maturities are as follows:

Year	Amount
2010	$ 54,068
2011	35,633
2012	31,929
2013	112,717
2014	9,546
Thereafter	5,064,840

Table of Contents

The following long-term debt was issued in 2009:

Company	Type		Interest Rate	Maturity	Amount
American Water Capital Corp:	Private activity fixed rate:	(1)	5.25%	2039	$ 28,500
		(1)	5.63%	2039	26,000
			6.00%	2018	18,250
			6.10%	2019	17,950
			6.25%	2032	23,325
			6.25%	2032	24,860
		(1)	6.25%	2039	45,390
			6.75%	2031	16,700
American Water Capital Corp:	Senior notes-fixed rate:		6.00%	2039	60,000
			7.21%	2019	24,500
			8.25%	2038	75,000
			8.27%	2039	25,500
Other subsidiaries:	Private activity-fixed rate:		1.27%	2029	2,242
			4.14%	2029	1,315
			5.00%	2039	10,500
			5.70%	2039	134,224
		(1)	6.20%	2039	80,000
Other subsidiaries:	Private activity—floating rate:		1.00%	2015	8,560
Other subsidiaries:	Mortgage bonds—fixed rate:		5.48%	2019	25,000
			6.35%	2039	75,000
Other:	Capital lease	(1)	8.82%	2011	41
Total issuances					$722,857

(1) The proceeds of these issuances are initially kept in Trust, pending the Company's certification that it has incurred qualifying capital expenditures. These issuances have been presented as non-cash on the accompanying Consolidated Statements of Cash Flows. Subsequent release of all or a lesser portion of these funds by the applicable Trust are reflected as the release of restricted funds and are included in investing activities in the accompanying statement of cash flows.

The following long-term debt and preferred stock with mandatory redemption requirements were repurchased or retired through optional redemption or payment at maturity during 2009:

Company	Type	Interest Rate	Maturity	Amount
Long-term debt				
American Water Capital Corp	Private activity bonds—floating rate	1.55%-2.20%	2018-2032	$ 86,860
	Senior notes—fixed rate	6.87%-8.25%	2011-2038	28,147
Other subsidiaries.	Private activity bonds—fixed rate	0.00%-5.90%	2009-2034	8,505
	Private activity bonds—floating rate	1.50%-10.00%	2015-2032	33,420
	Mortgage bonds—fixed rate	6.90%-9.22%	2009-2011	20,847
Mandatory redeemable preferred stock		4.60%-6.00%	2013-2019	218
Notes payable and capital leases		4.90%-13.31%	2011-2026	352
Total retirements & redemptions				$ 178,349

Other subsidiaries senior debt of $40,000 and $613 was reclassified to other subsidiaries' fixed rate private activity bonds and government funded debt and mortgage bonds, respectively.

Gains from early extinguishment of debt included in Interest, net amounted to $0 in 2009 and 2008, and $13,113 in 2007, respectively.

Interest, net includes interest income of approximately $10,422, $5,690 and $10,985 in 2009, 2008 and 2007, respectively.

Note 12: Short-Term Debt

The components of short-term debt at December 31 are as follows:

	2009	2008
Revolving credit line	$ —	$ 437,000
Commercial paper, net of $5 and $0 discount at 2009 and 2008, respectively	84,995	—
Book overdraft	34,502	42,010
Total short-term debt	$ 119,497	$ 479,010

AWCC had the following available capacity under its commercial paper program at December 31:

	2009	2008
Commercial paper program	$ 700,000	$ 700,000
Commercial paper program available capacity	615,000	700,000

AWCC has entered into an $840,000 senior unsecured credit facility syndicated among the following group of 11 banks with JPMorgan Chase Bank, N.A. acting as administrative agent:

Bank	Commitment Amount Through September 15, 2012	Commitment Amount Through September 15, 2013
JPMorgan Chase Bank, N.A.	$ 115,000	$ —
Citibank, N.A.	115,000	115,000
Citizens Bank of Pennsylvania	80,000	80,000
Credit Suisse	80,000	80,000
William Street Commitment Corporation	80,000	80,000
Merrill Lynch Bank USA	80,000	80,000
Morgan Stanley Bank	80,000	80,000
UBS Loan Finance LLC	80,000	80,000
National City Bank	50,000	50,000
PNC Bank, N.A.	40,000	40,000
The Bank of New York Mellon	40,000	—
	$ 840,000	$ 685,000

This revolving credit facility is principally used to support the commercial paper program at AWCC and to provide up to $150,000 in letters of credit. On September 15, 2008, a majority of the banks agreed to further extend $685,000 of commitments under this revolving credit facility to September 15, 2013. On December 18, 2008, The Bank of New York Mellon joined the credit facility syndicate with a commitment amount of $40,000 through September 15, 2012. If any lender defaults in its obligation to fund advances, the Company may request

the other lenders to assume the default lender's commitment or replace such defaulting lender by designating an assignee willing to assume the commitment, however the remaining lenders have no obligation to assume a defaulting lender's commitment and we can provide no assurances that we will replace a defaulting lender.

At December 31, AWCC had the following sub-limits and available capacity under the credit facility.

	2009	2008
Letter of credit sublimit	$150,000	$150,000
Letter of credit available capacity	101,754	106,097

At December 31, 2009, the Company had $50,579 of outstanding letters of credit, $48,246 of which was issued under the revolving credit facility noted above.

The following table presents the short-term borrowing activity for AWCC for the years ended December 31, 2009 and 2008:

	2009	2008
Average borrowings	$347,413	$291,821
Maximum borrowings outstanding	708,691	570,429
Weighted average interest rates, computed on a daily basis	0.82%	3.51%
Weighted average interest rates, at December 31	0.39%	0.75%

Interest rates on advances under the credit facility are based on either prime or the London Interbank Offering Rate ("LIBOR") plus an applicable margin based upon credit ratings of the Company, as well as total outstanding amounts under the agreement at the time of the borrowing. The maximum LIBOR margin is 55 basis points.

The credit facility requires the Company to maintain a ratio of consolidated debt to consolidated capitalization of not more than 0.70 to 1.00. The ratio at December 31, 2009 was 0.58 to 1.00.

None of the Company's borrowings are subject to default or prepayment as a result of a downgrading of securities, although such a downgrading could increase fees and interest charges under the Company's credit facilities.

As part of the normal course of business, the Company routinely enters contracts for the purchase and sale of water, energy, fuels and other services. These contracts either contain express provisions or otherwise permit the Company and our counterparties to demand adequate assurance of future performance when there are reasonable grounds for doing so. In accordance with the contracts and applicable contract law, if the Company is downgraded by a credit rating agency, especially if such downgrade is to a level below investment grade, it is possible that a counterparty would attempt to rely on such a downgrade as a basis for making a demand for adequate assurance of future performance. Depending on its net position with a counterparty, the demand could be for the posting of collateral. In the absence of expressly agreed provisions that specify the collateral that must be provided, the obligation to supply the collateral requested will be a function of the facts and circumstances of the Company's situation at the time of the demand. If the Company can reasonably claim that it is willing and financially able to perform its obligations, it may be possible to successfully argue that no collateral should be posted or that only an amount equal to two or three months of future payments should be sufficient. The Company does not expect to post any collateral which will have a material adverse impact on the Company's results of operations, financial position or cash flows.

AWCC has entered into a one year $10,000 committed revolving line of credit with PNC Bank, N.A. This line of credit will terminate on December 31, 2010 unless extended and is used primarily for short-term working capital needs. Interest rates on advances under this line of credit are based on either the prime rate of the financial institution or the applicable LIBOR rate for the term selected plus 175 basis points.

Table of Contents

Note 13: General Taxes

Components of general tax expense from continuing operations for the years ended December 31 are as follows:

	2009	2008	2007
Gross receipts and franchise	$ 81,244	$ 79,228	$ 71,360
Property and capital stock	79,420	80,025	75,172
Payroll	29,749	31,060	28,406
Other general	8,849	8,826	8,315
	$199,262	$199,139	$183,253

Note 14: Income Taxes

Components of income tax expense from continuing operations for the years ended December 31 are as follows:

	2009	2008	2007
State income taxes			
Current	$ (18,525)	$ 16,196	$16,135
Deferred			
Current	(1,599)	409	2,079
Non-current	40,687	10,332	(11)
	20,563	26,937	18,203
Federal income taxes			
Current	555	1,522	30,213
Deferred			
Current	(11,929)	1,973	9,382
Non-current	113,662	82,929	30,468
Amortization of deferred investment tax credits	(1,433)	(1,534)	(1,510)
	100,855	84,890	68,553
	$121,418	$111,827	$86,756

A reconciliation of income tax expense from continuing operations at the statutory federal income tax rate to actual income tax expense for the years ended December 31 is as follows:

	2009	2008	2007
Income tax at statutory rate	$ (39,083)	$(157,708)	$ (89,432)
Increases (decreases) resulting from:			
State taxes, net of federal taxes	13,366	17,509	11,832
Change in valuation allowance	(6,578)	(158)	(4,727)
Flow through differences	2,918	2,731	2,780
Amortization of deferred investment tax credits	(1,433)	(1,534)	(1,510)
Subsidiary preferred dividends	714	716	799
Impairment charges	150,705	252,158	171,247
Other, net	809	(1,887)	(4,233)
Actual income tax expense	$121,418	$ 111,827	$ 86,756

The following table provides the components of the net deferred tax liability from continuing operations at December 31:

	2009	2008
Deferred tax assets:		
Advances and contributions	$ 568,422	$ 539,165
Deferred investment tax credits	12,417	12,973
Other postretirement benefits	100,936	102,371
Tax losses and credits	352,426	124,311
Pension benefits	147,904	187,498
Unamortized debt discount, net	24,100	26,718
Capital loss not utilized	—	6,165
Other	23,891	54,965
	1,230,096	1,054,166
Valuation allowance	(25,621)	(28,862)
	1,204,475	1,025,304
Deferred tax liabilities:		
Utility plant, principally due to depreciation differences	1,771,263	1,446,655
Income taxes recoverable through rates	76,697	76,159
Deferred security costs	4,144	5,358
Deferred business services project expenses	4,456	4,456
Deferred other postretirement benefits	53,152	51,145
Deferred pension benefits	77,924	88,768
Other	68,516	58,350
	2,056,152	1,730,891
	$ (851,677)	$ (705,587)

At December 31, 2009 and 2008, the Company recorded federal net operating loss (“NOL”) carryforwards of $1,123,938 and $239,654, respectively. The Company believes the federal NOL carryforwards are more likely than not to be recovered and require no valuation allowance. The Company evaluated its ability to fully utilize the existing federal NOL carryforwards in light of the RWE divestiture in November 2009. Under Internal Revenue Code (“I.R.C.”) Section 382, an ownership change occurs if there is a greater than fifty percent (50%) change in equity ownership of a company over a three year period determined by reference to the ownership of persons holding five percent (5%) or more of that company’s equity securities. If a company undergoes an ownership change as defined by I.R.C. Section 382, the company’s ability to utilize its pre-change NOL carryforwards to offset post-change income may be limited.

The Company believes that the limitation imposed by I.R.C. Section 382 generally should not preclude use of its federal NOL carryforwards, assuming the Company has sufficient taxable income in future carryforward periods to utilize those NOL carryforwards. The Company’s federal NOL carryforwards do not begin expiring until 2024.

At December 31, 2009 and 2008, the Company recorded state NOLs of $760,190 and $431,694, respectively, a portion of which are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The state NOL carryforwards began expiring in 2008.

At December 31, 2009 and 2008, the Company had Canadian NOL carryforwards of $13,033 and $17,528, respectively. The majority of these carryforwards are offset by a valuation allowance because the Company does not believe these NOLs are more likely than not to be realized. The Canadian NOL carryforwards began expiring in 2008.

At December 31, 2009 and 2008, the Company had capital loss carryforwards for federal income tax purposes of $16,282 and $17,614, respectively. The Company has recognized a full valuation allowance for the capital loss carryforwards because the Company does not believe these losses are more likely than not to be recovered.

The Company files income tax returns in the United States federal jurisdiction, and various state and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state or local or non-U.S income tax examinations by tax authorities for years before 2004.

The Company has state income tax examinations in progress and does not expect material adjustments to result.

In December 2008, the Company filed a request with the Internal Revenue Service ("IRS") to change its tax accounting method for repair and maintenance costs on its utility assets. The IRS partially approved the request in October 2009, allowing the Company to take a current deduction for costs that were previously capitalized for tax purposes. As a result, the Company recorded a deferred income tax liability for this temporary difference.

The following table summarizes the changes in the Company's gross liability, excluding interest and penalties, for unrecognized tax benefits:

Balance at January 1, 2008	$ 1,642
Decreases due lapse statute of limitations	(291)
Balance at December 31, 2008	1,351
Increases in prior period tax positions	88,248
Increases in current period tax positions	22,631
Decreases due to lapse of statute of limitations	(209)
Balance at December 31, 2009	$112,021

The liability balance as of December 31, 2009 and 2008 does not include interest and penalties of $439 and $312, respectively, which is recorded as a component of income tax expense. The majority of the increased tax position is attributable to temporary differences. The Company does not anticipate material changes to its unrecognized tax benefits within the next year. If the Company sustains all of its positions at December 31, 2009 and 2008, an unrecognized tax benefit of $7,785 and $1,104, respectively, excluding interest and penalties, would impact the Company's effective tax rate.

The following table summarizes the changes in the Company's valuation allowance:

Balance at January 1, 2008	$29,021
Increases in current period tax positions	2,369
Decreases in prior year tax positions	(2,528)
Balance at December 31, 2008	28,862
Increases in current period tax positions	2,778
Decreases in current period tax positions	(5,698)
Decreases in prior period tax positions	(321)
Balance at December 31, 2009	$25,621

Note 15: Employee Benefits

Pension and Other Postretirement Benefits

The Company maintains noncontributory defined benefit pension plans covering eligible non-union employees of its regulated utility and shared services operations. Benefits under the plans are based on the

employee's years of service and compensation. The pension plans have been closed for any employees hired on or after January 1, 2006. Union employees hired on or after January 1, 2001 had their accrued benefit frozen and will be able to receive this benefit as a lump sum upon termination or retirement. Union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006 are provided with a 5.25% of base pay defined contribution plan.

The Company's funding policy is to contribute at least the minimum amount required by the Employee Retirement Income Security Act of 1974. Pension plan assets are invested in a number of investments including equity and bond mutual funds, fixed income securities and guaranteed interest contracts with insurance companies.

Pension expense in excess of the amount contributed to the pension plans is deferred by certain regulated subsidiaries pending future recovery in rates charged for utility services as contributions are made to the plans. (See Note 7)

The Company also has several unfunded noncontributory supplemental non-qualified pension plans that provide additional retirement benefits to certain employees.

The Company maintains postretirement benefit plans providing varying levels of medical and life insurance to eligible retirees. The retiree welfare plans are closed for union employees hired on or after January 1, 2006. The plans had previously closed for non-union employees hired on or after January 1, 2002.

The Company's policy is to fund postretirement benefit costs accrued. Plan assets are invested in equity and bond mutual funds.

The obligations of the plans are dominated by obligations for active employees. Because the timing of expected benefit payments is so far in the future and the size of the plan assets are small relative to the Company's assets, the investment strategy is to allocate a large portion of assets to equities, which the Company believes will provide the highest return over the long-term period. The fixed income assets are invested in long duration debt securities in order to better match the duration of the plan liability.

The Company periodically conducts an asset liability modeling study to ensure the investment strategy is aligned with the profile of the obligations. The long-term goals are to maximize the plan funded status and minimize contributions and pension expense, while taking into account the potential volatility risks on each of these items.

None of the Company's securities are included in pension or other postretirement benefit plan assets.

The asset allocation for the Company's U.S. pension plan at December 31, 2009 and 2008 by asset category, are as follows:

	Target Allocation	Percentage of Plan Assets At December 31,	
Asset category	2009	2009	2008
Equity securities	70%	71%	70%
Fixed income	30%	29%	30%
Total	100%	100%	100%

The investment policy guidelines of the pension plan require that the fixed income portfolio has an overall weighted average credit rating of AA or better by Standard & Poor's and the minimum credit quality for fixed income securities must be BBB- or better. Up to 20% of the portfolio may be invested in collateralized mortgage obligations backed by the United States Government.

The fair values of pension plan assets at December 31, 2009, by asset category, follow:

Asset Category	Target Allocation 2010	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2008
Cash	—	$ 10,156	$ 10,156	$ —	$ —	—
Equity securities:						
U.S. large cap	36.0%	250,353	250,353	—	—	35.8%
U.S. mid-cap growth	12.0%	88,397	88,397	—	—	12.1%
International	22.0%	153,719	153,719	—	—	21.7%
Fixed income securities:	30.0%					30.4%
U.S. Treasury and government bonds	—	23,495	23,495	—	—	—
Corporate bonds	—	23,624	—	23,624	—	—
Mortgage-backed securities	—	89,736	—	89,736	—	—
Guaranteed annuity contracts	—	56,040	—	8,593	47,447	—
Total	100.0%	$695,520	$ 526,120	$121,953	$ 47,447	100.0%

The following table presents a reconciliation of the beginning and ending balances of the fair value measurements using significant unobservable inputs (Level 3):

	Guaranteed Annuity Contract
Balance, January 1, 2009	$ 42,386
Actual return on assets	9,959
Transfers in(out)	(4,898)
Balance, December 31, 2009	$ 47,447

The Company's other postretirement benefit plans are partially funded. The asset allocation for the Company's other postretirement benefit plans at December 31, 2009 and 2008, by asset category, are as follows:

Asset category	Target Allocation 2009	Percentage of Plan Assets At December 31, 2009	2008
Equity securities	70%	70%	70%
Fixed income	30%	30%	30%
Total	100%	100%	100%

The postretirement benefit plan assets are invested in a manner consistent with the pension plan investment policy.

The fair values of postretirement benefit plan assets at December 31, 2009, by asset category, follow:

Asset Category	Target Allocation 2010	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Percentage of Plan Assets at December 31, 2008
Cash	—	$ 2,459	$ 2,459	$ —	$ —	—
Equity securities:						
U.S. large cap	36.0%	108,703	108,703	—	—	34.2%
U.S. mid-cap growth	12.0%	40,575	40,575	—	—	12.2%
International	22.0%	70,111	70,111	—	—	24.2%
Fixed income securities:	30.0%					29.4%
U.S. Treasury securities	—	25,072	25,072	—	—	—
Corporate bonds	—	31,265	—	31,265	—	—
Mortgage-backed securities	—	33,857	—	33,857	—	—
Total	100.0%	$312,042	$ 246,920	$ 65,122	$ —	100.0%

Valuation Techniques Used to Determine Fair Value

Cash—Cash and investments with maturities of three months or less when purchased, including certain short-term fixed-income securities, are considered cash and are included in the recurring fair value measurements hierarchy as Level 1.

Equity securities—With respect to equity securities, the trustees obtain prices from pricing services, whose prices are obtained from direct feeds from market exchanges, which the Company is able to independently corroborate. Equity securities are valued based on quoted prices in active markets and categorized as Level 1.

Fixed-income securities—U.S. Treasury securities and government bonds have been categorized in Level 1 because they trade in highly-liquid and transparent markets that the Company can corroborate. The fair values of corporate bonds, mortgage backed securities and a certain guaranteed annuity contract are based on evaluated prices that reflect observable market information, such as actual trade information of similar securities and have been categorized as Level 2 because the valuations are calculated using models which utilize actively traded market data that the Company can corroborate. Certain other guaranteed annuity contracts are invested in a commingled fund and categorized as Level 3 because the investments are not publicly quoted. The fund administrator values the fund using the net asset value per fund share, derived from the quoted prices in active markets of the underlying securities. Since these valuation inputs are not highly observable, the commingled funds have been categorized as Level 3.

The following table provides a rollforward of the changes in the benefit obligation and plan assets for the most recent two years for all plans combined:

	Pension Benefits		Other Benefits	
	2009	2008	2009	2008
Change in benefit obligation				
Benefit obligation at January 1	$1,016,889	$ 916,994	$ 475,742	$ 451,944
Service cost	28,426	26,207	13,172	12,425
Interest cost	62,919	58,195	29,180	28,197
Plan participants' contributions	—	—	2,216	1,803
Amendments	1,600	850	—	—
Actuarial (gain) loss	53,135	46,988	50,357	2,426
Special termination benefits	—	—	—	—
Gross benefits paid	(34,807)	(32,345)	(24,297)	(22,669)
Federal subsidy	—	—	1,769	1,616
Benefit obligation at December 31	$1,128,162	$1,016,889	$ 548,139	$ 475,742
Change in Plan Assets				
Fair value of plan assets at January 1	$ 513,283	$ 626,272	$ 234,501	$ 293,392
Actual return on plan assets	131,252	(158,322)	57,968	(65,400)
Employer contributions	85,792	77,678	41,654	27,375
Plan participants' contributions	—	—	2,216	1,803
Benefits paid	(34,807)	(32,345)	(24,297)	(22,669)
Fair value of plan assets at December 31	$ 695,520	$ 513,283	$ 312,042	$ 234,501
Funded status at December 31	$ (432,642)	$ (503,606)	$(236,097)	$(241,241)
Amounts recognized in the balance sheet consist of:				
Current liability	$ (1,632)	$ (1,544)	$ (52)	$ (48)
Noncurrent liability	(431,010)	(502,062)	(236,045)	(241,193)
Net amount recognized	$ (432,642)	$ (503,606)	$(236,097)	$(241,241)

The following table provides the components of the Company's accumulated other comprehensive income and regulatory assets that have not been recognized as components of periodic benefit costs as of December 31.

	Pension Benefits		Other Benefits	
	2009	2008	2009	2008
Net actuarial loss (gain)	$275,188	$334,934	$145,780	$143,907
Prior service cost (credit)	3,140	1,722	(12,120)	(13,301)
Transition obligation (asset)	—	—	520	694
Net amount recognized	$278,328	$336,656	$134,180	$131,300
Regulatory assets	$166,441	$198,506	$134,180	$131,300
Accumulated other comprehensive income	111,887	138,150	—	—
	$278,328	$336,656	$134,180	$131,300

At December 31, 2009 and 2008, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with a projected obligation in excess of plan assets were as follows:

	Projected Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2009	2008
Projected benefit obligation	$ 1,128,000	$ 1,017,000
Fair value of plan assets	696,000	513,000

	Accumulated Benefit Obligation Exceeds the Fair Value of Plans' Assets	
	2009	2008
Accumulated benefit obligation	$ 993,000	$ 887,000
Fair value of plan assets	696,000	513,000

The accumulated postretirement benefit obligation exceeds plan assets for all of the Company's other postretirement benefit plans.

In August 2006, the Pension Protection Act ("PPA") was signed into law in the U.S. The PPA replaces the funding requirements for defined benefit pension plans by requiring that defined benefit plans contribute to 100% of the current liability funding target over seven years. Defined benefit plans with a funding status of less than 80% of the current liability are defined as being "at risk" and additional funding requirements and benefit restrictions may apply. The PPA was effective for the 2008 plan year with short-term phase-in provisions for both the funding target and at-risk determination. The Company's qualified defined benefit plan is currently funded above the at-risk threshold, and therefore the Company expects that the plans will not be subject to the "at risk" funding requirements of the PPA. The Company is proactively monitoring the plan's funded status and projected contributions under the new law to appropriately manage the potential impact on cash requirements.

Minimum funding requirements for the qualified defined benefit pension plan are determined by government regulations and not by accounting pronouncements. The Company plans to contribute at least amounts equal to the minimum required contributions in 2010 to the qualified pension plans. The Company plans to contribute its 2010 other postretirement benefit cost to its Voluntary Employee's Benefit Association Trust.

Information about the expected cash flows for the pension and postretirement benefit plans is as follows:

	Pension Benefits	Other Benefits
2010 expected employer contributions		
To plan trusts	$81,200	$38,719
To plan participants	1,632	52

The Company made 2010 contributions to fund pension benefits and other benefits of $12,900 and $9,680, respectively through February 2010.

The following table reflects the net benefits expected to be paid from the plan assets or the Company's assets:

	Pension Benefits	Other Benefits	
	Expected Benefit Payments	Expected Benefit Payments	Expected Federal Subsidy Payments
2010	$ 42,380	$ 22,598	$ 1,487
2011	46,711	25,834	1,629
2012	51,165	28,602	1,811
2013	55,963	31,600	1,992
2014	61,190	34,843	2,162
2015—2019	389,769	218,881	13,675

Because the above amounts are net benefits, plan participants' contributions have been excluded from the expected benefits.

Accounting for pensions and other postretirement benefits requires an extensive use of assumptions about the discount rate, expected return on plan assets, the rate of future compensation increases received by the Company's employees, mortality, turnover and medical costs. Each assumption is reviewed annually. The assumptions are selected to represent the average expected experience over time and may differ in any one year from actual experience due to changes in capital markets and the overall economy. These differences will impact the amount of pension and other postretirement benefit expense that the Company recognizes.

The significant assumptions related to the Company's pension and other postretirement benefit plans are as follows:

	Pension Benefits			Other Benefits		
	2009	2008	2007	2009	2008	2007
Weighted-average assumptions used to determine December 31 benefit obligations						
Discount rate	5.93%	6.12%	6.27%	5.82%	6.09%	6.20%
Rate of compensation increase	4.00%	4.00%	4.25%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 8.50% in 2010 to 5% in 2017+	graded from 8% in 2009 to 5% in 2015+	graded from 8% in 2008 to 5% in 2014+
Weighted-average assumptions used to determine net periodic cost						
Discount rate	6.12%	6.27%	5.90%	6.09%	6.20%	5.90%
Expected return on plan assets	7.90%	7.90%	8.00%	7.60%	7.75%	7.38%
Rate of compensation increase	4.00%	4.25%	4.25%	N/A	N/A	N/A
Medical trend	N/A	N/A	N/A	graded from 8% in 2009 to 5% in 2015+	graded from 8% in 2008 to 5% in 2014+	graded from 9% in 2007 to 5% in 2011+

N/A—Assumption is not applicable.

The discount rate assumption was determined for the pension and postretirement benefit plans independently. A yield curve was developed for a universe containing the majority of U.S.—issued Aa—graded corporate bonds, all of which were non callable (or callable with make-whole provisions). For each plan, the discount rate was developed as the level equivalent rate that would produce the same present value as that using spot rates aligned with the projected benefit payments.

The expected long-term rate of return on plan assets is based on historical and projected rates of return for current and planned asset classes in the plans' investment portfolios. Assumed projected rates of return for each

of the plans' projected asset classes were selected after analyzing historical experience and future expectations of the returns and volatility of the various asset classes. Based on the target asset allocation for each asset class, the overall expected rate of return for the portfolio was developed, adjusted for historical and expected experience of active portfolio management results compared to the benchmark returns and for the effect of expenses paid from plan assets. The Company's pension expense increases as the expected return on assets decreases.

Assumed health care cost trend rates have a significant effect on the amounts reported for the other postretirement benefit plans. The health care cost trend rate is based on historical rates and expected market conditions. A one -percentage -point change in assumed health care cost trend rates would have the following effects:

	One - Percentage- Point Increase	One - Percentage- Point Decrease
Effect on total of service and interest cost components	$ 6,265	$ (5,167)
Effect on other postretirement benefit obligation	$ 72,084	$ (60,025)

The following table provides the components of net periodic benefit costs for the years ended December 31:

	2009	2008	2007
Components of net periodic pension benefit cost			
Service cost	$ 28,426	$ 26,206	$ 25,611
Interest cost	62,919	58,195	53,288
Expected return on plan assets	(42,224)	(51,701)	(47,052)
Amortization of:			
Prior service cost (credit)	182	181	127
Actuarial (gain) loss	23,968	5	262
Periodic pension benefit cost	$ 73,271	$ 32,886	$ 32,236
Special termination pension benefit charge	—	—	93
Net periodic pension benefit cost	$ 73,271	$ 32,886	$ 32,329
Other changes in plan assets and benefit obligations recognized in other comprehensive income, net of tax			
Amortization of prior service credit (cost)	$ (46)	$ (26)	$ (36)
Current year actuarial (gain) loss	(9,981)	64,139	(924)
Amortization of actuarial gain (loss)	(5,994)	(1)	(72)
Total recognized in other comprehensive income	$(16,021)	$ 64,112	$ (1,032)
Total recognized in net periodic benefit cost and comprehensive income	$ 57,250	$ 96,998	$ 31,297
Components of net periodic other postretirement benefit cost			
Service cost	$ 13,172	$ 12,425	$ 12,683
Interest cost	29,180	28,197	25,383
Expected return on plan assets	(18,638)	(23,002)	(21,065)
Amortization of:			
Transition obligation (asset)	173	173	173
Prior service cost (credit)	(1,180)	(1,180)	(1,180)
Actuarial (gain) loss	9,155	810	—
Net periodic other postretirement benefit cost	$ 31,862	$ 17,423	$ 15,994

The Company's policy is to recognize curtailments when the total expected future service of plan participants is reduced by greater than 10% due to an event that results in terminations and/or retirements.

The estimated amounts that will be amortized from accumulated other comprehensive income and regulatory assets into net periodic benefit cost in 2010 are as follows:

	Pension Benefits	Other Benefits
Actuarial (gain) loss	$17,902	$ 8,159
Prior service cost (credit)	322	(1,180)
Transition obligation (asset)	—	173
Total	$18,224	$ 7,152

Savings Plans for Employees

The Company maintains 401(k) savings plans that allow employees to save for retirement on a tax-deferred basis. Employees can make contributions that are invested at their direction in one or more funds. The Company makes matching contributions based on a percentage of an employee's contribution, subject to certain limitations. Due to the Company's discontinuing new entrants into the defined benefit pension plan, on January 1, 2006 the Company began providing an additional 5.25% of base pay defined contribution benefit for union employees hired on or after January 1, 2001 and non-union employees hired on or after January 1, 2006. The Company expensed contributions to the plans totaling $8,082 for 2009, $7,789 for 2008, and $7,305 for 2007, respectively. All of the Company's contributions are invested in one or more funds at the direction of the employee.

Long-Term Incentive Plan

The Company participated in a RWE long-term incentive plan for executives ("RWE LTIP"). Under the RWE LTIP, Company employees were granted 120,004 performance shares of RWE common stock which vested over three years beginning January 1, 2005. Subject to the vesting provisions, the performance shares were payable in cash. The performance shares were accounted for as a liability. Participants received their awards in cash in 2008. No expense was recognized related to these shares during 2008 and no liability remained at December 31, 2008. For the year ended December 31, 2007, the Company recognized approximately $4,127 of share-based compensation expense related to the performance shares in operation and maintenance expense.

Retention Bonuses

The Company established a retention bonus program that was intended to retain employees in key leadership roles through the timely completion of the IPO. If a participant remained employed by the Company through March 31, 2008, the participant received a cash bonus based on a predetermined percentage of his or her base salary in effect on January 1, 2006, or his or her hire date, if he or she was hired after January 1, 2006. Participants received their awards in cash in 2008. For the years ended December 31, 2008 and 2007, the Company recognized approximately $455 and $2,498 respectively, of expense related to the retention bonuses in operation and maintenance expense.

Completion Bonuses

The Company offered a completion bonus to reward selected senior executives for their contributions to the IPO process. Each eligible executive was entitled to receive a cash bonus based on a predetermined percentage of his or her base salary in effect on December 31, 2007, or his or her hire date, if he or she was hired after January 1, 2006. Participants received their awards in cash in 2008. During 2009, the Company recognized income of $321 for reversal of a prior accrual that was not paid out. For the years ended December 31, 2008, and 2007, the Company recognized approximately $749 and $832, respectively, of expense related to the completion bonuses in operation and maintenance expense.

Note 16: Commitments and Contingencies

OMI/Thames Water Stockton, Inc. ("OMI/TW") is a 50/50 joint venture between a subsidiary of the Company and Operations Management International, Inc. ("OMI"). In February 2003, OMI/TW and the City of

Stockton, California (the "City") entered into a 20-year service contract for capital improvements and management services of water, wastewater and storm water utilities. By mutual agreement, OMI/TW and the City of Stockton terminated the contract effective February 29, 2008 (the "Termination Date"). Upon termination, responsibility for management and operation of the system was returned to the City. OMI/TW agreed to provide a limited twelve-month warranty relating to certain components of the facilities that OMI/TW constructed (the "WW39 Plant"), which expired on December 31, 2008. OMI/TW also agreed to correct any latent defects relating to significant deficiencies in the structural components of certain capital improvements discovered prior to November 15, 2009, if any. Additionally OMI/TW committed to pay for certain employee transition costs and assumed financial responsibility for regulatory fines levied through the Termination Date, if any, resulting from OMI/TW's failure to comply with applicable National Pollutant Discharge Elimination System permit requirements and/or incidents traced to design defects in the WW39 Plant. During 2007, the California State Water Resources Control Board (the "Board") issued a notice of violation and a corresponding Settlement Communication related to a discharge into an adjacent river. The City has reached a final settlement agreement with the Board related to the discharge. In connection with the final settlement agreement, OMI/TW has agreed to pay a civil penalty and monitoring costs of $425. Given the uncertainties related to resolving the remaining issues described above and financial settlement with OMI, the Company has a loss reserve of approximately $1,300 at December 31, 2009 and 2008, respectively.

The Company is also routinely involved in legal actions incident to the normal conduct of its business. At December 31, 2009, the Company has accrued approximately $3,100 as probable costs and it is reasonably possible that additional losses could range up to $22,000 for these matters. For certain matters, the Company is unable to estimate possible losses. The Company believes that damages or settlements, if any, recovered by plaintiffs in such claims or actions will not have a material adverse effect on the Company's results of operations, financial position or cash flows.

The Company enters into agreements for the provision of services to water and wastewater facilities for the United States military, municipalities and other customers. The Company's military services agreements expire between 2051 and 2060 and have remaining performance commitments as measured by estimated remaining contract revenue of $2,097,000 at December 31, 2009. The Company's Operations and Maintenance agreements with municipalities and other customers expire between 2010 and 2048 and have remaining performance commitments as measured by estimated remaining contract revenue of $1,305,000 at December 31, 2009. Some of the Company's long-term contracts to operate and maintain a municipality's, federal government's or other party's water or wastewater treatment and delivery facilities include responsibility for certain major maintenance for some of those facilities, in exchange for an annual fee. Unless specifically required to perform certain maintenance activities, the maintenance costs are recognized when the maintenance is performed.

Included in the military services performance commitment at December 31, 2009 are contracts the Company was awarded during September 2009 for operation and maintenance of the water and wastewater systems at military installations at Fort Belvoir, Virginia and Fort Meade, Maryland. According to the agreements, the awards of the contracts are estimated at approximately $288,000 and $650,000, respectively, over a 50-year period as measured by gross contract revenue subject to price re-determinations and customary federal contracting termination provisions. Federal contract price re-determination is a mechanism to periodically adjust the service fee in subsequent periods to reflect changes in contract obligations and market conditions.

Commitments have been made in connection with certain construction programs. The estimated capital expenditures required under legal and binding contractual obligations amounted to $139,519 at December 31, 2009.

The Company's regulated subsidiaries maintain agreements with other water purveyors for the purchase of water to supplement their water supply. The Company's subsidiaries purchased water expense under these types of agreements amounted to approximately $98,821, $95,739, and $92,403 during the years ended December 31, 2009, 2008, and 2007, respectively. The estimated annual commitment related to the minimum quantities of water purchased is expected to approximate $50,343 in 2010, $45,922 in 2011, $45,842 in 2012, $44,850 in 2013, $44,851 in 2014 and $509,317 thereafter.

Note 17: Net Loss per Common Share

Earnings per share is calculated using the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security. The Company has participating securities related to restricted stock units, granted under the Company's 2007 Omnibus Equity Compensation Plan, that earn dividend equivalents on an equal basis with common shares. In applying the two-class method, undistributed earnings are allocated to both common shares and participating securities. There were 21 participating securities that were not included in the basic net loss per common share calculation at December 31, 2009 because they were anti-dilutive. There were no participating securities for the years ended December 31, 2008 and 2007. The following is a reconciliation of the Company's net loss and weighted average common shares outstanding for calculating basic net loss per share:

	Years Ended December 31,		
	2009	2008	2007
Basic			
Loss from continuing operations	$(233,083)	$(562,421)	$(342,275)
Loss from discontinued operations	—	—	(551)
Net loss	(233,083)	(562,421)	(342,826)
Less: Distributed earnings to common shareholders (a)	137,597	64,055	—
Less: Distributed earnings to participating securities	—	—	—
Undistributed earnings	(370,680)	(626,476)	(342,826)
Undistributed earnings allocated to common shareholders (b)	(370,680)	(626,476)	(342,826)
Undistributed earnings allocated to participating securities	—	—	—
Total loss available to common shareholders, basic (a) + (b)	$(233,083)	$(562,421)	$(342,826)
Weighted average common shares outstanding, basic	168,164	159,967	160,000
Basic net loss per common share	$ (1.39)	$ (3.52)	$ (2.14)

Diluted net loss per common share is based on the weighted average number of common shares outstanding adjusted for the dilutive effect of common stock equivalents related to the restricted stock units, stock options, employee stock purchase plan and restricted stock. The dilutive effect of restricted stock units, stock options, the employee stock purchase plan, and restricted stock is calculated using the treasury stock method and expected proceeds on vesting of the restricted stock units and restricted stock, exercise of the stock options and purchases under the employee stock purchase plan. The following is a reconciliation of the Company's net loss and weighted average common shares outstanding for calculating diluted net loss per share:

	Years Ended December 31,		
	2009	2008	2007
Diluted			
Total loss available to common shareholders, basic	$(233,083)	$(562,421)	$(342,826)
Undistributed earnings allocated to participating securities	—	—	—
Total loss available to common shareholders, diluted	$(233,083)	$(562,421)	$(342,826)
Weighted average common shares outstanding, basic	168,164	159,967	160,000
Shares from stock-based compensation plans	—	—	—
Weighted average common shares outstanding, diluted	168,164	159,967	160,000
Diluted net loss per common share	$ (1.39)	$ (3.52)	$ (2.14)

Options to purchase 2,265 and 926 shares of the Company's common stock were excluded from the calculation of diluted common shares outstanding because they were anti-dilutive for the years ended December 31, 2009 and 2008, respectively. Additionally, 258 restricted stock units and 32 shares under the employee stock purchase plan at December 31, 2009 and 119 restricted stock units and 33 shares under the employee stock purchase plan at December 31, 2008 were excluded from the diluted net loss per share calculation because they were anti-dilutive. There were also 459 and 1,134 stock options and 144 and 148 restricted stock units which were excluded from the calculation of diluted common shares outstanding because certain performance conditions were not satisfied as of December 31, 2009 and 2008, respectively. The Company had no potentially dilutive shares for the year ended December 31, 2007.

Note 18: Fair Values of Financial Instruments

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments.

Current assets and current liabilities: The carrying amount reported in the Consolidated Balance Sheets for current assets and current liabilities, including revolving credit debt due to the short-term maturities and variable interest rates, approximates their fair values.

Preferred stock with mandatory redemption requirements and long-term debt: The fair values of preferred stock with mandatory redemption requirements and long-term debt are determined by a valuation model which is based on a conventional discounted cash flow methodology and utilizes assumptions of current market rates. As a majority of the Company's debts do not trade in active markets, the Company calculated a base yield curve using a risk-free rate (a US Treasury securities yield curve) plus a credit spread that is based on the following two factors: an average of the Company's own publicly-traded debt securities and the current market rates for US Utility BBB+ debt securities. The Company used these yield curve assumptions to derive a base yield and then adjusted the base yield for specific features of the debt securities of call features, coupon tax treatment and collateral.

The carrying amounts (including fair value adjustments previously recognized in acquisition purchase accounting) and fair values of the financial instruments at December 31 are as follows:

2009	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 24,164	$ 26,257
Long-term debt (excluding capital lease obligations)	5,336,351	5,633,384

2008	Carrying Amount	Fair Value
Preferred stocks with mandatory redemption requirements	$ 24,368	$ 23,887
Long-term debt (excluding capital lease obligations)	4,797,838	4,430,117

Fair Value Measurements

To increase consistency and comparability in fair value measurements, FASB guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels as follows:

- Level 1—quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access as of the reporting date. Financial assets and liabilities utilizing Level 1 inputs include active exchange-traded equity securities, exchange-based derivatives, mutual funds and money market funds.
- Level 2—inputs other than quoted prices included within level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data. Financial

assets and liabilities utilizing Level 2 inputs include fixed income securities, non-exchange-based derivatives, commingled investment funds not subject to purchase and sale restrictions and fair-value hedges.

- Level 3—unobservable inputs, such as internally-developed pricing models for the asset or liability due to little or no market activity for the asset or liability. Financial assets and liabilities utilizing Level 3 inputs include infrequently-traded non-exchange-based derivatives and commingled investment funds subject to purchase and sale restrictions.

Recurring Fair Value Measurements

The following table presents assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of December 31, 2009 and 2008, respectively:

	At Fair Value as of December 31, 2009			
Recurring Fair Value Measures	Level 1	Level 2	Level 3	Total
Assets:				
Restricted funds	$61,232	$ —	$ —	$61,232
Rabbi trust investments	—	2,551	—	2,551
Deposits	11,612	—	—	11,612
Total assets	72,844	2,551	—	75,395
Liabilities:				
Deferred compensation obligation	—	8,881	—	8,881
Total liabilities	—	8,881	—	8,881
Total net assets (liabilities)	$72,844	$(6,330)	$ —	$66,514

	At Fair Value as of December 31, 2008			
Recurring Fair Value Measures	Level 1	Level 2	Level 3	Total
Assets:				
Restricted funds	$11,053	$ —	$ —	$11,053
Rabbi trust investments	—	3,562	—	3,562
Deposits	10,958	—	—	10,958
Total assets	22,011	3,562	—	25,573
Liabilities:				
Deferred compensation obligation	—	7,741	—	7,741
Total liabilities	—	7,741	—	7,741
Total net assets (liabilities)	$22,011	$(4,179)	$ —	$17,832

Restricted funds—The Company's restricted funds primarily represent proceeds received from financings for the construction and capital improvement of facilities and from customers for future services under operations and maintenance projects. The proceeds of these financings are held in escrow until the designated expenditures are incurred. Restricted funds expected to be released within twelve months subsequent to year-end are classified as current.

Rabbi trust investments—The Company's rabbi trust investments consist primarily of fixed income investments from which supplemental executive retirement plan benefits are paid. The Company includes these assets in other long-term assets.

Deposits—Deposits includes escrow funds and certain other deposits held in trust. The Company includes cash deposits in other current assets.

Deferred compensation obligations—The Company's deferred compensation plans allow participants to defer certain cash compensation into notional investment accounts. The Company includes such plans in other long-term liabilities. The value of the Company's deferred compensation obligations is based on the market value of the participants' notional investment accounts. The notional investments are comprised primarily of mutual funds, which are based on observable market prices.

See Note 15 for the Company's fair value of qualified pension and postretirement welfare plans' assets.

Non-recurring Fair Value Measurements

As discussed in Note 8, the Company recognized goodwill impairment charges of $450,000, $750,000 and $509,345 for the years ended December 31, 2009, 2008 and 2007, respectively. The Company's goodwill valuation model includes significant unobservable inputs and falls within level 3 of the fair value hierarchy.

Note 19: Operating Leases

The Company has entered into operating leases involving certain facilities and equipment. Rental expenses under operating leases were $37,004 for 2009, $36,200 for 2008 and $34,946 for 2007. The operating leases for facilities will expire over the next 20 years and the operating leases for equipment will expire over the next five years. Certain operating leases have renewal options ranging from one to five years.

At December 31, 2009, the minimum annual future rental commitment under operating leases that have initial or remaining non-cancelable lease terms in excess of one year are $29,024 in 2010, $24,655 in 2011, $20,438 in 2012, $15,455 in 2013, $12,694 in 2014 and $107,000 thereafter.

The Company has a series of agreements with various public entities (the "Partners") to establish certain joint ventures, commonly referred to as "public-private partnerships." Under the public-private partnerships, the Company constructed utility plant, financed by the Company, and the Partners constructed utility plant (connected to the Company's property), financed by the Partners. The Company agreed to transfer and convey some of its real and personal property to the Partners in exchange for an equal principal amount of Industrial Development Bonds ("IDBs"), issued by the Partners under a state Industrial Development Bond and Commercial Development Act. The Company leased back the total facilities, including portions funded by both the Company and the Partners, under leases for a period of 40 years.

The leases related to the portion of the facilities funded by the Company have required payments from the Company to the Partners that approximate the payments required by the terms of the IDBs from the Partners to the Company (as the holder of the IDBs). As the ownership of the portion of the facilities constructed by the Company will revert back to the Company at the end of the lease, the Company has recorded these as capital leases. The lease obligation and the receivable of the principal amount of the IDBs are presented by the Company on a net basis. The carrying value of the facilities funded by the Company recognized as a capital lease asset was $160,259 and $160,997 at December 31, 2009 and 2008, respectively, which is presented within utility plant. The future payments under the lease obligation are equal to and offset by the payments receivable under the IDBs.

At December 31, 2009, the minimum annual future rental commitment under the operating leases for the portion of the facilities funded by the Partners that have initial or remaining non-cancelable lease terms in excess of one year included in the proceeding minimum annual rental commitments are $3,502 in 2010, $3,519 in 2011 through 2013, $3,518 in 2014, and $85,372 thereafter.

Note 20: Related Party Transactions

Interest expense on the Company's borrowings with RWE amounted to $0 in 2009 and 2008, and $26,797 in 2007, respectively.

TWILUX, an affiliate and wholly owned subsidiary of RWE, was the holder of $1,750,000 of the Company's preferred stock. Preferred dividends included in interest expense amounted to $0 in 2009 and 2008, and $74,569, in 2007, respectively. The preferred stock was redeemed in 2007 utilizing the proceeds from $1,750,000 in variable rate borrowings from RWE. The variable rate borrowings from RWE were subsequently redeemed with proceeds from the senior notes issuance. (See Note 11)

One of the Company's Directors is employed by an electrical utility that supplies electricity and electrical services to the Company's subsidiaries in Ohio, Pennsylvania, and New Jersey. The Company purchased, from various subsidiaries of this electrical utility, approximately $8,558 and $7,183 of such services in 2009 and 2008, respectively. This Director has announced his intended retirement from that electrical utility effective March 31, 2010.

Note 21: Discontinued Operations

In 2007, the Company completed the sale of its Residuals business for $9,660. There was no gain or loss recorded on the sale. Summarized results during 2007 of this business included operating revenues of $7,128, pre-tax loss of $636, and a tax benefit of $85, resulting in a loss from discontinued operations of $551. There were no assets or liabilities classified as discontinued operations in the accompanying Consolidated Balance Sheets at December 31, 2009 and 2008, respectively.

Note 22: Segment Information

The Company has two operating segments referred to as the Regulated Businesses and Non-Regulated Businesses segments. The Company's chief operating decision maker regularly reviews the operating results of the Regulated and Non-Regulated Businesses segments to assess segment performance and allocate resources. The evaluation of segment performance and the allocation of resources are based on several measures. The measure that is most consistent with that used by management is adjusted earnings before interest and income taxes from continuing operations ("Adjusted EBIT").

The Regulated Businesses segment includes the Company's 23 utility subsidiaries that provide water and wastewater services to customers in 20 U.S. states. With the exception of one company, each of these public utility subsidiaries is subject to regulation by public utility commissions and local governments. In addition to providing similar products and services and being subject to the public utility regulatory environment, each of the regulated subsidiaries has similar economic characteristics, production processes, types and classes of customers and water distribution or wastewater collection processes. Each of these companies is also subject to both federal and state regulation regarding the quality of water distributed and the discharge of wastewater residuals.

The Non-Regulated Businesses segment is comprised of non-regulated businesses that provide a broad range of non-regulated water and wastewater services and products including homeowner water and sewer line maintenance services, water and wastewater facility operations and maintenance services, granular carbon technologies and products for cleansing water and wastewater, wastewater residuals management services and water and wastewater facility engineering services.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see Note 2). The Regulated and Non-Regulated Businesses segment information includes intercompany costs that are allocated by American Water Works Service Company, Inc. and intercompany interest that is charged by AWCC, which are eliminated to reconcile to the consolidated results of operations. Inter-segment revenues, which are primarily recorded at cost plus mark-up that approximates current market prices, include carbon regeneration services and leased office space, furniture and equipment provided by the Company's non-regulated subsidiaries to its regulated subsidiaries. Other includes corporate costs that are not allocated to the Company's subsidiaries, eliminations of inter-segment transactions, fair value adjustments and

associated income and deductions related to the Acquisitions that have not been allocated to the segments for evaluation of segment performance and allocation of resource purposes. The adjustments related to the Acquisitions are reported in Other, as they are excluded from segment performance measures evaluated by management. The following table includes the Company's summarized segment information:

	As of or for the Year Ended December 31, 2009			
	Regulated	Non-Regulated	Other	Consolidated
Net operating revenues	$ 2,207,290	$257,710	$ (24,297)	$ 2,440,703
Depreciation and amortization	272,462	5,871	15,907	294,240
Impairment charge	—	—	450,000	450,000
Total operating expenses, net	1,617,815	238,072	411,207	2,267,094
Adjusted EBIT(1)	591,606	21,264		
Total assets	11,659,525	247,594	1,545,532	13,452,651
Capital expenditures	779,428	5,837	—	785,265

	As of or for the Year Ended December 31, 2008			
	Regulated	Non-Regulated	Other	Consolidated
Net operating revenues	$ 2,082,740	$272,186	$ (17,998)	$ 2,336,928
Depreciation and amortization	254,803	5,858	10,600	271,261
Impairment charge	—	—	750,000	750,000
Total operating expenses, net	1,554,731	248,425	720,668	2,523,824
Adjusted EBIT(1)	531,774	26,307		
Total assets	10,941,133	244,891	2,045,794	13,231,818
Capital expenditures	1,005,360	3,446	—	1,008,806

	As of or for the Year Ended December 31, 2007			
	Regulated	Non-Regulated	Other	Consolidated
Net operating revenues	$ 1,987,565	$242,678	$ (16,028)	$ 2,214,215
Depreciation and amortization	254,998	10,295	2,042	267,335
Impairment charge	—	—	509,345	509,345
Total operating expenses, net	1,490,794	225,600	482,692	2,199,086
Adjusted EBIT(1)	500,088	23,579		
Total assets	10,180,482	280,692	2,490,153	12,951,327
Capital expenditures	738,824	11,986	—	750,810

(1) Management evaluates the performance of its segments and allocates resources based on several factors, of which the primary measure is Adjusted EBIT. Adjusted EBIT does not represent cash flow for periods presented and should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a source of liquidity. Adjusted EBIT as defined by the Company may not be comparable with Adjusted EBIT as defined by other companies.

Table of Contents

The following table reconciles Adjusted EBIT, as defined by the Company, to loss from continuing operations before income taxes:

	For the Year Ended December 31, 2009		
	Regulated	Non-Regulated	Total Segments
Adjusted EBIT	$ 591,606	$21,264	$ 612,870
Add:			
Allowance for other funds used during construction	11,486	—	11,486
Allowance for borrowed funds used during construction	7,224	—	7,224
Less:			
Interest, net	(231,858)	3,005	(228,853)
Amortization of debt expense	(6,089)	—	(6,089)
Segments income from continuing operations before income taxes	$ 372,369	$24,269	396,638
Impairment charge			(450,000)
Interest, net			(67,692)
Other			9,389
Loss from continuing operations before income taxes			$ (111,665)

	For the Year Ended December 31, 2008		
	Regulated	Non-Regulated	Total Segments
Adjusted EBIT	$ 531,774	$26,307	$ 558,081
Add:			
Allowance for other funds used during construction	14,497	—	14,497
Allowance for borrowed funds used during construction	8,171	—	8,171
Less:			
Interest, net	(227,384)	2,958	(224,426)
Amortization of debt expense	(5,346)	—	(5,346)
Segments income from continuing operations before income taxes	$ 321,712	$29,265	350,977
Impairment charge			(750,000)
Interest, net			(60,729)
Other			9,158
Loss from continuing operations before income taxes			$ (450,594)

	For the Year Ended December 31, 2007		
	Regulated	Non-Regulated	Total Segments
Adjusted EBIT	$ 500,088	$23,579	$ 523,667
Add:			
Allowance for other funds used during construction	7,759	—	7,759
Allowance for borrowed funds used during construction	3,449	—	3,449
Less:			
Interest, net	(219,371)	(8,629)	(228,000)
Amortization of debt expense	(5,169)	—	(5,169)
Segments income from continuing operations before income taxes	$ 286,756	$14,950	301,706
Impairment charge			(509,345)
Interest, net			(55,165)
Other			7,285
Loss from continuing operations before income taxes			$ (255,519)

Note 23: Unaudited Quarterly Data

The following table sets forth certain supplemental unaudited consolidated quarterly financial data for each of the four quarters in the period ended December 31, 2009 and 2008, respectively. The operating results for any quarter are not indicative of results that may be expected for a full year or any future periods.

2009	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in thousands, except per share data)			
Operating revenues	$ 550,170	$612,740	$679,956	$597,837
Operating income (loss)	(335,370)	157,192	214,406	137,381
Income (loss) from continuing operations	(413,079)	51,989	91,636	36,371
Net income (loss)	(413,079)	51,989	91,636	36,371
Basic and diluted earnings (loss) per common share	$ (2.58)	$ 0.32	$ 0.52	$ 0.21

2008	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in thousands, except per share data)			
Operating revenues	$ 506,815	$589,369	$672,193	$568,551
Operating income (loss)	(670,358)	142,658	211,754	129,050
Income (loss) from continuing operations	(732,484)	45,498	88,158	36,407
Net income (loss)	(732,484)	45,498	88,158	36,407
Basic and diluted earnings (loss) per common share	$ (4.58)	$ 0.28	$ 0.55	$ 0.23

Amounts may not sum due to rounding; per share amounts may not sum due to changes in shares outstanding during the year.

Income (loss) from continuing operations includes impairment losses of $450,000 and $750,000 in the first quarters of 2009 and 2008, respectively.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

American Water Works Company, Inc. maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in its reports filed or submitted under the Securities Exchange Act of 1934 (“the Exchange Act”) is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosure.

Our management, including the Chief Executive Officer and the Chief Financial Officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) of the Exchange Act) as of December 31, 2009 pursuant to 15d-15(e) under the Exchange Act.

Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2009, our disclosure controls and procedures were effective at a reasonable level of assurance. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms.